THE “LABOUR MARKET STUDIES” PROJECT OF THE EUROPEAN STRUCTURAL FUND NATIONAL PROGRAMME “LABOUR MARKET STUDIES OF THE MINISTRY OF WELFARE”

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WAGES AND IMPACTING FACTORS

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The “Labour Market Studies” project of the European Structural Fund national programme “Labour Market Studies of the Ministry of Welfare” No. VPD1/ESF/NVA/04/NP/3.1.5.1./0001/0003 research “Wages and Impacting Factors” (WIF) was conducted by partnership “RS Group” which includes foundation “Baltic Institute of Social Sciences” and “FACTUM” as well as external experts under Dr.soc. B.Zepa leadership. The WIF research is co-financed by European Union.

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The quantitative employees’ and employers’ surveys were conducted “Sociolōģisko pētījumu institūts”, Ltd..

Within the framework of the WIF research, the influence of individuals and characteristic factors of their workplace on the wage were analyzed, describing the structure of wages and form of its payment. For this purpose, study of opinions of employees and employers was performed using both, qualitative and quantitative methods of data collection. Wages in Latvia are mainly characterized by fixed basic wage that is complemented by different additional payments and non-financial remuneration (health insurance, participation in seminars, trips sponsored by the workplace, etc.) to favour work efficiency. The specific weight of financial and non-financial addition payments differ among companies depending on its size and individual qualities of employees. The higher is the education of an employee and to the more qualified group of occupation he/she belongs, the higher is the wage and the greater is the offer of additional payments.

Key words: labour income, earnings, financial and non-financial remuneration
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LIST OF ABBREVIATIONS

CSB – Central Statistical Bureau of Republic of Latvia

CSP LFS – Labour Force Survey conducted by Central Statistical Bureau of Republic of Latvia

EU – European Union

FTUCL – Free Trade Union Confederation of Latvia (Latvijas Brīvo arodbiedrību savienība, LBAS)

ECL – Employers’ confederation of Latvia (Latvijas Darba devēju konfederācija, LDDK)

ME – Ministry of Economics of Republic of Latvia

MF – Ministry of Finance of Republic of Latvia

MW – Ministry of Welfare of Republic of Latvia

NACE Classifier – General Industrial Classification of Economic Activities (NACE Rev. 1.1) for breakdown by kind of economical activities

SRS – State Revenue Service

WIF – the “Labour Market Studies” project of the European Structural Fund national programme “Labour Market Studies of the Ministry of Welfare” No. VPD1/ESF/NVA/04/NP/3.1.5.1./0001/0003 research “Wages and Impacting Factors”
DEFINITIONS OF TERMS

Employee is worker or individual who do some work for pay or profit under the guidance of employer.

Wage is each month payment for a work of employee which stated as fixed or variable (basic) wage.

Salary is regular compensation of an employee, monetary (financial) remuneration for a work, which includes wage and additional payments and bonuses (premiums) fixed in a collective agreement or labour agreement as well as other compensations on labour.

Non-monetary remuneration is non-financial compensation of work provided by employer which could be assigned in form of items and services etc.

Complementary benefits of wage are non-monetary remuneration provided employer for a worker as well as irregular premiums and payments for a work.

Minimum wage is the minimum level of legal monthly gross wage for full time employee according to Article 61 of the Labour Law. The amount of minimum wage is stated by Cabinet of Ministers.

Untaxed minimum is the minimum level of tax-exempted income according to the Law on Personal Income Tax Articles 3 and 12. The amount of untaxed minimum is stated by Cabinet of Ministers.
INTRODUCTION

Research “Wages and Impacting Factors” (WIF) is a part of the “Labour Market Studies” project of the European Structural Fund national programme “Labour Market Studies of the Ministry of Welfare”. General objective of the research is to establish reasonable and effective analytical base for decision making for facilitate employment growth and formation of inclusive labour market. The implementation of WIF research occurred between July 26, 2005 and September 25, 2006.

The definite objective of the WIF research is to give complete and adequate perception of Latvian wage system and to provide some suggestions for its improvements. It requires estimation of regularity of the wage fixing mechanisms. The objective foresees the analysis of both aspects: an impact of state regulation limitations and social and psychological interaction between employees and employers as individuals happening during the negotiating stage when parties agree on payment issues.

According to the project objectives, the following research tasks should be fulfilled:

- To evaluate existing differences of labour income on individual (or personal) level: to determine associations between labour payment and some characteristics of employee – education, age, experience, history of person’s career, as well as other factors identifying the level of influence for each factor and separating it from any impact of other factors (ceteris paribus);
- To evaluate existing differences of labour income on a company (or enterprise) level: to determine associations between labour payment in an enterprise and kind of economic activity, ownership, size, age, region and efficiency;
- To analyze the amount of existing additional benefits or bonuses besides the wage (premiums, award, and other non-financial remuneration) from the total worker’s compensation and their impacting factors.

According to the project objectives, the following tasks of policy analysis should be fulfilled:

- To evaluate the increase of minimal wage as regulating factor of labour payment system;
- To examine the influence of the rise of minimal wage to a growth of wages in Latvia, the decrease of wage gap between qualified and low-qualified labour force and growth of employment;
- To describe information flow and to develop recommendations for improving of statistical data collection and effectiveness of information flow;
- To make recommendations on changes in the existing legislation, as well as other further arrangements for enabling improvements of wage system in Latvia.

Prior to establishment of the project of the European Structural Fund national programme “Labour Market Studies of the Ministry of Welfare”, studies on different issues of labour market were implemented both by order of ministries and within framework of local and international projects; however, this work was done in insufficient amount due to limited funding. In issues of earnings, secondary data provided by Central Statistical Bureau (for instance, Labour Force and Occupational survey) was analysed. Within this analysis, legal salary was investigated and associations between earnings and parameters of individuals (age,
education, occupation) were analysed. WIF research proposes wider view on labour remuneration in Latvia examining it in both macro (national) and micro (individual) level.

The results of WIF research broaden competence of state institutions, social partners and society in general on remuneration structure and workers compensation forms in Latvia. The influence of some wage impacting factors observed into previous studies has been clarified or improved. Opinions of employees and employers gathered within qualitative studies on legislation and wage regulation issues refine data analysis. It is feedback to state institutions when implementing functions of state administration. WIF research should be considered as a project of policy analysis as well because the field policy alternatives had been evaluated within the framework of the study.
MAIN CONCLUSIONS AND RECOMMENDATIONS

The results of the WIF research show that in the majority of cases employees receive a fixed basic wage, and the variable basic wage that depends on the efficiency of work is a comparatively popular remuneration form as well. It may supplement or replace completely the fixed basic wage.

Payment of a fixed basic wage or variable basic wage depends on the qualification of an employee and the size of an enterprise. The higher the qualification is, the bigger the chance is that an employee will receive a fixed wage rather than a variable basic wage. In micro enterprises and a part of small enterprises (up to 10 employees), the position of which in the labour market is less stable, the fixed basic wage is paid less rarely.

Application of the system of individual work motivation (additional payment for individual results) or common collective work motivation (additional payment for enterprise results) is characteristic in the enterprises in Latvia. Additional payments for results of a team or a department are not so widespread. Although additional payments for results of a team or a department do not exist because of objective reasons, i.e. small numbers of employees, these additional payments neither are characteristic for medium and large enterprises.

When favouring wages in accordance with the efficiency of the work, it is advisable for the Ministry of Welfare to popularize the application of variable basic wages, hourly pay and additional payments for the efficiency of work in the enterprises of Latvia.

In addition to the basic wage and different additional payments, about a half or employees receive non-financial remuneration. These are mainly the following forms of remuneration: health insurance policy, presents of an enterprise for employees, training courses, education of participation in seminars, compensation of mobile phone communication, transport and feeding as well as different forms of support. The higher the post of an employee is, the more various forms of non-financial remuneration are available for him/her.

One of the most important contributory factors that favour the wage is education of an employee. It influence can be felt directly and indirectly. The direct effect is: the higher education of an employee is, the higher wage he/she has. The indirect effect is: employees having higher education occupy more frequently higher positions and work in better remunerated professions.

The highest point of labour income in all levels of education in Latvia is attained at a comparatively early age – at 30 to 35 in average. The data of the WIF research show that the age when an employee has the highest incomes has not changed during the last years and it still is far away form the average indicator of the states of the EU.

Considering the other factors that influence the wage, the importance of the ethnicity factor is mentioned in research. Results of the WIF research show that the differences between wages among representatives of various ethnicities can be explained by language skills rather than by their nationality. These are the language skills that create the segregation of occupations – employees with lower level of language skills are concentrated in professions that do not
require the any language skills. Although there differences do not exclude cases of
discrimination, it may be assumed that the employees are not discriminated as to their
ethnicity, and the differences in wage originate from the lack of Latvian language skills which
is a factor describing productivity.

To describe in details this regularity, it is advisable for the Central Statistical Bureau to
include the question on the Latvian language skills of employees in the Labour Force Survey.
Taking into consideration the necessity of foreign language skills, one should also study the
level of skills of the English language, the Russian and other foreign languages and their
influence on the wage.

The main factors that influence the wage within an enterprise are the size of an enterprise,
kind of economic activity, sector (public or private), region and development indicators of an
enterprise.

The size of an enterprise affects positively the wage of employees within it. It has been
observed that in larger enterprises there are higher wages than in small enterprises. The
highest wage in Latvia is in the following fields: construction, energy and power supply,
finances as well as state administration and social insurance. These fields are followed by
transport and communications sphere and manufacturing. In the public sector, the wage is
lower than the wage in the private sector.

In general, the wage in the statistical regions of Riga and the Pieriga is considerably higher
than in other regions of Latvia. However, the difference the optimal minimum wage named by
employers of Riga and the Pieriga differ less form the answers than from the real variation in
the wages. The reason for this prudent evaluation might be activities of an enterprise not only
in Riga or the Pieriga where an enterprise is registered, but also in other regions of Latvia.

In the WIF research, a definite influence of economical development on the wage was
observed. In growing and developing enterprises the wage is higher than in case if it would
operate without changes of progress or it meets definite difficulties. If an enterprise grows and
develops or it operates without considerable changes, there is a smaller possibility that illegal
remuneration will be practiced. This means that the Ministry of Economics should continue
supervision of entrepreneurship environment in cooperation with other national institutions by
realizing the programme of environment favourable circumstances.

At the moment, the employers indicate that there is lack of labour force. Despite the common
view that the main cause is labour force drain because of the low wages, one can name three
main reasons for this phenomenon. The first is labour force drain to other countries of the
European Union, the second is lack of motivation amount the potential employees and
requirements that far too much exceed their skills, and third is – lack of interest about
occupations of definite fields. It is considered that the first two reasons create wage increase
that does not correspond to the efficiency of work. Moreover, there is also lack of labour force
in the fields there is a comparatively high remuneration (for example, construction and
manufacturing). It is advisable for the Ministry of Welfare to take part in informing the
society about the factors that influence the wage as well as creating of an understanding that,
in other countries of the EU, not only wages, but also the prices of everyday goods and public
facilities are higher.
When summarizing the above mentioned, we can see that education and higher qualification has a considerable impact on the wage of an employee in Latvia at the level of one individual. The size of an enterprise, its sector of activities and economical development influence the wage at the level of an enterprise. As the result of this, the minimum wage as the mechanism of wage control and untaxed minimum as the tool of tax burden reduction affect the most the wage of low-qualified employees especially in micro enterprises. In general, while fixing the minimum wage, the state is trying to hit two targets. The first target is to guarantee the possibility for employer people to receive the necessary resources for subsistence within the framework of full working hours. The second target is to reduce spread of illegal remuneration. Both these targets are interrelated processes as to their realization. Along with the rise in the prices and change in the national economic development and aims of social policy, it is necessary to look though the mechanisms of the minimum wage fixation.

Evaluating the rate of the minimum wage and the most appropriate algorithm for its rise from 2010 to 2020, it is advisable for the Ministry of Welfare to define the proportion of the minimum wage as to the national average earnings. In the Concept Paper on the Minimum Wage, the target that the minimum wage should reach 50% from the national average earnings is set. It was estimated in the study that the possibilities of fulfilling this aim are rather low, but the realization of it could be prolonged to 2020. The sustainable target to increase of the minimum wage to the level of 68% from the national average labour income that is defined in the Concept Paper on the Minimum Wage should be reevaluated by the Ministry of Welfare taking into consideration the results of the WIF study and other research as well as experience of the European Union.

When analyzing the statutory minimum wage in the EU member states, one can see that its highest proportion as to the national average earnings is in Ireland (~50%). In other countries, the proportion of the minimum wage is lower (in the majority of cases it does not exceed 45%). If the average growth rate of the average wage in Latvia remains fast, the Ministry of Welfare can preserve the present proportion of the minimum wage as to the national average labour income, i.e. about 37%.

The main faults in the process of the minimum wage fixation at the national level are insufficient accessibility to the information. There is general information available that do not always characterize the labour market precisely. That is why it is difficult to evaluate what the impact of policy will be on less developed regions. In order to prevent the negative impact that may occur in this situation, it would be more preferable to favour agreement of labour unions and employers’ association on inadmissible limits of minimum wages or on differentiation of wages in the regions at the national level. As the WIF research shows, employers in less developed regions named the desirable minimum wage that is 20% lower than the employees in more developed regions (Riga and Pieriga) did.

Although in the member states of the European Union, where the minimum wage is fixed in collective agreements, there also are differences in wages between the kinds of economic activity, but there are no such practice in the countries where the statutory minimum wage is defined. Evaluating possibilities of minimum wage differentiation in Latvia, a particular attention is paid to the spheres of national economy that are subjected the most to the risk of undeclared employment (construction, retail trade, forest exploitation and wood-processing). Although wage differentiation in the fields of construction, retail trade, forest exploitation and wood-processing is possible, at the moment there exist several obstacles for implementation of this political alternative. They are: difficulties of enterprise identification of the field,
growth of administrative expenses of control institutions, choice of calculation methodology of differentiated wage and occurrence of different negative impacts while realizing this approach. As the results of the WIF research show, construction at the moment is one of the best remunerated fields of national economy and there is no reason to suppose that differentiation of the minimum wage is the most appropriate tool in reducing undeclared employment there.

Experience of the EU member states show that strengthening of employers’ associations and labour unions and conclusion of collective agreements that is applicable to the entire field of national economy is an alternative solution to the differentiated national minimum wage. The Labour Law of the Republic of Latvia also provides a similar case, but this may happen only when employers cover 60% of employees within the sector (Article 18 Part 4 of the Labour Law). Although there is a collective agreement concluded in some companies (mainly in large ones). It is hard to reach an agreement of the whole sector both, because of the passivity of employers and of employees.

When evaluating the possibilities of implementing the norms of the Labour Law on bargaining of a minimum wage that is provided by the collective agreement between an employer and an employee in all enterprises within the sector, there are two main preconditions. First of all, the Ministry of Welfare as the implementation of the national policy should be confident that concluding of general agreements is the aim to fulfil within a definite period of time. In the operative political documents the significance of the national minimum wage is accentuated, but there is no necessity of concluding agreements defined. Secondly, employers and employees should experience the need for motivation to join institutions of interest protection so that it became possible to conclude general agreements.

If the Ministry of Welfare will define that it supports conclusion of sector agreements where there are different minimum wages, the Ministry may apply different measures to favour practical application of the Article 18 of the Labour Law. It would be advisable is, first of all, to improve the basis of normative acts in order to stimulate employers and employees enter the organizations that protect their interests. Secondly, it is advisable to annul the force of the statutory minimum wage in large enterprises (above 500 employees) by charging them with the responsibility of concluding collective agreements with the labour union of their enterprise or the entire sector. Thirdly, it is proposed to reduce the requirement of the Article 18 part 4 of the Labour Law by reducing the 60% of employees being united to 50% or even 40%, and then, when organizations of employers and employees will be established, to restore gradually the proportion within an enterprise to the present level. Evaluating political priorities and indispensable resources for implementation of the above mentioned recommendations, thee government may continue to determine the statutory minimum wage as in the EU member states.
I THEORETICAL FRAMEWORK OF THE RESEARCH

1.1. Theoretical background of wage analysis

Wage as a social phenomenon may be viewed from various standpoints. On the one hand, it is payment for labour services (payment for application of person’s abilities and skills within certain period of time) that employer can afford within economic production process of goods. Wage level is determined by interaction between labour demand and supply. Labour demand depends on demand for products and services (general economic situation in the country) as well as labour capacity (productivity). Labour productivity depends on technologies, natural resources, labour quality, administration and organization (Ehrenberg, Smith 2003: 36-9). Thereby labour demand is simultaneously determined both by characteristic of individuals as certain human resources and technical resources and work organization of certain enterprise performed by director of enterprise (employer), as well as by macroeconomic ambience in the state. All listed components more or less are analysed within the framework of WIF research.

Labour supply depends on number of inhabitants in certain age groups, institutional ambience (legislation) and alternative sources of income, for instance, currently it is an opportunity to work abroad, level of pensions and allowances etc. (Ehrenberg, Smith 2003: 40-2).

Firstly, in competitive conditions wage level and used labour amount are determined by labour demand and supply. Secondly, wage is equal to marginal revenue product. It is value of one extra unit of product produced using one extra man-hour (or man-month etc.) in the given company (Ehrenberg, Smith 2003: 59-60). Thirdly, wage level derives from investment in human capital (education and health protection). That shows at both individual level (person who has invested in education gets higher wage) and enterprise level (depending on enterprise contributions in employee training). Fourthly, wage is affected by different political, institutional (legislation, activity of labour unions etc.), social and psychological factors (Sachs, Larrain 1993: 497; Ehrenberg, Smith 2003: 452). Fifthly, wage deviation from market level is determined by enterprise size, labour competition situation and human resources management strategy.

Thus, employees’ wage is related to their productivity, that is, employees get their wage in proportion to accomplished work. That results from basic principle of enterprise activity – profit maximization. Enterprise analyses its activity by searching for optimal disposition of resources and labour is one of available resources.

Marginal product of labour is rather a theoretical concept which is not always possible to estimate at enterprise level (Ehrenberg, Smith 2003: 67). Therefore, other indices are applied to determine wage – average productivity minus enterprise profit and costs.

Depending on education, experience and other features of employees, wage may be increased or reduced. Both employers and employees are interested to know the impact range of these affecting factors before making decision (to employers – about recruiting and wage determination, to employee – about readiness to work and determination of minimum wage
threshold necessary for him). Description of effect of education, experience and other features on wage is important source of information also to formers of state policy, as it allows to identify possible problems in conformity of wage and productivity, as well as to make decisions for forming future state policy in order to facilitate employment and welfare of employees.

Further on we will dwell on basic components of wage equation. One of the key variables is age of employee (Ehrenberg, Smith 2003: 276). It is used as general experience characterizing variable – irrespective of educational level, employees with age also gain work experience. Even if employee has changed his profession and place of employment, previously gained work experience gives extra productivity (the greater is experience, the higher is productivity and the higher value employee creates to employer), therefore, expected effect on wage is positive – wage should grow with age of employee.

However, wage has also contrary effect – by getting older employee’s productivity starts to decrease, as physical and mental working capacity declines (employee can not work as long and effectively as before and slower acquires new knowledge). That reduces effect of gathered experience; hence we can assume that employee’s age effect on wage can be characterized as a second order equation: employee's age in the first order reflects growth of general experience, but employee's age in the second order reflects ageing and decline of working capacity.

In addition to age, we will use as a wage determinant employment duration of employee in the particular enterprise which characterizes specific experience. It is experience specific to certain profession and/or certain enterprise. Although it does not describe all experience gathered by employee, it is considered that experience gathered in the certain enterprise gives additional impact on employee’s wage (Ehrenberg, Smith 2003: 371) – the longer employee works in place of employment, the better he adjusts to particular job responsibilities, as well as better amalgamates with other colleagues, as a result creating additional productivity. Particular situation develops also in present work place of work experience if the latter is below one year – during the first year employer often tests skills of employee and offers lower wage to hedge his losses.

Second most important component of wage equation is effect of employee’s educational level on wage (Ehrenberg, Smith 2003: 278). The main educational levels in Latvia are elementary education (mandatory educational level guaranteed by the state), general secondary education (people may choose not to acquire secondary education, yet it is financed from the national budget excluding private schools), secondary vocational education, industrial education after elementary education of vocational education after secondary education, as well as higher education which consists in several sublevels – first level higher vocational, academic higher education, postgraduate studies. Educational levels differ by extent of imparted knowledge and proficiency. Each of educational levels a little bit differently affects employee’s skills, hence it is estimated in wage equation what is the effect of theses levels on employee’s wage.

The effect of age and educational levels on employee’s wage is based on human capital model. Human capital model views employee’s desire to acquire certain educational level as contribution bringing benefit. Acquisition of education is related to expenses – tuition fee, expenses for necessary educational materials, unearned income (as during studies student or pupil can not work with full load), indirect costs of physical and mental effort (Ehrenberg, Smith 2003: 267). Student expects that higher educational level will increase his potential
income in future thus compensating its acquisition expenses, i.e., it is considered that acquisition of education will increase competency and productivity of employee to great enough extent in order that he gets higher wage in labour market. However, we should keep in mind that income of employees, firstly, depend on productivity and, secondly, not in all cases education gives growth of productivity which is great enough to compensate expenses. Productivity is related to competency of employee to perform work himself – factors peculiar to particular person, working capacity and attitude towards work.

Well-grounded question arises why employer who chooses employee should offer higher wage to employee with higher educational level, without knowing yet his real productivity. This aspect is related to so called signalling model stating that employer perceives education acquired by employee as a signal of productivity – the higher is educational level, the higher productivity it indicates to (Ehrenberg, Smith 2003: 291). Since employers compete in the market to recruit the most productive employees, initially they can not afford to offer too low wage because then their competitors might get the best employees. At the same time, employer can not afford to pay too high wage, for if employee has low productivity enterprise will suffer losses. Hence, educational level is perceived as productivity signal (signal may be not only educational level but also school, training program or country where education is acquired). Similarly, employees frequently perceive educational levels as signals, i.e., they decide to acquire educational level not in order to increase their working capability but to give a signal to employer about their potential productivity.

If quality control and standards of education system in the state are adequate, signalling model works effectively enough both from standpoint of employer and employee (Ehrenberg, Smith 2003: 296).

Next important factor in labour market is knowledge of official language as it is necessary to perform work. Situation of Latvia is unusual with a fact that there is large share of employees whose mother tongue is Russian and knowledge of Latvian for many of them is not at mother tongue level. This means that “value” of these employees in labour market is lower due to possible communication problems. However, such statement is not always fully well-grounded. In part of work places Russian as basic work language is used or employee does not work with customers or with documentation and therefore Latvian might not be decisive factor. However, the research team considered that knowledge of Latvian is important production factor and its effect on wage was estimated.

So far, in wage equation modelling and impact estimation only nationality of employee was considered, and results indicated that it has substantial effect on employee’s wage (Organisation for Economic Co-operation and Development [OECD] 2003: 11). However, from standpoint of theory, ethnical identity of employee has no causal relationship with productivity of individual as the latter depends on capability of each particular person and not on his ethnical or religious affiliation. In WIF research data on language knowledge level of employees were available. Although it was subjective valuation, now it is possible to verify additional assumptions that wage depends on language knowledge instead of nationality.

Factors observed so far are qualities of employed person that might characterize his productivity. However, wage is affected by many factors of institutional ambience or factors based on entrenched traditions of public life which are not related to employee’s productivity, for instance, gender, activity of labour union at employment place of employee or location of place of employment.
Gender inequality in current labour market research is a topical issue as female wages almost always are lower than male wages – both in research evaluating wage equations and comparative statistics female wages are lower than male wages and this difference can not be explained by productivity characterizing factors (Ehrenberg, Smith 2003: 379-80). Besides, previous research conducted in Latvia that were based mainly on data analysis of Central Statistical Bureau indicate that gender income inequality within period of 1997 – 2002 has increased – male wage has increased faster than female wage (Hazans 2005a:42).

One of the possible arguments why female wages are lower than male wages is female’s potential “leaving” from labour market to confinement leave, maternity leave and leave for child care (Ehrenberg, Smith 2003: 216-7). Due to children upbringing women more often than men work on part-time load, as well as along with accouchement work experience is interrupted which means that when returning back to labour market female’s experience is smaller that male’s; however, controlling for work experience and work hours, differences are still significant meaning that these factors are not the only ones affecting female wages. Therefore, also in this research when forming wage equation variable that characterizes gender of respondents is added in order to statistically verify the hypothesis that female wages at other factors remaining constant are lower than male wages.

Since economic development is not even in all national territory, variable characterizing regions should be included in the analysis. They allow to compare and estimate significance of wage differences as well as to identify most developed regions and cities. Such information is helpful to policy makers in order to decide on granting government support and increase of economic activity in national territory. Research have proved that regional differences in wage payment in Latvia grew within 1997 – 2002 years period (Hazans 2005a: 43) but declined within 2002 – 2005 years period (Hazans 2006).

As an alternative to region variables unemployment level in work region of employee can also be applied. Unemployment level also characterizes level of economic activity and indicates to discrepancies between labour market demand and supply – the higher is unemployment level, the larger is discrepancy. Higher unemployment level is also related to low wages. Lower productivity and lower wage asked by employees can be mentioned as main reasons. If there is low economic activity in certain region, average productivity also is lower; hence wages of employees should be lower as well. Higher unemployment also means that idle labour force is available, which means that employer can choose from larger group of potential employees. It also means that larger number of unemployed persons has to compete for working places, therefore job seekers can lower their claims for wage amount in order to increase their chance to get employed (Ehrenberg, Smith 2003: 512).

Wage of employees at other equal conditions depends also on kind of economic activity of place of employment (for instance, by NACE classifier) and occupation (group by Occupational classifier). Productivity differs in various sectors; hence, wages of employees also differ. Such analysis allows identifying sectors where wage is larger at equal employee’s qualification, region etc. conditions, which is very valuable information from standpoint of employee in order to plan his career. The same applies to groups of professions. Theoretical argument of wage difference created by professions and sectors of economic activity is related not only to differences in work productivity but also to compensatory wage differentials (Ehrenberg, Smith 2003: 233). This theory states that sectors and positions are mutually different, for instance, risk of getting injuries, degree of influence and state of health of employee, degree of responsibility etc.
In sectors with higher risk of getting injuries should also be paid higher wages in order to compensate risk to employees they undertake by working in particular sector. Similarly, to managers and senior specialists, whose functions are related to great responsibility and high level of mental strain, wages should be higher comparing to representatives of elementary occupations. As it is difficult to evaluate risk, stress, level of responsibility and other psycho-physiological features in terms of quantity and they practically can not be standardized for all sectors or occupations, it is not possible to use them in wage analysis. Therefore, risk and mental strain analysis is replaced by influence evaluation of sector and group of occupations.

As regards employment policy, public sector (state and municipal institutions, state and municipal enterprises, as well as nongovernmental organizations) has always differed from private sector. In private sector, each enterprise determines wages according to results of his economic activity, whereas in major part of public sector institutions and enterprises wage is planned within national or municipal budget, and it is relatively constant within the framework of annual budget. Public sector to a greater extent is obliged to follow standards determined in labour legislation, as well as to pay from wage all provided taxes, while in private sector more often various breaches are possible as it is not possible to register and control for them. Such difference in wage planning and determining may cause significant additional difference also in average wages.

Enterprise size is wage affecting factor for two reasons. Firstly, the larger the enterprise, the smaller average administration costs per employee. Second reason is production capacity of enterprise – the larger the enterprise, the larger work volume it can accomplish. Bulky works are better paid considering their volume and complexity level; hence, larger enterprises can accomplish larger operations. As a result it is expected that wage in middle and large enterprises might be higher than in small and micro enterprises (Ehrenberg, Smith 2003: 372-3).

Previously, it has already mentioned that wage is equal to marginal revenue product. However, it should admit that not always employer follows this regularity and he can determine so called efficiency wage. In this case, wage is raised above the marginal product in order to attract best specialists to his enterprise. In this way employer acts as long as his gain exceeds extra wage expenses (Ehrenberg, Smith 2003: 360-2).

In addition to that, employer may apply various employee motivation or productivity calculation schemes. Productivity calculation requires monitoring of employee’s work, i.e., supervision which not always is cost-effective and requires investing more expenses in administration of enterprise. Instead, it is more profitable to apply motivation schemes, by defining individual or collective targets. In this case, employer does not have to monitor employees as it is replaced by employee’s personal desire to reach better results (Ehrenberg, Smith 2003: 346-7).

Thus any analysis of wages and relevant factors from the perspective of the demand for labour must be based on an understanding that compensation is an important instrument in motivating employers, one that is in the hands of employers. That is because the motivation of an employee has a direct influence on the quality and productivity of the work that is done, and that, in turn, has much to do with the company’s economic progress.

Talking about remuneration forms, wages are reviewed from the perspective of several motivation-related theories. Employers choose various approaches in terms of motivating
their employees, and these choices depend on the sector in which the work is done, on the size of the company and its chances for development, and on a variety of other factors.

Theories of content motivation (authors Abraham Maslow and Frederick Herzberg) speak to the essence (content) of the needs of employees, but they say nothing about why employees choose specific activities in pursuit of their needs. Employers cannot have an effect on the content (internal motivations) of a specific individual’s needs, but they can have an impact on the steps that are taken (the process) when the individual seeks to satisfy his or her needs.

The cornerstone for event motivation theories is the set of reasons why employees decide to do specific things in order to satisfy their needs. Attention is focused on an evaluation of the individual’s level of satisfaction once the goals have been reached. There are several theories in this area, but the work of Lyman W. Porter (Porter, 1968) and Edward E. Lowler (Lowler, 1968) is most appropriate for our needs, because it covers elements from other event theories, as well. There are several key conclusions to be drawn from this model (Praude, Beļčikovs 2001, 357-8):

- the results which employees achieve depend on efforts, skills and abilities that are applied;
- the level of effort depends on compensation (a subjective consideration) and on the links between effort and compensation (existing, non-existing, partly existing);
- after work is done, there can be internal (satisfaction, self-confirmation, self-esteem) and/or external (wages, bonuses, nomination for a higher-ranking job) compensation;
- satisfaction is the result of internal and external forms of compensation;
- satisfaction has a reciprocal link to the behaviour of the individual in the future.

It should be noted here that the third of these conclusions (internal and external compensation) is in line with Herzberg’s motivation-hygiene (two factors) theory, which speaks to aspects which create satisfaction and those which prevent dissatisfaction with work. Herzberg has concluded that there are two categories of human needs and that they are nearly independent of one another, thus influencing work behaviour in different ways.

First, there are external factors, which Herzberg calls hygiene or maintenance factors. They’re called hygiene factors because they refer to the environment in which the person works, and they serve to satisfy basic needs. They are maintenance factors in that they cannot be preserved forever, and they cannot be fully satisfied, which means that they must constantly be maintained. According to Herzberg, hygiene factors can prevent an employee from being dissatisfied with his work, but they seldom cause satisfaction. Among hygiene factors, Herzberg lists such things as guarantees of job preservation, social status, the operations of the organisations, working conditions, relations with colleagues, and wages (Praude, Beļčikovs 2001: 347).

Second, there are internal factors, which Herzberg calls motivators. These are factors which effectively encourage people to do their very best in terms of activities and behaviours, motivating employees to do good work and helping to ensure job satisfaction. An absence of these factors, however, seldom causes dissatisfaction with one’s job (Praude, Beļčikovs 2001: 347). Among motivators, Herzberg lists achievements at work, recognition of same, the working process, the level of responsibility and both career and professional growth.

Social scientists who have worked with work motivation issues after both mentioned authors note that disadvantage of theory of F. Herzberg is lack of accent of individual factor in
motivation theory. One of the key findings of latest years is that hygiene factors just like motivators can be considered as motivation factors and they depend on needs of each particular employee (Praude, Beļčīkovs 2001, 349).

Model of Porter and Lowler allows employers to find a much greater variety of ways in which motivating their employees, but it is necessary to think about human behaviour to know why employers prefer internal or external forms of motivation. A study of the views and practices of employers suggests that under certain circumstances, organisations often make successful use of this model, and certain non-material forms of compensation (recognition, praise, promotion of individuals to higher-ranking positions) are a way of compensating for limited opportunities to enhance the material compensation (wages) which employees receive.

The main motivation for employers is to ensure the company’s profitability, economic progress and development. Employees are a resource, and wages have much to do with the returns which they provided. The theory of stimulating motivation can be applied in analysing salaries as an instrument of motivation and in analysing the types of compensation which employees receive. Similarly to event motivation theories, stimulating motivation theories look at human behaviour as the result of ideas drawn from previous experiences. Supporters of this theory feel that employees can be motivated only with special methods of compensation (or sanction) (Praude, Beļčīkovs 2001: 359).

Motivation, according to this theory, starts with stimuli which have to do with personal, organisational and external factors. The attitudes of employees’ vis-à-vis their work depend not only on existing needs, but also on their experience in satisfying needs. Organisations usually have four methods for stimulating employees – (1) positive methods (increasing salaries for those who do their work more effectively, thus promoting the organisation’s development, paying bonuses for the quality of work, etc.); (2) evasive methods (the employer avoids punishing an employee for activities that are inappropriate in the working environment – being late for work or disobeying disciplinary rules); (3) punitive methods (punishing employees who act improperly in the context of work – refusing a bonus, transferring the person to a lower-ranking job, etc.); and (4) methods of ignoring incorrect behaviour which is not directly related to the work that must be done – complaints, humiliating comments, etc. Each method has its own goal and its own form of use (Praude, Beļčīkovs 2001: 360-2).

The model of stimulating motivation, like other models that have been surveyed, allow us to analyse various systems of compensation at companies – systems which have an effect on wages and the way in which wage levels are determined.

Traditional forms of compensation are: (1) payment on the basis of specific hourly, weekly or monthly rates, or (2) wages that are fixed on the basis of the amount of time that is spent at work. There are also untraditional systems of wage-related stimulation: (1) compensation based on achievements or (2) participation in the distribution of profits. Wages on the basis of achievements mean differentiated bonuses for employees on the basis of the results of their work (Praude, Beļčīkovs 2001: 362). This system encourages employees to feel a greater sense of responsibility for the work that is done; it keeps the individual involved with a specific organisation. Employers say that they are interested in avoiding personnel turnover as much as possible, and this means that management must find ways of tying the employee to the organisation.
All of the aforementioned compensation systems are directly linked to the specification of wage levels. For instance, a company’s profits will be higher with the last of the mentioned compensation systems, and wages will be higher, as well. In choosing a system which helps to motivate employees, employers must think of human needs (again in line with the Maslow hierarchy), along with the expectations and motivations of the individual (for instance, by taking the event motivation theory into account). Only if both factors are considered can the employer successfully implement one or another compensation system.

The macroeconomic environment in Latvia is governed by government institutions which specify the legal framework within which dialogue between employees and employers takes place – reaching agreement on work conditions, the content of the work and the wages that are to be paid. At the practical level, observing or ignoring this legal framework can also be a component in the dialogue between employees and employers. Consequently, the framework of WIF study covers three parts to be involved – state, employers and employees.

If the three involved parties (the state, employers and employees) discuss the nature of their cooperation in public, we call it a social dialogue. In this dialogue all three parties have their own goals. Entrepreneurs (majority of employers) are interested to produce goods or offer services that enable them to earn maximum profit. Employees are interested to get remuneration for effort put in that would enable them to satisfy their individual needs. For instance, by using A. Maslow’s classification of needs (Omārova 1996: 105; Praude, Belčikovs 2001: 343), we can say that wage ensures means for physiologic (maintenance of life processes), existential (existence and physical and economic security), social (human contacts and attention) etc. needs.

The state in the social dialogue has two roles at the same time – it is a mediator between both subjects mentioned above (entrepreneurs and employees) and it is a provider of society development vision. The latter, society development vision is described and available to the public by intermediation of legislation and policy planning documents. Currently, when Latvia is a member of the European Union, labour legislation and several policy planning documents are harmonized not only with individual objectives of our state but also with development objectives set by the European Union.

Government support in the labour market is manifested first and foremost in the elaboration of legal frameworks for the satisfaction of physiological and security needs. The key principles are implemented through laws and regulations (labour laws, minimum wages, etc.). Institutions are set up to oversee the practical implementation of these principles in society (in Latvia, these are the State Labour Inspectorate, the State Employment Agency, etc.).

At the same time, however, it should be noted that the aforementioned activities in pursuit of social inclusion and legal protection involve not just positive, but also negative consequences. To a certain extent, the social life is limited. If various social groups have not arrived at the need to improve specific areas with the help of specific institutions and legislation (that was the reason why labour unions were established and labour laws were passed), and if the efforts of the state in this area are seen as inappropriate interference (social groups are not prepared to observe forced and formal norms, nor do they see how they could do so), then the result is a search for ways of reducing the pressures of the legislation.

If conflicts among the interests of various social groups replace government intervention over a longer period of time, then eventually this means that there is a need for specific models of
behaviour which initially are implemented in an informal way and in relation to the situation which prevails. The manifestations of such a self-regulatory mechanism have been noted in WIF research. Participants in focus group discussions (employees) said that over the last few years, employers have less often paid salaries under the table, preferring official wages instead. That has happened not because government institutions have been stricter in controlling companies and in punishing violators of the law more harshly, but rather because employers themselves have taken the relevant decisions when their companies have become more stable and employers have felt more secure about their ability to observe the law. The situation illustrates the fact that employees, like other social groups, are not always accepting of such employer decisions if they feel that their interests (a higher salary) are under threat.

The most important we would like to say is that self-regulatory mechanisms of society function also as promoters of development and by restricting their expressions development may slow down. However, to our opinion, it does not mean the necessity to reject the institutionalization directed by the important supporting principle. It is more significant to be aware of consequences of particular action while evaluating state policy in the field of labour market and social issues. The result of each implemented policy is some benefits and some losses. Benefits and losses of various implemented policies are different. In this way, we would like to emphasize that the state legislation and administrative procedures should be concerted with most important aspects necessary for life of society, for instance, corresponding equilibrium between protection of labour market (guarantees to satisfy human basic needs) and the state economic development (strong labour legislation restricts flexibility of labour market) is to be chosen (OECD 2004: 62, 64).

Summarizing, social dialog on the national level includes two components – developed and implemented employment state policy, which is closely related to the relevant EU attitudes, as well as the dialog of social partners’ representatives and achieved social agreements. In order the social dialog would succeed, all three parties should be interested and represented in it.

Corresponding to main aspects of wage analysis discussed above, the review of the WIF research results moves further from the analysis of cooperation and decision making process on national level to the level of single employees.

1.2. Abstract of policy planning documents and legal acts

Abstract of policy planning documents and legal acts is divided into two parts. General policy planning documents from the sector are reviewed in the first part. They describe the overall development goals of the European Union and the resulting economic growth strategies of the Republic of Latvia – ones which have a direct or indirect effect on Latvian laws, amendments to those laws, and the policy alternatives which are to be drafted and assessed as a part of this research. Labour Law and specific policy planning documents within the context of WIF research are reviewed in the second part of the abstract. They define precise mechanisms whereby government institutions plan to take the steps that are defined in the general planning documents and guidelines with respect to enhancing employment levels and creating a more favourable environment for employment.
1.2.1. General field policy planning documents

Latvia’s employment policy goals and their pursuit are closely linked to European development programmes, but national specifics and interests are taken into account. The European Union’s development goals are defined in the Lisbon Strategy, which was approved by the Council of the European Union at its meeting on March 23-24, 2000. The Lisbon Strategy offers “a new strategic goal for the European Union is: (1) to enhance employment, economic reforms, and (2) social consolidation as a component of the knowledge-based economy” (European Commission [EC] 2000: 11). The document has been reviewed and updated several times, and at this point it is one of the most important policy planning documents upon which the EU’s policies are based. This has a direct and indirect effect on Latvia’s employment-related laws, strategies and plans, as well.

The primary aim of the strategy is to ensure economic growth so that by 2010, the EU can become “the most dynamic and competitive knowledge-based society in the world” (EC 2000: 11). The strategy contains little in the way of specific indicators that should be achieved, but it does state certain goals. In the area of employment, the aim is to increase the “level of employment from the average indicator of 61% (at this time) to as close to 70% as possible (in 2010), and to increase the number of women in employment from 51% to more than 60% (in 2010)” (EC 2000: 20). It is noted that the creation of more and better jobs is not just a political goal – it is an economic and social necessity. Because of significant demographic changes that are expected over the next 50 years and the resulting socio-economic consequences, it has been predicted that Europe’s pension and social insurance systems will face a very heavy burden, indeed, in the future. Improving the situation with employment, therefore, is one mechanism for reducing the forecast pressure of the demographic situation.

As the strategy was being implemented, there was an evaluation of reports filed by governments and institutions, and it was concluded that the results were fairly poor. Member states were not doing very well in implementing the reforms. This was because of economic problems, excessive work that had to be done, poor co-ordination and, in some cases, differing priorities. Important decisions have been taken with the aim of improving the situation. The European Commission has proposed that reforms be concentrated in two areas – more durable and more distinct growth, and the creation of high-quality jobs (European Commission 2004: 2).

The effectiveness of controlling the situation is ensured by virtue of the fact that each spring member states file reports on their progress, and then the European Commission issues an overall report. The basic pillars for the Lisbon Agenda at this time include knowledge and innovation in pursuit of growth, attracting investors and labour, and increasing the number and improving the quality of jobs that are available. In order to make Europe more attractive to investors and workers, obstacles that are created by the legislative systems of member states must be torn down – those which affect employment rates and regulate business operations.

When it comes to the employment-related aspects of the Lisbon Strategy, of key importance is the European Employment Strategy (EES), insofar as employment and labour market goals are concerned. The employment strategy was drafted in November 1997, the aim being to achieve significant progress in the battle against unemployment over the subsequent five
years. As a result of the relevant reforms, it was declared on April 8, 2003, that the emphasis would be on medium-term programmes and employment guidelines which contain policies that are aimed at pursuing the relevant goals. It was stated that the European Employment Strategy would also facilitate greater social cohesion. The employment guidelines have applied to the new EU member states since the moment of their accession to the EU in 2004. In 2004, the Council of the European Union issued recommendations on employment policies in the member states, in which it was stated that Latvia must bring greater numbers of people in to the labour market. In the context of this research, this could be done by ensuring that the system of the minimum wage, taxes and subsidies be as attractive as possible in terms of encouraging people to work in the formal economy (European Council 2004: 61).

These are goals which were declared as priorities in Latvia even before the country’s accession to the European Union. For instance, the establishment of a wage structure that is “friendly” to employment levels was one of Latvia’s priorities in the area of employment policy, one which required progress and oversight. These issues were addressed in a Joint Assessment Paper signed by the Latvian government and the European Commission on February 6, 2003. The Joint Assessment Paper made note of the importance of reforms in the wage structure of the public sector, and Latvia was told to monitor the effects of increasing the minimum wage very carefully (Latvian government, European Commission 2003: 24-5).

Latvia’s Development Plan (Single Programming Document): Objective 1st Programme, 2004-2006 (SPD) is a document that was drafted to focus on the introduction of the European Union’s first Framework Programme in relation to the Structural Funds between 2004 and 2006. The SPD says that Latvia’s growth depends on four major issues. In the context of this research, the most important issues include structural unemployment and regional differences. Medium-term goals in terms of resolving these problems include development of human resources, facilitation of competitiveness and employment, and development of the infrastructure. All of this is correlated with other planning documents, such as the National Development Plan and the positions which have been taken by the EU.

It is recognised in the document that there must be increases in wages in accordance with increased productivity, which is important in promoting higher employment rates and in enhancing Latvia’s international competitiveness. It is noted that between 1996 and 2001, average wages increased significantly in Latvia. The document also says that a concept on the minimum wage has been designed in pursuit of the relevant goals, with increases in the minimum wage up until 2010, reaching a level of 50% of the average wage in the national economy in the previous year. The document also identifies problems with gender inequality when it comes to wages. It points to horizontal segregation of genders – female are concentrated in poorly paid sectors of the economy (Ministry of Finances 2003: 47). It is also pointed out that major tax burdens create obstacles against the establishment of new jobs with moderate wages; it does not facilitate the hiring of unemployed people in terms of low-wage jobs. The personal income tax rate of 25% and the social insurance fees that must be paid (24.09% by employers, 9% by employees) – these facilitate the emergence of the “shadow economy”. The Central Statistical Bureau reports that in 2001, the “shadow economy” represented 17% of GDP. The Finance Ministry has said that in fact it may represent as much as 25% of GDP.

The aforementioned two documents – the Joint Assessment Paper signed by the Latvian government and the European Commission, as well as Latvia’s Development Plan (the Single Programming Document) – were the cornerstone for the preparation of a Latvian National
Action Plan to Promote Employment. This document correlated the main indicators of labour market development, and it proposed political initiatives aimed at expanding the level of employment. The plan was developed anew each year, and each year it was published. The Latvian National Action Plan to Promote Employment in 2005 was integrated in National Lisbon Programme of Latvia, which was written up under the supervision of the Ministry of Economics (Ministry of Economics 2005b:1).

National Lisbon Programme of Latvia is a “policy planning document which shows the way in which Latvia will achieve the goals of the Lisbon Strategy during the period between 2005 and 2008, doing so on the basis of the integrated basic positions approved by the Council in July 2005” (Ministry of Economics 2005a: 2). The aim is to preserve growth and to enhance employment. It has to be said that unlike the Lisbon Strategy, National Lisbon Programme of Latvia for 2005-2008 mostly speaks to ways of promoting employment, devoting far less attention to issues of social cohesion and the evaluation of this cohesion in terms of its actual existence. If Lisbon strategy has noticed both employment promotion (main document – European Employment Strategy) and social inclusion (main document – European Social Cohesion Strategy) as equally important, then National Lisbon Programme of Latvia examines three levels of policy moving forward from general to particular: policy of macroeconomics, reforms of microeconomics and guidelines of employment policy. The Programme does not include an equivalent chapter on social policy issues. Possible problems in implementing social inclusion policy (for instance, unresponsiveness of target groups) have not been analysed.

In pursuit of the goals of the Lisbon Strategy, the national programme defines five basic directions for economic policy. Two of these are directly related to the subject of this research – ensuring macroeconomic stability and promoting employment.

Among the tasks related to ensuring macroeconomic stability are: (1) upholding the Maastricht criteria, reducing the national budget deficit gradually; (2) introducing medium-term budget planning; (3) promoting higher wages and labour productivity so as to avoid additional instability in the national economy, simultaneously considering the effects of inflation; and (4) ensuring that Latvia can successfully join the Euro zone. This work is under threat in Latvia at this time, because comparatively high rates of inflation have had a deleterious effect on the business environment. The economy has become less competitive, and this may be an obstacle against Latvia’s plan to introduce the Euro in 2008. Currently, alternative of introduction the Euro later is examined yet. As acceptable period is mentioned time period between 2010 and 2013 years (Ministry of Economics 2005a: 8).

The main tasks in promoting employment are these: (1) promoting economic activities in poorly developed regions; and (2) reducing the level of undeclared employment. The latter of these attempts would make it possible to reduce the labour-related tax burden which, at this time, has a particularly negative effect on workers who receive low wages.

The programme cites political instruments which will facilitate higher wages, lower taxes for people with low income, and encouragement for people to join the official economy. These refer to increasing the minimum wage and the untaxed minimum. Increases in the minimal wage are defined in the Concept Paper on the Minimal Wage. Increases in the untaxed minimum are defined in a conceptual decision which the Cabinet of Ministers approved in 2004. Although the Concept Paper on the Minimum Wage says that this is the most important instrument in promoting higher wages, but the National Lisbon Programme does not make
note of the fact that increases in the minimum wage are already lagging behind the goals that are defined in the Concept Paper, which means that there is no evaluation of the risks that are related to the implementation of the conception. Neither is there any assessment of the extent to which goals that are defined in National Lisbon Programme of Latvia are mutually integrated.

Latvia’s inflation rate is above the Maastricht criteria at this time, and this may mean that there is a need for a more rapid increase in the minimum wage. During the implementation of currently planned and eventually necessary policy alternatives in pursuit of higher wages, the effect which these alternatives may have on the national budget must also be taken into account.

The wage system in the public sector which is in place at this time is indirectly linked to the government-specified minimum wage (that is, for instance, the case when it comes to the salaries of teachers). Rapid increases in the minimum wage would require additional financial resources. Should there be insufficient resources that would mean a higher budget deficit. An increase in the minimum wage can also encourage higher inflation in Latvia – a problem which is already dangerous in terms of the country’s other goals.

When we analyse the EU documents which are supposed to promote social cohesion and take a look at the plans which are in place to promote employment levels, we must talk about the modernisation of Europe’s social model. First, however, we must note that there are at least two different models for social assistance or welfare in Europe today.

The Nordic model of welfare is often seen as the one which would be desirable in Latvia, and it speaks to the provision of universal public services. This is sometimes known as the Social Democratic model, one which offers guarantees of equality. Extensive and nationally guaranteed social rights were, of course, a key element in the planned Soviet economy. Reforms of these principles were instituted very quickly in the early 1990s, and it was only later that a more carefully considered model of a social security system was put in place. This was promoted by the implementation of free market principles in the national economy and by the government’s shortage of resources.

A second possible model for welfare is that of a conservative and corporative state – one which seeks to preserve differences in status and supports traditional family structures (sometimes with the help of family support payments).

It could be argued that in pursuit of the Lisbon Strategy goal of becoming the most competitive economy in the world, the neo-liberal model of a welfare state might be the best one, given that it offers limited social assistance (Sjørup 2004: 143-144). This, however, would make it more difficult to achieve the other goal of the Lisbon Strategy – achieving social cohesion. That is because global competition among free market economies is a cause for a growing gap in society. On the other hand, the selection of a Nordic model of welfare or one that is similar to it would threaten the ability to achieve the first of the aforementioned goals.

The European Union’s goals of social cohesion are defined in the European Social Cohesion Strategy, which was approved in Lisbon in 2001 and reviewed in 2004. The document is quite general in content; it does not place an obligation on the shoulders of member states. There is a list of priorities and one which speaks to ways in which the strategy is to be pursued.
Certain normative acts and programmes at the national level make reference to this document, however, and so its main principles must be reviewed.

The strategy defines social cohesion as the ability of society to ensure welfare for all of its members, narrowing gaps and avoiding polarisation. A socially cohesive society is a community of people who offer support to one another, one that is made up of free individuals who use democratic methods to pursue the goals which they have in common. All societies have tensions which are created by the existence of social classes, but a socially cohesive society narrows these gaps in a democratic and transparent way, maintaining control and not allowing the gaps to threaten the stability of society. The strategy recognises that this goal cannot be achieved. There must be a ceaseless struggle in pursuit of social cohesion, and the process must be improved and adapted to malleable socio-economic, technological and political circumstances.

Latvia’s normative acts support the principles of the strategy, but there have been problems in implementing those principles. For instance, the existing social system cannot defend groups which are at risk of social exclusion, even though this goal, too, is stated in political documents. Financial limitations, moreover, are just one aspect of this situation. The state’s role in pursuing social cohesion is an activity which exists at the level of approving policies. There is, however, a very passive approach to implementing those policies. There is no consistency in defending human rights and democracy in Latvia, the social security system is not adequately linked to the system of taxation, and responsibility for social risk groups has largely been transferred from the state to the municipalities.

When it comes to policy documents, Latvia, like other former candidate countries of the EU, worked with the European Commission to prepare a pre-accession political document – Joint Memorandum on Social Inclusion of the Latvian Government and the European Commission. The aim was to “prepare the state for full participation through a method of open co-ordination when it comes to social cohesion issues at the moment of accession” (Ministry of Welfare 2003b: 1). The memorandum defines primary goals in reducing poverty and social alienation, it presents the political steps which Latvia must take on the basis of the agreement in terms of establishing government policies which are in line with the EU’s common goals, and it defines the main areas of politics in which monitoring and assessment of policies will continue.

Based on analysis conducted within the Memorandum, Latvian government and the European Commission reached agreement on the most urgent policy priorities in the fight against poverty and social alienation. The priorities speak to ensuring a minimally adequate income, the minimum wage, regular increases in state subsidy payments and pensions, as well as an increase in the amount of social assistance that is given by local governments to poor people.

On the basis of Joint Memorandum on Social Inclusion of the Latvian Government and the European Commission, the government adopted Latvian National Action Plan for Reduction of Poverty and Social Exclusion (2004-2006) – an instrument which is used in pursuit of the strategic goals that were defined by the European Council in Lisbon. There are two policy goals in the programme aimed at reducing poverty and social alienation which must be emphasised, because they correspond to the main goals of this project: (1) establishing an inclusive labour market and promoting employment levels; and (2) ensuring adequate income through wages, tax policies and social security systems (Ministry of Welfare 2004). In the context of wages, these plans have to do with instruments that are referred to in other policy
planning documents – the Concept Paper on the Minimum Wage and another on the untaxed minimum, for instance.

It must be noted that there are other areas (business, facilitating employment, gender equality, etc.) in which this is one of the few documents which makes reference to specific indicators that allow others to assess the achievements of the government’s policies. When it comes to increased wages, the conceptual document on the minimum wage must be seen as the most important indicator to have been defined so far in terms of the government’s actions and policies and in terms of their evaluation at a later point in time.

1.2.2. Labour Law and specific field policy planning documents

General regulations concerning relationships between employers and employees in Latvia are contained in the Labour Law (Saeima of the Republic of Latvia 2001) which Chapter 3 focuses on wages. Article 60 speaks to the principle of equal wages for male and female when they do the same work or work of equal value. Article 61 defines the concept of the minimum wage. In the context of WIF research, it must take into account all of the issues that are discussed in Chapter 3 of the Labour Law – wages, bonuses (for additional work, work under special circumstances, work at night, overtime), the cost of wages and the procedure for compensation for the expenditures of employees.

Experts say that Labour law of Latvia is comparatively strict when it comes to wages, particularly in terms of overtime. This, however, encourages companies to ignore the relevant norms of the law. It is also pointed out, however, that the strict social guarantees which are provided for in the law could be relaxed if wages in Latvia were higher. The comparatively low wage, in other words, is compensated with the employee’s security. There are limits on specifying the length of legal labour relations (for instance, a short job contract which is approved for a specific time for an employee) and on sacking employees.

Experts say that opportunities to regulate minimum wages in a specific part of the economy are referred to in Section B of the Labour law, which speaks to collective labour agreements. Article 17 of this section says that collective agreements can include agreements on how wages are paid. Article 18.4 says that if organisations of employers or organisations of employees employ more than 60% of employees in a specific sector, then a general agreement that is concluded between representatives of employers and the labour unions of employees is mandatory to all employers in the relevant sector, and it applies to all employees who are employed by those employers. This is a mechanism for regulating the wages of private sector employees in a certain sector of the economic activity without changing the national minimum wage. Representatives of employer and employee organisations in a specific sector agree on the minimum wage in their sector, and it can be higher than the national minimum wage.

When stimulating implementation of Article 18 of Labour Law in practice, there are two risks. First of all, the vast majority of companies in Latvia are micro, small and medium-sized companies, and organisations of employers and employees do not cover a majority of employees at such firms. That means that a general agreement is very hard to conclude. Second, major regional differences could reduce the competitiveness and perhaps even cause
the insolvency of certain companies (particularly small ones) if the minimum wage in a specific sector of the economy was to be raised on the basis of Article 18 of the Law. If large companies agree on an increased minimum wage in the country’s better-developed regions, then the decision is mandatory for the entire sector, and that means that a similar wage hike at a smaller company in a less-developed region of Latvia might mean an end to business operations.

The Concept Paper on the Minimum Wage, which was drafted by the Ministry of Welfare and accepted by the Cabinet of Ministers via Instruction No. 356 (28 May 2003) is the only planning document with specific government recommendations on how to encourage higher wages in Latvia by applying the instruments of politics to this purpose.

The aim of the Concept Paper is to define basic principles for setting minimum monthly gross wages in accordance with which those who have full time work would receive a minimum wage which underpins at least minimum standards of living in accordance with economic situation of Latvia, thus also guaranteeing the ability of employers to plan changes in the minimum monthly wage in a timely way (Ministry of Welfare [MW] 2003a: 1).

The minimum wage in Latvia is specified through Cabinet of Ministers regulations. In drafting the aforementioned conception, a working group at the Ministry of Welfare analysed the principles for setting the minimum wage in other European Union member states. Calculations were provided as to the effect of increasing the minimum wage on the national budget (in terms of tax income and expenditures related to wages in the public sector).

The Concept Paper says that most workers who are paid the minimum wage work in the private sector (MW 2003a: 7), so an increase in the minimum wage is of key importance in regulating wages in that sector.

The Concept Paper on the minimum wage also says that theoretically, an increase in the minimum wage could lead to higher unemployment in those parts of Latvia where wages are at the level of the minimum wage. The Central Statistical Bureau, however, has produced Labour Force Survey data which disprove this idea – in the relevant regions, unemployment has not increased. This means that a more detailed study of the situation is necessary.

It has been noted that an increase in the minimum wage is of the greatest effect among those employees who receive the minimum wage, because employers are forced to observe the law and to increase that wage. At the same time, however, this means higher wage costs for the employer, and this can facilitate increased unemployment. Still, studies show that employees in the private sector receive under-the-table (“envelope wage”) payments in addition to their officially declared salaries, and so wage costs will not increase at the same pace as the minimum wage (MW 2003a: 7). In drafting the conception, all of the aforementioned considerations encouraged the assumption that an increase in the minimum wage would not have much of an effect on unemployment levels.

According to the Concept Paper, a systematic increase in the minimum wage will increase the competitiveness of those companies which pay taxes on their entire wage fund, as compared to those who pay taxes on the minimum wage and provide the rest of employee salaries under the table (MW 2003a: 9). An increase in the minimum wage should legalise larger components of wages with respect to which taxes are paid.
Experts say, however, that those employers who, for one reason or another, do not want to increase wages to the minimum level specified by the state have found a different solution. They sign a job contract with the employee on part-time work (4 or 5 hours per day, for instance), which means that the person actually works full time, but the employer still pays the employer less. If the minimum wage is increased without careful consideration, therefore, that could influence, to some degree, the level of unregistered employment or being self-employed in Latvia.

Because the Concept Paper on the minimum wage speaks only to the importance of increasing the minimum wage and devotes less attention to the untaxed minimum, it has been actively criticised in the mass media over the last several years, the claim being that an increase in the minimum wage could have a negative effect on the competitiveness of Latvian companies and that for this reason, the minimum wage and the untaxed minimum should be increased simultaneously. The media claim that the latter of these is more important in terms of improving the purchasing power of population of Latvia (Ķirsons 2005: 3).

Several overall policy planning documents (such as National Lisbon Programme of Latvia for 2005-2008) make reference to the aims that are stated in the aforementioned Concept Paper – gradually increasing the minimum wage through the year 2010. For instance, on the basis of the concept of increasing the minimum wage through 2010, the Cabinet of Minister in 2004 approved a conceptual decision on a gradual increase in the untaxed minimum to LVL 60 in 2009 and LVL 70 in 2010 (Ministry of Economic 2005a: 55) or 50% of the minimum wage.

The Ministry of Finance has developed a statistical model on how income from the personal income tax would change if there were changes in the minimum wage and untaxed minimum, taking into account the number of taxpayers at the time when the government took this decision. When untaxed minimum increases, personal income tax revenue decreases. Forecast revenue from the personal income tax at this time corresponds to actual income very well, with actual revenue sometimes exceeding predictions. It can be assumed, therefore, that there are changes to increase the untaxed minimum more rapidly, but there would also have to be thought given to other factors which might have an influence – the possibility of increased productivity, for instance.

In general, the purpose of the statutory minimum wage is to guarantee a decent floor of remuneration to all working people (Sachs, Larrain 1993: 497). Depending on state, the definition of “decent floor” differs. It can include the necessity to provide for means of subsistence of one person or one person and one depended person. Similarly, depending on state, the content of “subsistence basket” differs. Generally speaking, specification of the minimum wage can be based on several principles or definitions. According to ideas persisted in public sphere, the minimum wage can be:

1. 50% of the average gross wages of working people in the previous year as it is stated in the Concept Paper on Minimum Wage (MW 2003a: 1);
2. 66% of national income per capita, or 68% of the average national wage that it follows from the recommendations by the committee of independent experts regarding the amount of “poverty threshold” of the earnings in the mid-1970s (Samuel 1997: 78);
3. Sufficient so that the net wage corresponds to the value of the minimum subsistence basket for one individual, as calculated by the Central Statistical Bureau;
4. Sufficient so that the net wage corresponds to the value of the minimum subsistence basket for two individuals, as calculated by the Central Statistical Bureau;
5. Any other minimum wage that is agreed by the employers and representatives of employees in the relevant sector of the economy according to Article 18.4 of Labour Law.

Some economists indicate that the existence of minimum wage affects labour market and demand of labour force. For instance, minimum wage increases the unemployment rate among young labour force because it sets a wage level above the market-clearing rate. Similarly, the minimum wage reduces not only the incentive to hire the less qualified workers, but also the incentive to offer them on-the-job training (Sachs, Larrain 1993: 497). To reduce these effects, governments try to implement different programmes of relieves. For instance, the minimum wage of young employees (usually between age of 15 and 22 years) is stated lower in several member states of European Union.

The Concept Paper on the Minimum Wage speaks to the problem of establishing links between the minimum wage and the substantial minimum. The substantial minimum is calculated by the Central Statistical Bureau in accordance with the requirements of the Cabinet of Ministers and its predecessor, the Council of Ministers, but this cannot be seen as a nationally specified minimum, because there are no normative acts which define it (MW 2003a: 4).

The Concept Paper on the Minimum Wage at this point stresses the importance of increasing the minimum wage, linking it to the average gross wage in Latvia, as determined by the Central Statistical Bureau. It is important to note, however, that the Bureau receives information about wages from reports which institutions and companies file once per quarter, although these are divided up on a per-month basis. These reports reflect only official wages with respect to which the personal income tax and social insurance contributions are paid. This means that the minimum wage calculations do not include the segment of wages that is paid illegally and under the table.

According to ideas persisted in public sphere, criteria in defining the untaxed minimum could be:

1. 50% of the minimum wage according to a conceptual decision taken by the Cabinet of Ministers;
2. A sum equal to the value of the minimum subsistence basket calculated by CSB for one person, irrespective of how high the minimum wage is;
3. 50% of the value of the minimum subsistence basket calculated by CSB for one person, irrespective of how high the minimum wage is 50%.

The implementation of the Concept Paper is behind schedule. Currently, the minimum wage (as of 1 January 2006 – LVL 90) is smaller than had been predicted for the relevant period (LVL 97) (MW 2003a: 1). Second, it has been noted that the net minimum wage is far below the minimum substance basket that has been calculated by the Central Statistical Bureau, and the growth rate in the minimum wage is too slow to compensate for increases in the cost of living. There are several important things to understand about the increase in the cost of living. In the public arena, people usually are told about the average inflation rate, but it is more important to analyse the increased cost of those products which are of everyday importance to people – utility services, for instance.

There are several obstacles against using the minimum wage and the untaxed minimum as instruments which the government can put to use in increasing wages in Latvia. The first
obstacle is concerns that a more rapid increase in the minimum wage will stimulate inflation. That is a risk if we think about Latvia’s plan to join the Euro zone in 2008. However, specialists say that a more rapid increase in inflation at this time is inevitable, and a “wage freeze” is not the only policy instrument which can be used to limit the growth of inflation. The second obstacle is the fact that the salaries of teachers are linked to the minimum wage. Article 53.2 of the Education law says that teachers with the lowest professional qualifications must receive wages per one full-time workload that is not lower than double the national minimum wage.

The third obstacle is the fact that the need to increase the salaries of everyone who works in the public sector in order to maintain wage variations among different levels of qualification of employee. It requires for assignation of sufficient state budget funds.

The fourth obstacle is related with difficulties to specify an appropriate minimum wage because of major differences in the situation of various regions of Latvia. The minimum wage which is in effect at this time is satisfactory in some regions, but in the metropolitan area of Riga it is much too low. The World Bank has recommended minimum wage differentiation by region (Rutkowski, Scarpetta 2005: 236).

The fifth obstacle is the risk that revenues of municipalities from the personal income tax would decline. Currently, approximately 75% of personal income tax revenue goes into local government budgets.

Although it is true that a higher minimum wage would mean more budget spending on increased salaries in the public sector, the social budget would gain – income from social insurance contributions would be on the rise.

The salary of any employee is reduced by the wage tax (one form of the personal income tax). Its rate, the procedure for collecting the tax, and rules related to tax relief are all defined in the law On the personal income tax (Higher Council of the Republic of Latvia 1993). The rate of social insurance contributions paid by the employer is determined in the law On state social insurance (Saeima of the Republic of Latvia 1997).

The law On the personal income tax sets the tax rate on the income of employees at 25% (Article 15), exempting untaxed income, which are made up of the untaxed minimum itself (Article 12), any tax relief that is available to the taxpayer (for dependents, for instance, this being taken into account by the employer when calculating the taxes – Article 13), and justified expenditures (Article 10).

There have been increasing debates in Latvia about reducing the personal income tax from 25% (at present) to 15% (which is the corporate income tax rate). These are the main arguments in favour of lower taxes (Fridrihsone 2005: 3):

1. Decrease of the company income tax rate showed that budget revenues did not suffer;
2. Equal rates for the corporate and individual income tax would be more fair for individual economic operators and employees;
3. Increased net wages and, by extension, increased purchasing power.

When discussing the possibility of reducing the personal income tax, it has to be said that this is a policy alternative which may threaten the fiscal goals which are stated in National Lisbon Programme of Latvia for 2005-2008 (decrease the state budget deficit).
When discussing a reduction in the personal income tax (from 25% to 15%), it seems natural that the same principles which affected greater payments of the corporate income tax when the corporate income tax rate was decreased will be in place if the personal income tax is reduced. However, if we look at the property structure of Latvian companies and compare corporate income tax rates among the member states of the European Union, then we see that increased revenues from the corporate income tax was based on different causes. Most of profitable companies of Latvia are subsidiaries of foreign firms, which mean that the owners of these companies may have different considerations in terms of leaving profits in Latvia or withdrawing them. The lower corporate income tax rate could lead to the decision to leave profits in Latvia, in which case less is paid in the corporate income tax than would be the case in another country.

These factors, however, cannot ensure greater revenues of the personal income tax. The only reason to reduce the personal income tax might be the psychological factor – it is not worth taking the risk of hiding income from the taxation if the rate is so low. There is another risk, however, from the possible reducing in the personal income tax. The short-term benefit is higher net wages, but it can also encourage employers to refuse to review wages for some time afterward. Employers have received their benefits, and higher wages would be necessary only if the increase in the cost of living is one again such that real wages are impacted.

1.3. Review of data and previous studies

The objective of this chapter is to describe key tendencies of employment and workers compensation systems which have been investigated until national programme of “Labour Market Studies” developed. In review of data and previous studies, WIF team compares Latvia with other EU member states, especially, with neighbouring states. For purposes of comparison, recent, volume and most frequently quoted studies are selected. Based on experience of Estonia and Hungary, it is possible to make assumptions about influence of minimum wage increase on employment and provision of low-paid workers. Thus, in Latvia, estimations of such kind have not been exercised yet. Other studies helped to find issues in which additional investigation would be necessary as well as regularities observation of which should be continued within framework of WIF research.

For comparison with other EU member states, WIF team uses report of European Commission “Employment in Europe 2005” (European Commission [EC] 2005: 163 – 197). It is annual report on labour market in EU countries that also includes labour remuneration analysis. In this issue includes analysis of earnings inequalities and earnings determining factors in EU (chapter IV) in the context of social and territorial cohesion in the EU. Analysis is based on Structure of Earnings Survey (SES) results from the European Statistical Office (Eurostat), released at the end of April 2005. Analysis in this report is based on statistical and econometric analysis of the survey data.

The data indicates that in 2002 there were wide disparities between the EU-15 and the new Member States of Central and Eastern Europe, where annual earnings average were two to four times lower. Across the EU-25, “services” continued to pay slightly more than “industry”, yet industrial hourly wages were still comparatively high in Denmark, Germany, Norway and the UK and relatively low in Latvia and Lithuania (in Latvia earnings in
“industry” were by 88.5% lower than EU average, but “services” paid approximately 88.2% lower wages than EU average. “Financial intermediation” was the highest paying activity, and by contrast “hotels and restaurants” was the lowest (EC 2005: 163 – 197).

Compared to average wages in the “industry”, average earnings in “financial intermediation” were by 57% higher, but earnings in “hotels and restaurants” – by 26% lower. For Latvia corresponding differences were by 85% higher earnings in “financial intermediation” and by 16% lower in “hotels and restaurants” than countries average earnings in “industry” (“hotels and restaurants were the lowest paying sector in Latvia also in year 2004 - wages in “hotels and restaurants” were by 37% lower than counties average wages).

Some regions of the employed experienced significant earnings inequality, in particular earnings inequalities for male and female – earnings of female were on average by 23% lower than earnings of male. If these results are to be compared Structure of Earnings Survey carried out in 1995, gender inequalities are decreased, because in 1995 earnings of female were by 25% lower (EC 2005: 163 – 197).

Econometric analysis of survey data yielded the following results on gender impact on earnings inequality in private sector – in Norway earnings of female were by 13% lower (if hourly wages are to be compared, controlling for other individual factors) while in Estonia this gap was 32% (largest in the sample). In Latvia earnings of female were by 20% lower than those of male and it is fairly close to EU average.

Some regions actually exhibited greater inequality at the lower deciles of the earnings distribution, i.e., the larger are the earnings of the deciles, the lower are the earnings inequality within it. However, compression was not uniform across the earnings distribution. Moreover it also depended strongly on institutional features such as minimum wages or collective bargaining agreements.

Company size had a positive impact on individual earnings, exclusive of Cyprus, Portugal and Romania, where analysis suggested the opposite.

Regression analysis also indicated that workers on part-time contracts earned on average 10% less than half of the wage of comparable full time worker (19% lower in Latvia).

If manual and non-annual workers are compared, non-manual workers earned on average by 26% higher wages (by 16% higher in Latvia). Smallest difference in manual/non-manual workers wages were observed in Greece (non-manual workers earned on average by 1% higher wages), while it was the highest in United Kingdom (by 41% higher wages) (EC 2005: 163 – 197).

In this research non-wage remuneration was also analysed (remuneration additional to wage offered by the employer) – in the EU on average bonuses and other non-wage earnings comprise 8.4% from total remuneration of the employed. In Latvia bonuses comprise only 6%, but this proportion is significantly higher than in Lithuania and Estonia – correspondingly, 2% and 3.5% (EC 2005: 163 – 197).

This report gives very good background to perform further research on situation in Latvian labour market and compare it with EU member states, allowing using experience of other member states in forging future wage policy in Latvia. Nevertheless, it must be noted, that
data obtained by Structure of Earnings Survey in Latvia are not fully adequate because of two significant reasons: (i) they do not include “envelope wages”; (ii) working hours cannot be precisely measured, because enterprises usually do not declare overtime in their reports (Hazans 2005b: 3), moreover, many enterprises do not to keep a tab actual hours worked and in their reports indicate all workers as fulltime or 8 hours per day.

Research “Working Life Barometer in the Baltic Countries 2002” by Juha Antila and Pekka Ylöstalo is one of the most frequently quoted studies on employment issues in Estonia, Latvia and Lithuania. This study covered 900 working people in Estonia, 904 in Latvia and 909 in Lithuania in year 2002 aged 16-64 years. There were nine themes: unionisation and bargaining, salary and livelihood, working time and contracts, stress factors, wage earners possibilities of influencing their jobs, job satisfaction, tele-work and information technology in working life, job-related training and development of work organisations.

General assessment of Latvia indicates that in Latvia unionisation (approximately 20% of respondents confirmed their membership in unions) is more widespread than in Estonia (14%) and Lithuania (11%), though, if comparing with previous issue of Working Life Barometer, unionisation have decreased (in 1998 25% of respondents stated that they are members of labour unions, in Estonia and Lithuania – respectively 12% and 15%).

In Latvia, study of the 1998 year has indicated that earnings of trade-unionist are the same as non-trade-unionists; however, in 2002, earnings of trade-unionists are higher. It should be noted that these tendencies are not equal among the Baltic States. In Lithuania, there is evident association between unionisation and higher labour income; however, in Estonia, the opposite tendencies are observed (Antila, Ylöstalo 2003: 118-9). When union makes agreement with employer, the collective agreement can be contract within an enterprise. If there is collective agreement in an enterprise, workers compensation is higher than in enterprise where collective agreement does not exist (Antila, Ylöstalo 2003: 120). These results show that WIF research should continue an investigation of impact of unionisation on labour income.

Overtime work is still widespread in private sector, there are no significant changes. Only slightly more than one half of respondents had written employment contracts.

Examination of labour remuneration indicates that majority of employed receives fixed salary (73%), but significant part of the rest receives piece rate wage (21%). From the total number of the employed 42% received fixed monthly salary without any additional payments, 12% - fixed monthly salary and regular additional payments (extra), but 19% - fixed salary and results fee (Antila, Ylöstalo 2003: 90).

This study indicates that average real earnings in Latvia have increased by 12.9% compared to 1998, while median real earnings – by 17.5%. In Estonia, real earnings have decreased respectively by 0.7% and 3.2%, but in Lithuania – increased by 5.1% and 4.9% (Antila, Ylöstalo 2003: 95-110). It means that Latvia experienced the fastest growth of real earning, partly due to low inflation.

Comparison of real earnings in public and private sectors (between 1998 and 2002) indicates that average real earnings in Latvia increased faster in private sector than public sector (respectively – by 10.1% and 8.3%), while median earnings increased faster in public sector (increase in public sector was 17.5%, but in private sector – decrease by 5.6%).
Such development of earnings implies that in private sector inequality in the distribution of earnings have increased – increases in average earnings, but decrease in median earnings indicate that highest wage growth was for upper half of employed. In public sector the opposite effect was observed. Situation in Lithuania is different – median earnings in private sector have increased, while average earnings have decreased, but in public sector – both average and median earnings have increased (median earnings had higher growth rate). In Estonia both average and median earnings in private sector have increased (average earnings increased more than median), while in public sector both average and median earnings decreased. It means that employers in private sector faster adjusts to changes in inflation by adjusting the nominal earnings, while in public sector indexation of earnings was imperfect, leading to decrease in real earnings.

Comparison of old enterprises (founded before transition period), reorganized enterprises and new firms indicated that in Latvia old enterprises real earnings increased by 9.5% on average (17.5% increase in median earnings), while in reorganized – 29.8% on average (17.5% median), but in new firms – only 5.2% on average (median earnings decreased by 15.0%) (Antila, Ylöstalo 2003: 108).

To sum up previously mentioned facts – earnings in Latvia were growing fast (all comparisons were based on net earnings) between 1998 and 2002. Nominal growth rate of earnings have been higher than inflation, so real earnings increased. In Estonia increase in prices offset increase in earnings, so real earnings decreased, but in Lithuania changes were small, but positive – real earnings increased.

The objective of study Determinants of Earnings in Estonia, Latvia and Lithuania provided by Organisation for Economic Co-operation and Development [OECD] is to assess impact on earnings of various explanatory factors in the Baltic States. Three comparable studies concerning determinants of earnings in each of the Baltic states (Latvia, Lithuania and Estonia) are summarized in this report – each study uses econometrics to estimate multiple factor earnings function. Estimates are based on data from each country’s Labour force surveys (years 1999 and 2000).

In order to estimate impact of human capital on earnings, levels of education and job experience were used as explanatory variables. It was concluded that education and experience obtained during Communist regime (USSR), generates smaller returns than education and experience obtained during transition period. Values of skills like computer literacy, language skills and market oriented knowledge have increase. Acquisition of such skills was impossible before the transition period.

Estimated earnings model suggests that higher education increased the wage by 66 to 80% (compared with basic education). The wage premium for secondary vs. basic education was only 13% to 14% in Latvia and Lithuania and 19% in Estonia, while the premium paid for higher vs. secondary education alone varied from 44% in Latvia to 59% in Lithuania. If the occupational group is controlled for, the marginal effect of each education type is reduced by approximately one-half, but still highly significant (OECD 2003: 2).

If these results are compared with results from similar studies in other countries, only Lithuania’s higher education appears to have unusually strong effects. The returns to secondary education are much lower by any measure in the Baltic States than in most transition countries, and also lower than in more advanced economies, but this is possibly a
result of the relatively small proportion of workers with less than secondary education in the Baltic States.

Age can be taken as a proxy for work experience. Similar studies in Western countries indicate that age-earning profile in most education groups is steadily increasing up to about age 50-52, after which it decreases, but in the Baltic states situation is different – peaks occur already at age 20-24 or 25-34 in Estonia and Latvia, but in Lithuania at age 35-44 for male and 45-54 for female (OECD 2003: 4). However, there is reasonable explanation of such phenomenon – education and experience obtained in USSR is less valuable in labour market of transition economy, so that experience and education of workers that are older than 35 – 40 have very small impact on their earnings (Hazans 2005a: 33).

Also tenure have small but positive impact on earnings – additional year of tenure generated increase in earnings by 0.5% in Estonia and 0.3% in Lithuania that is actually more than estimates in Central European countries (OECD 2003: 5).

Examination of gender inequalities in Baltic States indicated that the average wage for female in Latvia and Lithuania was around 80% of the average for male, but more than the 75% reported for Estonia in 2000. Between 1997 and 2000, female tended to reduce their relative disadvantage in Estonia and Lithuania, but only marginally so in Latvia (OECD 2003: 5).

Only a limited part of the observed wage gaps can be explained by other factors. The wage gaps that remain after discounting the effects of controlled variables amount to around 10% in Latvia, 14% to 15% in Lithuania and 17% to 21% in Estonia in 2000 (OECD 2003: 10).

According to Labour force surveys in 2000, the average wage differential between the Baltic majority populations and ethnic minorities was 16% in Estonia and 9% in Latvia and Lithuania (OECD 2003: 11). Occupational segregation of ethnical minorities is also notable, but the effect on earnings is not that straight forward as gender segregation – ethnical minorities are not concentrated only in low wage occupations. Occupational segregation appears to be the strongest in Lithuania while it is weakest in Latvia.

Unexplained earnings differential for ethnical minorities was approximately 9% in Latvia and Lithuania and 18% in Estonia (OECD 2003: 12). One of unobserved factors that can influence earnings is language skills, but there is no such information in Labour force surveys. Then, WIF employees’ survey has measures skills of the Latvian language of employee.

Examination of differences in employment in cities and rural areas indicated that workers in rural areas received on average by 8% to 9% lower wages than workers in small cities. Workers in capital cities in Latvia and Estonia received on average by 21% to 23% higher wages than workers in small cities, but in Lithuania – by 12% higher wages (OECD 2003: 12-3).

Examination of impact of distance from the capital city on earnings, in Latvia every 10 km of distance between a job location and Riga decreases the ceteris paribus wage by 1.1% (except if the job is in Ventspils). The effect of the distance from Riga is only slightly reduced if one controls for the local unemployment rate. Every kilometres of commuting increased the wage by 2.5% to 3% (OECD 2003: 13-4).
There were some additional relationships observed in Latvia (OECD 2003: 14):

- Working or living in Latgale results in a wage cut of 11 to 14% compared to small cities elsewhere;
- Predicted wage is reduced by 11% if a worker has been registered as unemployed in the past.

This study is an important source of information in order to compare Baltic States. Although there is no additional information on Latvia compared to previously mentioned studies, its value is in comparisons of Baltic States.

The objective of the paper “Unemployment and the Earnings Structure in Latvia” by Mihail Hazan is to perform analysis of labour flows between employment, unemployment, and non-participation as well as analyze impact of education, age, gender, ethnicity and regional factors on earnings in Latvia. To this purpose, econometric and statistical analysis of Labour Force Survey and Household Budget Survey data was made.

The issue of returns to education is of particular interest for Latvia, where the labour force is increasingly well-educated (in year 2002 64.4% of population had at least secondary education, but 23.2% - higher education). Estimation of returns to educations (using basic education as reference group) showed that workers with higher education (controlling for other factors except profession) received on average by 80% higher wages. These returns were significantly larger for females than for males (90% vs. 66%), for Latvians compared to non-Latvians (86% vs. 64%) and in the public sector than in the private sector (101% vs. 62%). Those working in the countryside have seen somewhat larger payoffs to education than their urban counterparts. A similar pattern is found when returns to higher vs. secondary comprehensive education (just above 50% on average) are considered, but in this case the rural – urban gap in returns is also big (Hazans 2005a: 30-1).

Returns to education in Latvia are similar to most recent available estimates for Lithuania. They are higher than in the most other EU accession countries and many western countries but lower than in Ireland and Germany. Returns to secondary education are low compared to either Central and Eastern European countries or developed market economies (Hazans 2005a: 31-2).

Assessment of age-earnings profiles indicated that in year 2000 workers received maximal earnings at age of 32 years (at age of 36 for male and age of 30 for female). Such result is significantly lower in than typical industrialized country where age-earnings profile for male in most education groups is rising up to about age 50-52, after which it decreases. For female, it often peaks somewhat earlier (Hazans 2005a: 33).

Assessment of “loyalty” of workers (number of years in one firm – tenure) indicated that average tenure was 6 years (5 years for men and 7 years for women). It was estimated that one year of tenure increases earnings by 1.2%. Returns to tenure are higher in Latvia than in Lithuania and Estonia (correspondingly 0.3% and 0.5%). Russian-speakers are estimated to have higher returns to tenure than ethnic Latvians. Lowest payoff to tenure is found in the public sector, but this is most likely due to the inflow of young well-educated people (during first year in public sector firms employees earn only 7% less than otherwise similar workers with longer tenures) (Hazans 2005a: 35).
Comparison of earnings by the type of contract, it can be concluded that temporary and seasonal employees receive on average by 12% lower wages than permanent workers with the same characteristics (education, experience, etc.). Temporary and seasonal workers receive by 8% less when occupation and firm size are also controlled for (Hazans 2005a: 35-6). This can be explained by the fact that most fixed-term workers have failed to find permanent jobs, and therefore have low reservation wages.

After assessment of main labour market indicators between years 1997 and 2002, author concludes that (Hazans 2005a: 41-3):

☑ value of education have increased with increase in returns to higher education and increase in the difference between probability to become unemployed for workers with higher education and other education levels (i.e., secondary and basic education);
☑ gender pay gap have increased via higher growth rate of male earnings;
☑ regional differences in earnings have increased (differences in earnings in Vidzeme, Latgale, Kurzeme and Zemgale regions compared to Riga region).

This study gives us detailed overview on situation in Latvian labour market and it is good reference to compare results of further studies. Since this study is based on data obtained from Labour Force Surveys of Central Statistical Bureau of Latvia, comparability of results of this study with previous periods is reduced as some data were not included in previous Labour Force Surveys, as well as data on earnings was obtained in wide intervals, by this decreasing accurateness of estimation. Until year of 2002, Labour Force Surveys registered gross wages that also reduced reliability of estimates, because of large proportion of the employed receives “envelope wages”, so there is possibility that workers actually do not know their real gross wage or they can state their official wage level that is usually equal to the minimum wage limit. Since year of 2002, Labour Force Survey obtains information on net earnings (real money income) by this minimizing possible bias in further.

When estimating the impact of minimum wage on national economy, useful information can be obtained if states similar to Latvia are examined. An interesting example is Hungary which government has increased minimum wage rapidly in 2001. The impact of government decision on flows between employed and unemployed is analysed in paper “Fighting “Low Equilibria” by Doubling the Minimum Wage? Hungary’s Experiment” by Gábor Kertesi and János Köllö. Econometric analysis of statistical data on employed and unemployed obtained in the survey of enterprises is conducted.

A decade of transition to the market economy brought Hungary’s employment ratio, similarly to most other transforming countries, down from one of the highest in the world to one of the lowest in Europe. While the metropolitan areas and most of the highly industrialised zones of Central and Eastern Europe gradually recovered from the transformational recession, in the least developed regions of Central and Eastern Europe there still were low-wage/low-employment. “Low Equilibria” is the state of labour market, when the net gains from searching and working are modest as the fixed costs of search and work (including alternative costs as social benefits, lost home production) is relatively high, so there is large part of unemployed citizens who chose not to search for work. Increase of minimum wage level can serve as an instrument to give such unemployed citizens enough motivation to search for the job and actually work.

In January 2001 the Hungarian government increased the minimum wage from Ft 25,500 to Ft 40,000 (by 57%). One year later the wage floor rose further to Ft 50,000, by this practically
doubling the minimum wage level. At its introduction in year 1989, the minimum wage level amounted to 34.6% of the average wage, a level deep below the European average. After the two hikes in 2001 and 2002 index increased to 39% in 2001 and 43% in 2002 – levels still lower than the EU average but higher than those of the UK, Spain or Portugal (Kertesi, Köllö 2003: 7). In the short-run the hike significantly increased labour costs and reduced employment in the small firm sector, especially in most depressed regions, and adversely affected the job retention and job finding probabilities of low-wage workers (Kertesi, Köllö 2003: 2).

In order to assess impact of such rapid minimum wage level increase on employment, data from financial reports at the end of year 2000 and at the end of year 2001 of, correspondingly, 2878 and 2008 small enterprises (with 5 – 20 employees) were analysed. Half of the enterprises had more than 13 employees and in half of the enterprises there were at least 5 employees whose earnings were below the new minimum level. After the first minimum wage hike wages increased by more than 11.2% for half of the employed (Kertesi, Köllö 2003: 20). Elasticity of real labour costs to changes in minimum wage limit were from 0.66 in regions with lower unemployment level and to 0.77 in regions with high unemployment (elasticity 0.66 means that 1% change in level of minimum wage limit results to 0.66% change in real labour costs), respectively, labour costs increase faster in regions with higher unemployment. There is logical explanation – in regions with higher unemployment level there is more workers whose wage level is equal or close to minimum wage level. Overall employment level in small enterprises went down by 0.7 workers per enterprise. Decrease in employment was higher in enterprises with higher minimum wage worker proportion in their employee structure (Kertesi, Köllö 2003: 21-2).

Authors conclude that rapid increase in minimum wage level actually decreased employment possibilities in less developed regions. Approximately 3% of employees in small firms lost their job during the first year of minimum wage increase, also probability of job retention and job finding for low – wage workers significantly decreased. The depressed regions were more severely affected despite their conditions that favour a positive employment effect.

Another paper on impact of minimum wage on labour market is “The Impact of Minimum Wage on the Labour Market in Estonia: An Empirical Analysis” by Marit Hinnosaar and Tairi Rõõm. The objective of the paper is to assess an impact of increase in minimum wage level on levels of employment and wages in Estonia from the year 1995 till 2000 using Econometric analysis of Labour Force Survey data.

In the second half of 1990’s minimum wage level in Estonia was approximately 25% from country’s average wage. By year 2002 it reached 31% level and it is scheduled that it will reach 41% level from the average wage level in the country by year 2006. In order to assess what possible consequences such policy can cause, this paper estimates impact of minimum wage increase in late 1990’s on employment and wage structure in Estonia (Hinnosaar, Rõõm 2003: 3).

Impact from increases in minimum wage level Heckmann model was used – it estimates impact from explanatory variables (income group, current wage, ethnicity, education etc.) on probability that worker retains his job. This analysis indicates that probability of job retention decreases most significantly for the workers whose wage is between old and new minimum
wage level (hereinafter – target group). This effect is significant (at 95% level). For other wage groups this effect was not significant (Hinnosaar, Rõõm 2003: 27).

By converting results from the Heckmann model, increase in minimum wage by 10% can cause decrease of employment in target group by 0.43 – 0.66%. This estimate is low if compared by similar studies in USA where estimated minimum wage/target group employment elasticity was greater than 1% (however, there are significant differences between Estonia’s and USA labour market) (Hinnosaar, Rõõm 2003: 28).

Relatively large proportion of employed stated that they receive wages that are lower than minimum wage while working full-time. It is impossible to determine what causes this – it could be “informal economy” (some firms can pay wages less than minimum to workers that do not have contract of employment) or workers that do not know that they are actually considered half time workers (in spite of actual working hours, in financial reports they are registered as part time workers and they wage is appropriate to part time job) (Hinnosaar, Rõõm 2003: 26).

In order to test does changes in minimum wage affect proportion of workers with wage lower than minimum in the total structure of employed, another Hausmann model was estimated with log of minimum wage as explanatory variable. Model indicates that changes in minimum wage level have significant (at 99% confidence level) positive on probability that workers wage can drop below minimum level. This effect is stronger for women and low-skilled workers (low-skilled workers were used as a reference group and coefficient of other professions were negative) – it indicates that low-skilled workers have larger probability to receive wage below minimum level if minimum wage level is to increase (Hinnosaar, Rõõm 2003: 30-1).

By converting results from this model, 10% increase in minimum wage level can cause 2% increase in proportion of workers whose wage is below minimum (Hinnosaar, Rõõm 2003: 29).

Comparison of distribution of real earnings in Estonia in year 1995 and year 2000 indicates that distribution is practically the same in both years except for small positive bias of average real wage. In both years distributions peaks approximately at minimum wage limit (in real terms) – it indicates that minimum wage level is binding constrain in Estonia (Hinnosaar, Rõõm 2003: 29).

Authors conclude that increase in minimum wage limit can negatively affect employment level in Estonia and, as it will mainly affect low-skilled workers, increase of the minimum wage is not the best possible policy if increase in welfare of low-income citizens is the target. As alternative solution increase in tax-exempt minimum or reduction of income tax for low wage levels (it is planned to decrease personal income tax from 26% to 20% and double the tax-exempt minimum) could create larger positive welfare effects, though these effects will be fully financed by government via decrease in tax revenues.

This paper gives important information on possible impact of minimum wage increase on employment, in particular because Estonia is quite similar to Latvia. This example shows that, although small but negative impact on employment can be caused by increase in minimum wage level. This effect is most notable in less developed regions where wages are lower than country’s average. However, it is difficult to asses how binding is the minimum wage level in
Latvian labour market without performing equivalent research, because there is significant part of informal economy in Latvia that pays higher wages than minimum while officially registering only minimum wages in order decrease labour costs via avoiding tax payments. The higher is the proportion of such informal economy, the smaller is the impact of minimum wage increases on employment.

1.4. Hypothesis of the research

In the initial stage of the research, WIF team proposed following hypothesis which characterized worker compensation system in Latvia and an impact of social partners:

- Additional payments that are paid for the productivity of work or in accordance with the financial indices of an enterprise is one of the mechanisms how to legally and flexibly react to deterioration of activity indices or macroeconomic environment of an enterprise.
- Social image of trade unions keeps some characteristics from soviet times. Employees lack information on the role of trade unions and their possibilities in the situation of market economy inclusive negotiating on wages. This is an obstacle preventing employee’s possible participation in trade unions.
- Benefiting from non-material values in addition to the wage is more characteristic for the sphere of service rendering than for other sectors of the national economy. Availability of non-material values increase along the growth of the position.
- The amount of unregistered remuneration reduces due to the growth of operating duration of an enterprise.
- Quality of education and its regular improvement has a positive influence on the wage and the rate of it is growth.
- Belonging to so-called “risk groups” (young mothers, workers above age of 40 years, persons without work experience, long-term unemployed persons) diminish the level of demands of an employee in the labour market by agreeing on the wage with the employer.
II DESCRIPTION OF THE RESEARCH DESIGN AND METHODS OF DATA ANALYSIS

To reach all defined research objectives, several mutually complementary research methods were applied. Each of these methods was used by developing different sampling frames and covering various target groups; as the result they reflect investigated problems in both ways – as qualitative and quantitative indices.

Research “Wages and impacting factors” consists of following stages:
- Employees’ focus group discussions;
- Employers’ in-depth interviews;
- Employees’ survey and the statistical analysis of its results;
- Employers’ survey and the statistical analysis of its results;
- Econometric analysis of CSB LFS 2003 – 2004 data;
- Audit of information systems;
- Development and evaluation of field policy recommendations.

2.1. Employees’ focus group discussions

The objective of employees’ focus group discussions were to investigate perception of workers on remuneration system, to describe financial and non-financial types of compensation which are typical for Latvia distribution of which would be measured within employees’ quantitative survey. In addition, important task was to describe formal and informal relations between employee and employer when reaching an agreement on particular workers compensation.

If main survey aspects in previous studies were devoted to analysis of wage as the result and its correlation with the objective characteristics of human resources (education, age, gender etc.), then WIF research is more focussed on the extension of range of the inspected factors, stressing those subjective and variable aspects, that are more or less important “during negotiations of reaching agreement on definite wage level”.

Method of focus group discussion was used. It allows identifying of all practically important opinions on examined issue as there is limited amount of opinions about any topic in the whole society or definite social group. Application of this approach will let to hear language which is used by employees when they discuss matters related to wages and work conditions that are important to them being critical to accept or decline any proposal of employer.

Within framework of WIF research, 12 focus group discussions were conducted six of which took place in Riga and six – outside Riga, at other towns of Latvia, correspondingly. All participants of the discussions were full-time employees and both sectors – public and private – were covered. Composition of focus groups by socio-demographic characteristics of participants is shown in table 1.
Table 1. Division of focus group discussions by socio-demographic characteristics of participants

<table>
<thead>
<tr>
<th>Populated area</th>
<th>Language</th>
<th>Gender</th>
<th>Level of net labour income</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Low (until 150 LVL)</td>
</tr>
<tr>
<td>Riga</td>
<td>Latvian</td>
<td>Male</td>
<td>40 – 60 years</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Female</td>
<td>30 – 45 years</td>
</tr>
<tr>
<td></td>
<td>Russian</td>
<td>Male</td>
<td>20 – 30 years</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Female</td>
<td>20 – 35 years</td>
</tr>
<tr>
<td>Outside Riga</td>
<td>Latvian</td>
<td>Male</td>
<td>20 – 40 years (Cēsis)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Female</td>
<td>35 – 55 years (Jēkabpils)</td>
</tr>
<tr>
<td></td>
<td>Russian</td>
<td>Male</td>
<td>20 – 35 years (Jelgava)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Female</td>
<td>25 – 40 years (Ventspils)</td>
</tr>
</tbody>
</table>

Separate focus groups were organized for different socio-economic categories of employees. Composition of each focus group was homogenous by chosen criteria. They were: language, gender, age and level of net labour income which includes both types of it – legal and illegal remuneration. Notations of participants of focus group discussions mentioned within table 1 are used in future review when illustrate mode of expression of employees.

Above mentioned criteria for selection of participants of focus group discussions were drawn according to research theme. WIF research team considered that male and female communication and experience with employers concerning wage issues could be different, separate group discussions for male and female will be carried out. Groups must be homogenous both on language and incomes levels, as well as age variations of participants must not be overly wide. These considerations reflected within selection of participants of group discussions. However, in the division after occupations one group could be heterogeneous if other abovementioned conditions agree.

2.2. Employers’ in-depth interviews

The objective of employers’ in-depth interviews was to examine how economical indicators of enterprise affect wages of its employees; what is the process of studying supply of labour market, and how it influences the decision of employer to raise wages.

In depth interview is method of qualitative studies. For purposes in an interview, guidelines are developed. Within conversation, professionally trained interviewer finds an individual approach to every respondent. It allows to obtain as mush detailed information as possible (especially, discussing talking about specific sensitive subjects)
Method of in-depth interview should be used because different respondents are included into sample which otherwise would not feel comfortable meeting together in a single focus group (e.g. Latvians and Russians, different age groups, various sizes of enterprises, different regions etc.). Considering companies’ managers usually being leader type personalities, in-depth interview as data collection method let us to avoid the unnecessary side-effects, like the competition between group participants when all of them have strong leader qualities. In-depth interviews are also convenient to reach the respondent at any acceptable time, and thus attaining greater responsiveness and participation. Within this part of WIF research, 26 in-depth interviews were conducted characteristic of which given into table 2.

### Table 2. Division of in-depth interviews by characteristics of an enterprise

<table>
<thead>
<tr>
<th>Residence</th>
<th>Size of a company</th>
<th>Main field of activity of company</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Production</td>
</tr>
<tr>
<td>Riga</td>
<td>Micro (up to 9 employees)</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Small (10 – 49 employees)</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>Medium (50 – 249 employees)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Large (250+ employees)</td>
<td>1</td>
</tr>
<tr>
<td>Outside Riga</td>
<td>Micro (up to 9 employees)</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>Small (10 – 49 employees)</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>Medium (50 – 249 employees)</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Large (250+ employees)</td>
<td></td>
</tr>
</tbody>
</table>

When dividing Latvian enterprises by three main types of kind of economic activity (production, sales and other service), considering various sizes of companies (micro, small, medium and large), as well as location (Riga or outside Riga), division of conducted in-depth interviews are shown in table 2.

Enterprises of construction and agriculture were included into “production” sub-group, enterprises of wholesales, retail sale, and repair of personal and household goods were included into “sales’ sub-group, and other kinds of economic activities were included into “other service” sub-group. It should be added that the actual number of enterprises in each subgroup in Latvia is not the criteria for choice of respondents for in-depth interviews. Notations mentioned into table are used for identifying of quotations within paper as well.

### 2.3. Employees’ survey

The objective of employees’ survey was to collect numerical data on wages, form of remuneration, including non-financial remuneration, as well as other aspects which allowed analysing influence of various factors described in theoretical background. Employees’ survey of WIF research consisted from three parts. Firstly, it was choice of sampling model, secondly, it was fieldwork, and, third, it was the data analysis including econometrics.
Sample for quantitative survey among full time employees is defined as stratified sample of several levels. Total amount of the sample is 4040 full time employees (according to subjective opinion of respondents) excluding high level managers and legislators.

Such definition of population follows from requirements for wage structure studies and the objective of WIF research – to give adequate perception of Latvian wage system. For this purpose, the homogenous population of employees wage of which does not depends on their own decision is needed. Marginal values (located in a distance for core value) which decrease homogeneity are excluded. Within the study, marginal values consists those employees which are decision makers on their own wage or can influence it in a great extent and which remuneration is considerably higher wage and wider range of available wage complementary benefits are observed. Simultaneously, these employees have higher competence on mechanisms which can affect wage; therefore, they can be considered to be experts instead of observation of the study. All characteristics mentioned above are typical for legislators, senior officials and managers; and this could be observed within employers’ in-depth interviews. Therefore, WIF research team considered that high level managers did not correspond to the population of survey and they should be excluded from the sample frame.

If include earnings of high level managers into calculations, the data with greater variance and set of marginal values would be obtained. The remuneration of managers is considerable higher (higher basic wage, wider range of non-financial remuneration, greater their financial value etc.) that results as more positive perception on labour income in Latvia that it is in case when high level managers are excluded from the population. Since the objective of the study is to describe wage fixation mechanisms instead of calculation of average wage then exclusion of high level managers from the population is informed decision.

Despite of correction of the population, the results of WIF research are comparable to the data of Labour Force Survey of CSB. When selecting in LFS the same target group as chosen for WIF research, the obtained results can be compared.

In order to choose the most suitable sampling model for WIF research, the secondary data analysis was made. The objective of cluster analysis is to find groups of local municipalities (clusters) which are characterized by similar employment indicators and wage determinate mechanisms. Following indicators were used in the cluster analysis:

- Ratio of employed population (%) regarding to all population in municipality;
- Average wage for which social contributions were paid in given municipality;
- Ratio of employees (%) with higher education regarding to all population in municipality;
- Ratio of employees (%) who moves for a job to bigger municipality every day;
- Ratio of service sector employees (%) in municipality excluding health and education sectors as atypical service fields where wages varies between public and private employers;
- Ratio of production sector employees (%) in municipality excluding construction.

Values of above mentioned indicators for each municipality were obtained from CSB LFS 2003 – 2004 data and State Social Insurance Agency. Hierarchical clustering procedures were applied. As the result, 14 groups of municipalities or clusters were obtained.

As a decision was made to develop sample from local authority groups gained in cluster analysis then every local authority group built up one stratum. The size of every separate
stratum determined total number of employees in local authorities which contained corresponding cluster. For development of numeric observation, there were data of State Social Insurance Agency about number of employees in populated territories used (according to registered residence address).

Within each cluster, primary sampling units (local authority) were chosen. The number of selected units in each cluster was determined on the basis of its size, taking employee number into account. When researching wage structures, it is of key importance to avoid accidental mistakes and non-response which can rise from several reasons: route of an interviewer, date and time of data gathering, particular current events etc. Therefore, WIF team decided that 40 interviews with respondents from the relevant target groups would be conducted at each sampling unit. The planned sample (4,000 full time employees) involved the collection of data at 100 primary units. This number is sufficient for Latvian conditions which possible influence on the results is estimated when applying econometric methods in data analysis.

The following supplemental criteria were taken into account when selecting primary units in the clusters:

- It was mandatory to include local authorities which, within a single cluster, represent higher and lower average salaries;
- In those cases when clusters were distinctly homogeneous, selections must be based on geographic coverage.

Locating an appropriate respondent from the target group at each survey location was conducted on the basis of the so-called route method. When it came to households with several appropriate respondents, the respondent was chosen on the basis of the principle of the "youngest man". Fieldwork was conducted between November 20, 2005 and February 10, 2006, applying face-to-face method (if necessary using cards with answers).

In order to gather 4000 observation of full time employees, there were 11587 contacts with respondents 8464 of which corresponded to target group. Within them, 4040 interviews were made and 4424 contacts referred to non-response. The sample structure of employees’ survey of WIF research is added into table 1 of an appendix.

Obtained data of employees’ survey were analysed by econometric methods to establish effect of factors characterizing employees on their wage. To accomplish it, models where wage is used as a dependent variable and indicators characterizing employees as independent variables are estimated.

As the main instruments to achieve these goals, wage equations, also as the earnings functions will used. The wage equation relates employee’s expected earnings \( w \) to the (observable) variables \( X_k (k=1,\ldots,K) \) and \( Y_j (j=1,\ldots,J) \) characterising the worker and the firm. Both technically and from the interpretation perspective it is better to work with the logarithm of wage rather than the wage itself, and this is the common approach in the literature. Taking into account that the worker’s earnings reflect also characteristics of the worker and the firm which are usually not observed or not available (e.g. individual’s ability and initiative; the firm’s position in the market, reputation etc.), as well as the impact of random factors, the wage equation can be presented in the following form:

\[
\ln(w_{it}) = \beta_0 + \sum_k \beta_k x_{ikt} + \sum_j \gamma_j y_{jit} + \delta_t + u_{it}. \tag{1}
\]
where \( i \) denotes individual workers, \( t \) – different observation periods. Worker's \( i \) wage at the main job in the period \( t \) is denoted \( w_{it} \), \( X_{ikt} (k = 1, \ldots, K) \) is the vector of worker's \( i \) personal characteristics (age, gender, education...) in the period \( t \), \( Y_{jit} (j = 1, \ldots, J) \) is the vector of characteristics of the firm where the worker \( i \) is employed in the period \( t \) (sector of economic activity, ownership form, number of employees, location etc), \( \delta_t \) - time period specific effects, \( u_{it} \) – random error term (representing the impact of unobserved and random factors on wages). By assumption, expected value of the error term is zero: \( E[u_{it}] = 0 \), and \( u_{it} \) us uncorrelated with \( X, Y \).

If sufficiently large and representative data set is available, the coefficients \( \beta_k (k = 0, 1, \ldots, K) \), \( \gamma_j (j = 1, \ldots, J) \) and \( \delta_t \) can be estimated by econometric methods. In this study, the maximum likelihood method will be applied. When survey data are used, one has to take into account:

- observation weights (so called p-weights, or probability weights, which show the number of population members represented by each respondent);
- the survey design (stratification, as well as possible error correlation within the primary sampling units, PSU).

If the weights are neglected, the estimates might be biased and the conclusions cannot be generalised to the whole population. If the error correlation is not accounted for, the coefficients’ estimates are unchanged but the standard errors might be wrong, leading to wrong conclusions about the significance of each of the variables (factors) For instance, observed association indicates higher level of significance.

Econometric methods which account for p-weights and error correlation within PSU, use heteroskedasticity consistent (robust) standard errors. This is important because wage data, even after the logarithmic transformation, usually are heteroskedastic (e.g. errors are larger in the high earnings region).

Further on, we will examine basic components of wage equation. As shown in Figure 1, the level of education affects individual’s wage in two ways: through other factors (mainly, occupation, industry, enterprise size, and ownership sector) and directly (within given industry, group of occupations, sector, and firm size class better educated workers, other things equal, are better paid).

Hence, the total effect of education on wages (return to education) can be split in two parts. The first component (the access return) consists of the first three terms, \( bB + cC + dD \), of the formula (2); it can be interpreted as the average effect of education on access to better paid jobs. The second component (the reward return) is the last term, \( A|P,N,S) \), of the formula (2). It is the education “premium” after excluding the effect of the workers’ category (the group of occupations, industry, and ownership sector).

As seen from (2), the access return is further split in three parts which express the effect of education on earnings through group of occupations, industry of employment (kind of economic activity), and ownership sector. Previous research has shown that especially substantial components of the access return to education are the ones associated with the main group of occupation and with the enterprise size. For simplicity of presentation, we will ignore the effect of education level on the choice of economic activity (industry) and ownership sector, assuming that \( c = d = 0 \).
Total effect of the education on earnings (after accounting for the effect of other factors E):

\[ A = bB + cC + dD + A|P,N,S \]  

(2)

Note. All effects in the Figure 1 are conditional: \( B=B|I,N,S \) etc. The effects of other factors on the choice of education, occupation, and sector are not shown.

In all regression models as dependent variable has been used total earnings – basic wage and premiums and perquisites; therefore, further in text, when referring to remuneration or wage, it should be understood as total net wage of employee, i.e., all earnings received from principal work are applied to 12 months.

Regression basic models were split into four groups:

☑ models where control for both professions and operation sectors of activity are included by controlling for the largest cities and statistical planning regions;
☑ models where control for sectors of activity are included but control of professions is not included by controlling for the largest and planning regions;
☑ models where control for both professions and sectors of activity is included by controlling for only planning regions;
☑ models that are built up on models of the first group and control effect of additional factors – are the disjunctive variables of other nationalities important, does family status and the fact that employee has children have any effect, what is effect of unemployment level and other factors.

If model does not include occupation and enterprise size, then beta coefficients on the educational dummies in this model (denoted \( \beta_{k,1} \)) reflect the total effect of education on earnings (\( A \) in formula (2)). Specifically, coefficient on each of the education levels shows the effect of this level of education on earnings compared with the reference group. The effect of
higher vs. lower education is expressed by the difference of respective coefficients. Percentage wage differentials can be calculated as follows:

Expected wage differential between education levels $k$ and $j = (\exp(\beta_k - \beta_j) - 1) \times 100\%$. (3)

Beta coefficients on the educational dummies (denoted $\beta_{k,2}$) measure the effects of education conditional on the group of occupations, industry (sector of economic activity), enterprise size, and the ownership sector. This is denoted by $A|P,N,S$ in formula (2) and can be interpreted as the reward component of return: the average premium to each education level after excluding the effects of the group of occupations, enterprise size, industry, and the ownership sector. The access component of return is obtained as the difference between total return and the reward component (see table 3).

### Table 3. Decomposition of return to education using two models

<table>
<thead>
<tr>
<th>The components of return to education level $k$ vs. level $j$</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total return $\beta_{k,1} - \beta_{j,1}$</td>
</tr>
</tbody>
</table>

Variables corresponding to respondent’s age and squared age were included in all models. Their inclusion in all models is necessary in order to control for employee’s age effect on wage by determining effect of other factors. In order to define an income – age profile (curve that characterizes the dynamics of average income of employee over the years of his work) models without controlling for group of professions were tested.

Following statistical packages were used for data processing: SPSS for Windows and STATA for Windows.

In this review, WIF team describes those relationships between variables observed in the research which are significant at least at 5% level (p value is 0.05 or less). It means that estimate is statistically significant at least 95% confidence level. In practice it means that possibility of erroneous observed regularities is 5% or less.

Describing results of econometric analysis, the term “control” will be used frequently. Control technique is applied as several “explanatory” variables are included in multivariate regression analysis. The multivariate model analyses also partial relations between two variables by controlling for them with other variables. It is said that variable is being controlled if its effect on other variables is eliminated. For example, by controlling educational level, relationship between two other variables with characteristic equivalent educational level is determined; by controlling for profession of employees, employees within one sector and within one group of professions are compared. Variables applied in control are indicated in our research, which means that respondents who have equivalent categories in indicated variables, for instance, equivalent education, group of profession etc. are compared.
2.4. Employers’ survey

The objective of employers’ survey was to collect numerical data on wages for different levels of qualifications, changes of total workers compensation fund within last year, non-financial remuneration, as well as attitude towards increase of national minimum wage and untaxed minimum.

In contradistinction to employees’ survey, in employers’ survey, there were not possible to separate which benefits were offered to which category of workers. Obtained answers include all employees of enterprise including high level managers – head of the board, members of the board, advisors etc. When comparing the results of both surveys, it is seen that considerable amount of wage complementary benefits (financial and non-financial) produces remuneration of high level management.

The population of employers consists of all economically active statistical units, i.e., both market sector statistical units (enterprises) and outside market sector statistical units (funds, societies, foundations, and state and local government institutions) are included.

The sample of employers’ survey was chosen applying systematic random sample. Selection of sampling units was done by CSB considering request of WIF research team: using systematic random sampling method by number of employees in enterprise (unit has higher probability to be selected if it has greater number of employees), to select economically active statistical units within three and more workers are employed. The criterion of three persons be employed was considered to be important in order to avoid choosing enterprises which managers had not had an experience of enterprise administration.

Sample size of quantitative survey among employers is 800 units each of them can be represented by one or several persons – owner of high level manager of an enterprise, manager of personnel department or other specialist according to invitation of manager (for instance, bookkeeper).

The objectives of WIF research determine two substantial requires for the sample of employers’ survey. Firstly, the impact of each unit (enterprise or institution) on national wage structure should be considered proportionally the number of employees there. Secondly, it is needed to provide the possibility to compare the data of both studies – employers’ and employees’ survey. For this reason, a frame was developed how many enterprises should be surveyed in division by region, number of employees, type of economic activity and ownership considering summary number of employees in population.

Statistical units were selected applying the coefficients of their influence according the number of employees at enterprise. Correspondingly, proportion of medium and large enterprises in sample was enlarged.

The comparison of the data is burden due to incapability of employees to name exact size of an enterprise (for instance, if he/she works at regional branch of large enterprise or institution), as well as to determine exact place of residence of enterprise. In most cases, large enterprises have been registered in Riga; therefore, in statistical data, they are included into region of Riga. In case of single individual, region of workplace is stated by place of residence de facto because place of main branch can be unknown. Therefore, when comparing
the results of both surveys, the influence of above mentioned factors should be considered. Despite of restrictions, possibility to compare the data of both surveys is evaluated as sufficient.

The fieldwork was conducted between February 1 and March 28, 2006 using face-to-face method. In some cases, cards with answers are shown to the respondent. In order to obtain 800 observations of employers, there were 1239 contacts with potential respondents 1203 of which corresponded to target group. Within them, 803 interviews were conducted and 403 contacts referred to non-response. The sample structure of employers’ survey is added into table 2 of the appendix.

In accordance with the fieldwork report, it may turn out that companies which pay less in unofficial wages have participated more than others. The large number of refusals in certain sub-groups of companies indicates that there are difficulties or problems in that area (micro and small enterprises, construction etc.).

It should be noted that fear of control of state institutions is not always be the reason of refusal. Among other reasons there is the fact that many surveys of companies have been organised over the last six months. Potential respondents are sceptical about surveys as such, or perhaps they have had negative experience with this process in the past. Some have much work to do at the time when data are being collected. Others fear, without reason that competitors will find out about their wage structure. It is not always possible to convince respondents of the benefits that will accrue to them when they take part in the survey.

2.5. Econometric analysis of CSB LFS 2003 – 2004 data

The aim of econometric analysis of Labour Force Survey data for the years 2003 and 2004 is to continue previously performed wage analysis and follow to development of regularities drawn by M. Hazans. Previous studies were made based on LFS data obtained until 2002. Regarding to M. Hazans experience, comparability of data will be ensured. When comparing the results of econometric analysis of both CSB LFS and employees’ survey data of WIF research, differences in earnings at the level of individuals. Similarly, larger sample size in the LFS allows obtaining results which was not possible to derive from the employees’ survey of WIF research.

Latvian Labour Force Survey data of 2003-2004 include about 18 000 observations of wage earners including repeated observations. According to the LFS rotation scheme, each respondent have been observed one, two or three times during these two years. Just about 6% of respondents have not answered the question on the last month earnings, and number of valid observation (about 17 000) is sufficient for estimating a detailed wage equation separately for male and female as well as for public and private sector employees.

Net monthly earnings will be used as the wage measure. The wage information in the LFS data is reported in interval form; therefore, we are going to apply survey interval regression method which has been developed for such data in the survey context. Previous studies (Hazans 2005a: 40) confirmed that the interval regression method gives reliable results. Moreover, main results concerning the wage structure based on LFS 2003-2004 are very
similar both to the results based on LFS 2005 data (Hazans 2006), and to the results of employees’ survey of WIF research.

Since 2002, Central Statistical Bureau of Latvia conducts LFS continuously throughout the year. Hence equitation (1) includes monthly dummies; when 2003 and 2004 data are pooled, the year 2004 dummy is included as well. This way, effects of the main variables of interest (education, age, etc.) will not be distorted by seasonality and inflation.

In the analysis of CSB LFS, labour income both models without controls of occupation and with controls for the nine major groups of occupations are shown (in addition, enterprise size is controlled for as well). Description of the benefit of two model usage is given within chapter of analysis of the results of employees’ survey of WIF research. This approach allows evaluating of the effect of education on individual’s wage in two ways: directly and through other factors (see figure 1).

In the analysis of CSB LFS, there are examined earnings functions estimated for employees with higher (tertiary) education, with special emphasis on the field of education. Five “field ratings” (according to field’s effect on earnings) will be obtained for the following categories of employees:
- full-time workers with higher education completed in 1992-2004;
- full-time workers with higher education completed before 1992;
- all full-time workers with completed higher education;
- full-time male workers with completed higher education;
- full-time female workers with completed higher education.

The estimates are based on pooled 2003-2004 LFS data set. The sample includes 3329 full-time workers with completed higher education. Taking into account that the field of education has a strong effect on the industry of employment, full effect of the field on earnings is obtained from models which do not include industry and occupation controls. It is worth noticing, that the field effect is a broader concept than just occupation effect. Field effects show how labour market values skills provided by different fields of education, disregarding whether or not the graduate is employed in corresponding industry and/or occupation. The results have implications for state education policy.

2.6. Audit of information systems

The objective of information system audit is to analyse the quality of statistical information and to develop recommendations that would allow representatives of governmental institutions to make more precise their further estimations of return of implemented policy. In order to reach efficient cooperation among different governmental institutions, the scheme of mutual cooperation and information exchange among appropriate institutions is exercised within audit of information systems to evaluate its efficiency and to develop recommendations for improvements.

The information systems audit was developed on the basis of a presentation conducted by Susan Henczel – “The Information Audit as a First Step towards Effective Knowledge Management: an Opportunity for the Special Librarian” read in 2000.
In considering the auditing method as a whole, it must first be remembered that most theoretical materials about information systems audits are focused on analysing the flow of information in private structures (Oz 2000: 8; Henczel 2000: 210-1). The focus in auditing the information system of a private structure is primarily on the organisation that is being studied and on an analysis of its needs.

For this purpose, it should be determined which is an organisation or organisations that develop national wage issues as audit of information systems investigates decision making structures. It means that the studied organisation must be one which can take a decision or influence the taking of a decision on wage issues at the national level. Choice of involved government institutions was made on the basis of regulations of Cabinet of Ministers No. 49 (Regulation of the Ministry of Welfare), No. 194 (Regulation of the Ministry of Finance), No. 413 (on fixation of the monthly minimum wage) and No. 995 (on wages of state employees).

On the basis of these regulations, the researchers determined the two institutions that are responsible for wages in Latvia: the Ministry of Finance (MF), which is responsible for the wages of those who work in the state sector, and the Ministry of Welfare (MW), which is responsible for drafting recommendations on increases in the minimum monthly wage in the country. Similarly, other government institutions or organisations which work on or are in some way related to the issue regulating wages in Latvia were identified. They are: the Ministry of Economics, the Policy Coordination Department of the National Chancellery, the Latvian Association of Local Self-Governments, the Free Trade Union Confederation of Latvia, and the Employers’ Confederation of Latvia.

Within framework of WIF research, the knowledge concept with respect to information systems audit designed by Henczel was used. The central issue is knowledge, not just analysis of the needs of the organisation that is being studied. Henczel defines three phases in an information systems audit: the data phase, the information phase, and the knowledge phase. The data phase is used to analyse the needs of the organisation that is being studied, i.e., the kinds of data that the organisation needs in order to prepare information. The information phase is one in which data are processed and placed into the context of the issue that is being analysed (the information phase must be seen as a process and as the most important component in knowledge), and the knowledge phase is last one (Henczel 2000: 212). It must be added that the status of data, information and knowledge will be dictated by the issue that is being studied.

Henczel divides knowledge up into two segments: explicit knowledge such as databases, reports and other kinds of documents, which are comparatively easy to obtain and inspect, and tacit knowledge or human knowledge – the experience and competence of employees of the relevant organisation or organisations (Henczel 2000: 213). According to Henczel, tacit knowledge is difficult to define, because it is made up of experience, education, intuition and other, often irrational components.

WIF team considered the MW and MF to be the primary creators of knowledge in the area of wages. This choice was based on the aforementioned factors – normative acts and the fact that the two institutions have a direct influence on the primary decision making institution – the Cabinet of Ministers. Each institution and organisation is described in accordance with the key recommendations of Henczel: to identify the organisation’s main functions; to determine the role of the organisation in the issue that is being researched; to note the key shortcomings in the flow of information, the creation of knowledge, communications and taking of
decisions; as well as to develop recommendations and forward them to the relevant organisation.

To accomplish audit of information systems, two data gathering methods were used – document analysis and expert interviews. During the study, there were interviews with 12 respondents – nine government institution representatives (Ministry of Welfare, Ministry of Finance, Ministry of Economics, State Chancellery and Central Statistical Bureau) and three representatives of non-government organisations (Latvian Association of Local Self-Governments, FTUCL and ECL). There were face-to-face interviews, as well as interviews by telephone and electronic correspondence, depending on the availability of the respondent and the form of contact that was selected.

The information sources that are listed in the study are mostly the ones that were mentioned by interviewed representatives of government institutions and organisations, which means that the listed information sources have a higher level of reference and greater influence in the process of taking decisions. Surveyed representatives of government institutions refrained from naming all sources of information that were used in preparing reports and calculations. Respondents made the excuse of a lack of time. The consequence was that some of the studies, statistical data and calculations related to wages were mentioned only gradually. Sometimes all that was mentioned was the country in which the research had been conducted and the year when it occurred.

Given the amount of time that was available for the research and the broad nature of the issue of wages, the information systems audit could not involve a study of the decision making structure of each organisation mentioned in the research. That would have created a set of information that would be huge and difficult to structure. It would be more difficult then to look at the overall work of the system and problems in the cooperation that exists.

2.7. Methods of the evaluation of field policy alternatives

Within the framework of the study “Wages and impacting factors” (WIF), three political alternatives chosen by the Ministry of Welfare were to be analyzed. Although a traditional approach in evaluation of political alternatives is the analysis of costs and benefits, it was not entirely possible to apply this technique to all the versions of alternatives. Difficulties related to identification of possible expenses and benefits were main reason for that. These difficulties are described in details in the respective paragraph of this review. As all alternatives to analyze contained situations that are related to a social and economical risk, identification and evaluation of the alternatives was carried out using technique of prognostication. The methods used for prognostications were fact graphic and expert methods.

Usually the methods for comparison of expenses and benefits are selected on the basis whether it is possible to evaluate benefit in financial terms or other quantity, or they can be considered qualitatively. If it is possible to evaluate benefit in financial terms, the cost – benefit analysis is applied. In cases then the value of benefit can not be evaluated in financial terms, the analysis of expense efficiency is applied (Kļaviņa, Klapkalne, Pētersone 2005: 32, 48).
Implementation of political alternative requires investments that can be dividend into (Kļaviņa, Klapkalne, Pētersone 2005: 26):

- Expenses of implementation that are necessary to start activities;
- Residence expenses what are necessary in a long-term perspective.

The probable consequences and risks of alternative implementation that the government should take into account when choosing an alternative to introduce were to be evaluated in the analysis of each alternative. The first alternative foresees the elaboration of algorithm for increase of minimum wage for the time period after 2010. That is why prognosis for Latvia macroeconomic environment was necessary. In order to evaluate the second alternative that foresees differentiation of wages in separate fields of national economy, the introduction and maintenance expenses of definite control mechanisms determined by state institutions were to be prognosticated. On the account of the mentioned reasons, the prognostication method was applied.

Prognostication is used to define future state of a particular indicator (like that of income, market demand, etc.) or to evaluate certain political influence (Kļaviņa, Klapkalne, Pētersone 2005: 53). Depending form the considered problem, prognosis may refer to the entire national economy, to a particular field, enterprise or territory or it can have a national, regional or local character. When the factors, to which the problem is subordinated, are known, one can prognosticate change of economical indices in relation to change of other indices. That may serve as grounds for decision-making.

Prognosis of socially economical indices is used to establish development scenario. Analysis of scenarios represents a supplementary part for the cost – benefit analysis. A scenario is a description of a probable situation made on the basis of several assumptions that not only includes prognosis, but it also reflects the environment. The aim of a scenario is to find out the most significant risks. In a scenario, the impact that the processes will undergo when the variable value is changes simultaneously. Conclusions are drawn on the grounds of objective analysis and subjective interpretation.

Depending on whether statistical data or evaluation of an expert is taken as the basis of conclusions, the prognostication methods may fall into (Kļaviņa, Klapkalne, Pētersone 2005: 55):

- objective (fact graphic) methods.
- subjective (expert) methods.

With the help of fact graphic methods a prognosis may be elaborated taking into account the information about the studied process or development of the object in the past and having an assumption that disposition of the process is not going to change in the future. Generally speaking, fact graphic methods may be called quantitative (Kļaviņa, Klapkalne, Pētersone 2005: 55). These methods are widely used in international calculations when elaborating macroeconomic scenarios. In the WIF study, fact graphic methods were used in order to make prognosis on macroeconomic environment in Latvia in 2010 an later, as the first alternative required.

In cases when it is difficult to predict the reaction of the society or there is no information available about the probable reaction on the factor of external environment, expert methods are to be used. They are used for elaboration of concrete prognosis if there is lack of information about the studied object of information collection, is too labour consuming, or
inadequately expensive. The expertise work group formulates the considered problem; it specifies the targets of examination and put them down in the form to be filled up by the experts (Kļaviņa, Klapkalne, Pētersone 2005: 59). A three-round expert inquiry was organized in accordance with the Delphi method for evaluation of the political alternatives in the WIF study.

The main principles of Delphi method are (Kļaviņa, Klapkalne, Pētersone 2005: 59):

- inquiry is organised in several rounds, in each of them reaching a higher level of concreteness;
- statistical processing of evaluations are made after each round;
- all experts are introduced to the statistical summary of evaluations;
- if there is an opinion of an expert that differs significantly from the collective evaluation, the expert has to substantiate it;
- expert inquiry is anonymous.

With the help of Delphi method, a new opinion is acquired without having any discussion among experts. The advantage of the applied method is the ability to acquire numerical values of expenses and benefits of political alternative implementation. Necessity to reach a collective opinion facilitates the description of political alternative implementation risks because in the result of indirect discussions a common vision of the problem is achieved. For the realization of the WIF study, it was important to concretize and extend the expert evaluation form in relation to the results of the preceding inquiry round. Anonymity of the experts and possibility to adjust the inquiry to the needs of each expert was another advantage of the applied Delphi method.

While evaluating the three mentioned political alternatives, research team organized three rounds of the inquiry, introducing the experts with the results of the previous round when the second and the third round came. In total, 19 experts participated in evaluation of political alternatives and prognostication of possible consequences. The experts represented all interested parties.

Initially the number of experts was not limited. The WIF team decided that there should be three interested parties involved. The first of them is representatives form state institutions that are connected with determination of the minimum wage in the country. There were representatives from the Ministry of Welfare, the Ministry of Finance and the subordinated institutions (eight representatives in total) among the experts of this group. The second party are representatives from employers’ and employees’ organizations (nine specialists in total). In the conformity to the content of the respective political alternatives, the WIF team also invited representatives of different spheres of activities to participate. Independent experts that do not represent directly any of the interested parties (two specialists) formed the third party. Involvement of independent specialists in evaluation of political alternatives justified itself because these specialists offered professionally substantiated opinions about the probable consequences rarely heard before in the public caused by implementation of one or another political alternative.

The first inquiry round was organized during the interview in order to get a more detailed commentary of the considered issue. The second and the third rounds were made in the form of a questionnaire.
III ORDER OF WAGE REGULATION AND INVOLVED SOCIAL PARTNERS

Nowadays, the developed countries actively participate in the person income development process by using different methods, mainly fixing minimal wage, taxation policy and social insurance programs.

To develop social dialog, there has been established National Tripartite Cooperation Council (NTCC) where representatives from the state, Employers’ Confederation of Latvia (ECL) and Free Trade Union Confederation of Latvia (FTUCL) work together. The purpose of NTCC activities is to promote the cooperation of the government, employers’ and employees’ organizations (trade unions) at the national level and provide coordinated solution of socioeconomic development problems that would suit both society and state interests, and would guarantee social stability and improvement of welfare. Concerning wage issues, fixation of minimum wages is a widespread instrument in making wage policy. In addition, allowances of personal income tax (untaxed minimum, relief for depended persons etc.) are instruments for decrease of tax burden for low-paid workers.

General model and form of cooperation among non-governmental organisations and state institutions on wage regulation issues and decision making process on minimum wage increase is shown in figure 2. It depicts the procedure by which the MW submits its informational reports to the Cabinet of Ministers, as well as the role which the MF plays in regulating wage issues. The scheme also depicts the participation of other government institutions and organisations in setting wages.

The decision making structure consists of four levels. The first level is main data and studies which is used by state institutions when preparing documents and motivate arguments on possibilities to increase minimum wage. The second level reflects information and knowledge which includes the analysis of processes which affect the quality of information reports and calculations, both from the perspective of explicit knowledge (documents) and from the position of tacit knowledge (experience of specialists). In the level of explicit knowledge, exchange of information occurs among state institutions and social partners, and the last ones evaluate proposals prepared by ministries. For the purposes of the evaluation, both explicit and tacit knowledge on earning structure in Latvia is applied.

The third level of decision making structure is called as knowledge transformation because it reflects additional evaluation of the knowledge (documents) that are prepared by government institutions by a meeting of state secretaries, by the National Tripartite Cooperation Council, and by the Latvian Association of Local Self-Governments. The National Chancellery is the central government institution for coordinating the aforementioned meetings and for organising the flow of information among partners involved in the meetings. The role of the National Chancellery gradually expanded as the role of the National Chancellery as a holder of knowledge expanded when data base of studies and publications has been made.

The fourth level of decision making structure is main institution – the Cabinet of Ministers where the final decision on increase of minimum wage is made.
Figure 2. The structure of decision making process on minimum wage increase

**Cabinet of Ministers**
Develops political position, takes final decision

**Committee of the Cabinet of Ministers**, attended by person responsible for report

**State Chancellery**

**Ministry of Welfare**

**Social partners**

**Representatives of government and institutions**

**NTCC, which reviews proposals concerning reports of the Ministry of Welfare**

**Information report on opportunities to raise the minimum wage, prepared by Labour Department of the Ministry of Welfare**

**Employers’ Confederation of Latvia**

**Free Trade Union Confederation of Latvia**

**Participation of experts, as needed**

**Proposals and objections – evaluation of report of MW**

**Calculations on possibilities to raise the wages of state institution employees (prepared by Budget Department)**

**Proposal of other ministries to raise the wages of the particular ministry and its subordinate institutions**

**Association of Self-Government participates at least once in three month**

**Information and knowledge 2.**

**Knowledge transformation 3.**

**Main institution 4.**

**Data and research 1.**

Notes: The orange arrows represent the forwarding to the Cabinet of Ministers of the information report prepared by the Welfare Ministry on possibilities to increase the minimum monthly wage. The blue arrows represent the recommendations from relevant partners that are included in the report. The green arrows represent the evaluations of the Finance Ministry with respect to the possibility of raising the salaries of those who work in the state sector.
According to scheme of decision making process on minimum wage increase issues shown in figure 2, hereafter each of the levels as well as participation of state institutions and non-governmental organisations into decision making process will be investigated.

### 3.1. Information basis of documents, its quality and availability

When state institutions (among them – ministries) prepare informational reports and calculations about wage issues, they mostly use CSB data and information prepared by other ministries (for instance, Ministry of Finance calculations on the effect on the minimum monthly wage of the national economy, the database on wages paid to those in the state sector etc.). In some cases, information obtained within studies (surveys) is used. Currently, the communication problems between main “data producer”, CSB, and some government institutions and non-government organisations which is our can be potential users of data exist. As CSB is primary and most frequently used data source in the state, in the beginning, CSB as data gathering and accumulation institution will be examined.

The most frequently mentioned source for statistical information on wages was the Central Statistical Bureau which is one of the major sources of data when the MW and the MF prepare reports and calculations. The CSP data are used by the Ministry of Economics and Association of Self-Governments and, to a lesser degree, the ECL and FTUCL. Other sources of statistical information are used far less frequently. Among foreign statistical data, those of Eurostat data must be emphasised – they are mostly used for comparative analysis by the MW and MF.

#### 3.1.1. Characteristic and usage of CSB data

The CSB correlates some 20 informational programmes (statistical data) which are related to wages. Given the great work burden of employees at the various institutions; there is the risk that employees of institutions have not studied all of the CSP data with respect to wages.

The information on wage and salaries provided by CSB is summarized into issues of publications, for example, “Results of the survey on occupations in Latvia in [date]” (annual), “Main results of Labour Force Survey [date]” (annual). Voluminous information on main indicators on salaries is possible to find in web site of CSB in section “Labour remuneration” “Tables Related to Monitoring of Anti-Poverty Efforts” etc. Each year the CSP prepares a national programme of statistical information which contains information about planned data collection programmes over the next year, both for local needs and for international institutions.

CSB data about wages in Latvia largely reflect legal wages. Information about wages comes from reports prepared by employers and government institutions. Data from other organisations usually indicate higher wages than CSP data do. For instance, CSB data about wages can differ from that prepared by other organisations by as much as 20 to 40%. (Institute of Economics of Latvian Academy of Sciences 2005: 8-13). Such difference is
described within study which has been conducted by Institute of Economics of Latvian Academy of Sciences in order to evaluate implementation of the draft conceptual document “On improving controls over the earnings of natural persons”.

Information from other organisations usually is based on an attempt to determine the true wages that are paid in Latvia, i.e., in addition to official income, the focus is also on ways of understanding illegal wages. In such cases, however, it is difficult to find a point of reference that would help in evaluating the share of results which covers unregistered income and is closer to the real situation than official statistics would suggest. This situation indicates that there are limitations on interpreting the data prepared by the CSB with respect to wages. On the other hand, it is a good thing that the CSB data have a safe and clearly none point of reference. Perhaps CSB statistics in official reports should more regularly been combined with data from ongoing studies such as the labour force survey and the study of household budgets.

When conducting surveys on household budgets and the labour force, CSB representatives have problems in surveying respondents with a high level of income – these respondents are least responsive. This suggests that the lack of such respondents reduces indicators related to household budgets and wages to a certain degree.

The CSB conducts annual calculations about the size of the shadow economy, but these data are not publicly available. Data about the shadow economy are a part of overall GDP calculations. These calculations are the work of the CSB Department of Macroeconomic Statistics and its National Accounts Division. The primary users of the data are the State Revenue Service and the Economics Ministry.

Representatives of government institutions do not take an in-depth look at the quality of data, except in those cases when the data radically differ from other indicators. There is reason for certain doubts about the knowledge of representatives of institutions when it comes to making proper use of the correlated data – definitions of concepts or indicators are often mixed up or interpreted incorrectly. It is said that this is because of a high level of staff turnover at ministries, along with the serious workload that is on the shoulders of stable employees (specialists).

There are no traditions of dialogue at this time between the CSB and data users. There are problems with projects that are commissioned by ministries. Sometimes ministry representatives ask the CSB to come up with more precise data, but the CSB has trouble in fulfilling this request, because insufficient time is given to do the job.

In order to improve the level of quality in the use of CSB data, information that is supplied at this time should be supplemented with brief commentary on the correct use of the data and the major mistakes that are made when people use CSB data. If necessary, seminars should be organised on the use of data.

In order to improve the knowledge of data users about the CSB offer, it would be desirable when employees of government institutions commission data, to make reference to other data collections that cover the same subject (electronic links to these collections should be made available).
3.1.2. Evaluations of undeclared earnings and their quality

The biggest problem for WIF team was to collect information about those sources of information which speak to illegal wages. That is because employees of government institutions are hesitant to speak about these issues. Some surveyed representatives of government institutions said that available data about this subject are questionable, and so there is no good reason to make practical use of such data. Some said that the problem of under-the-table wages has been exaggerated and that the true scope of the problem is insignificant. It should be noted here, however, that no study has ever confirmed those claims. In addition, some representatives said that there is no point in publishing the data, because they would not be of interest to anyone, and there would be no one who would be interested in resolving the problems.

In general, information on „envelope wage“ (under-the-table wages) and shadow economy is used rarely by representatives of state institution. Three main reasons can be mentioned although “Basic positions on steps to be taken to reduce illegal employment” are accepted since 2004.

On of the most important reasons refers to validity of information. Calculations conducted thus far offer different data about the extent of the problem, which causes doubts about the methodology for calculations. Second, there is no reason to believe in the results of the calculations, upon which the application of various political instruments can depend. Generally speaking, ministries and social partners speak of three sources information which provide data about under-the-table salaries and the shadow economy, There are: MF calculations done in 2002; CSB data (they are not available openly, they are located at the National Accounts Division of the Macroeconomic Statistics Department) and the study of Institute of Economics of Latvian Academy of Sciences “On Improving Controls Over the Income Earned by Natural Persons”. None of the surveyed ministry representatives could name all three information sources. Some respondents did not even know where to find the information which they themselves mentioned.

The second reason is that some data about the shadow economy are available for the internal use of a single ministry, and they are not offered to other institutions. It should be noted that calculations about under-the-table salaries are, by definition, hypothetical, but information and calculations prepared by ministries must be based on secure sources of information. Employees of government institutions claim that the quality of information and calculations does not deteriorate to a major degree if data about the shadow economy are not taken into account. It indicates that there is no unified ministry-level programme to fight against the shadow economy in Latvia – a programme that would increasingly suffer from the absence of the aforementioned data. Ministries have done work aimed at reducing the size of the shadow economy within the confines of their own competence. For instance, the burden of direct taxes and social insurance contributions has been reduced to a degree, and the minimum monthly wage is regularly increased. Still, the activities of individual ministries at a time when there is no unified view of the problem among all ministries make it less possible to influence the volume of illegal wages in the national economy in any effective way. Similarly, there has been no assessment of the effectiveness of instruments that have been brought to bear thus far, nor have risks related to the application of those instruments have been studied (for instance, why are the desired results not achieved).
The fact that the shadow economy is not an issue for a single ministry alone and it affects the operations of several ministries may be one reason why ministry representatives have so little interest in the shadow economy and under-the-table salaries in the national economy – no ministry has the direct duty of dealing with the shadow economy and the under-the-table salaries. Basic positions on steps to be taken to reduce illegal employment applies largely to the sub-structures of ministries (the National Labour Inspectorate and the State Revenue Service), and less to the ministries themselves.

All of this suggests that there is little demand for information about the shadow economy and under-the-table wages, and the use of such data in everyday work is negligible. Most surveyed representatives of government institutions and organisations, however, admitted that there are problems with illegal wages in Latvia. It may be that interest in data about under-the-table wages is diminished by the belief among government institutions employees that too much effort would be required to make any significant changes in the situation.

3.1.3. Additional information sources and their availability

When preparing annual reports and calculations, other, additional information sources for representatives of ministries are not available. So far, the amount of studies concerning wages and similar subjects is negligible. The first information source that is similar to statistics is the annual “Fontes Latvija” Ltd. study of wages at large companies. It should be noted that besides wages the study inspects other issues, for instance, wage complementary benefits, premiums, business car, mobile phone, computer etc. This study is used only by Ministry of Finance. The second is a study “On Improving Controls over the Income Earned by Natural Persons” (January 2005) which was conducted by the Economics Institute of the Latvian Academy of Sciences. The study can be found on the homepage of the KNAB, but it has not been used by any of the surveyed government institutions and organisations.

Studies done in other countries with respect to wages – these information resources are used only when wage policies are being developed, i.e., when long-term conceptual guidelines are drawn up on such policies. After the guidelines are prepared and confirmed, the experience of foreign countries is not taken into much account. The only exception is when the situation in Latvia is addressed in a report. In 2002, for instance, the Finnish government conducted a study “Working Life Barometer in the Baltic Countries 2002” (2003). The study can be found at the Welfare Ministry, and the LBAS has used it in its own work.

Currently, low level of abstraction is typical to information (statistical data and studies) which is used for preparation of policy documents and informative papers. In studies (surveys), the data which supplement statistics are obtained. The data of these studies are shown as primary data tables and figures; often, they are prepared without interpretation and applying of statistical analysis.

Before development of national programme “Labour Market Studies”, there has not been national policy in both levels – in whole and on wages issues in separate. The ministries commission research only for their own needs, without harmonising their needs with those of other government institutions or with the results of previous research. This problem indicates that there are communications problems among government institutions. Foreign research of
interest to Latvia is not adapted in Latvia – the aforementioned Finnish study, “Working Life Barometer in the Baltic Countries 2002” focused on the situation in Latvia, and it was used to prepare several information reports. The recommendations from these were approved by the Cabinet of Ministers. At the same time, that study was conducted in 2002, and its data are no longer used because they are out of date. The information from the study is still in demand, but the government does not spend its own money to conduct the relevant research.

3.1.4. Characteristics and usage of information prepared by ministries

Ministries do not summarise data themselves, they conduct comparative analysis, prepare reports, and make forecasts and calculations. Ministries obtain data for the preparation of reports and calculations from the Central Statistical Bureau and from internal databases that are assembled and maintained by institutions that are subordinated to ministries. Some information from internal databases is offered to the CSB, but some of that information is confidential and only for internal use. The status of information is determined by the law and by regulations of Cabinet of Ministers.

Ministry of Finance has two data sets: a database concerning wages paid to people in the state sector and SRS data about payments of personal income tax. The SRS database is primarily meant for the internal use of the MF so as to make wage-related calculations. The MF prepares calculations about proposals submitted by other ministries with respect to increasing the wages of those who work for the ministry and its subordinate institutions as well as calculate the effect on the national budget of an increase in the minimum monthly wage. The Finance Ministry and Economics Ministry are working together on “Basic Positions Concerning Macroeconomic Development and Fiscal Policy, 2006-2010” (Ministry of Finance 2005) which is mostly of a consulting nature. The document is taken into account when the MW prepares its information reports.

The database which focuses on the wages of people in the state sector is not publicly available. The information in the database is meant for internal MF use.

Some SRS data can be obtained in accordance with the law, and those data are posted on the institution’s homepage, but some data are not publicly available. The review of requests for data and the schedule for providing an answer are dictated by the law. The law does not provide for an opportunity that would allow researchers from private organisations to study the data of government institutions, and that, in turn, makes it hard to do the research work, and it hinders any ability to conduct in-depth analysis.

If there is research of national importance with results that would significantly affect national policy (an example of this is the national programme on “Labour market studies”), then the law on taxes and fees should allow micro level data to be released to researchers and scientists who work for private organisations. The law does not permit this at this time. Because employees of government institutions often have limited time resources to do statistical
analysis of the data which is collected, and because there are large volumes of information that is needed for secondary data analysis, the law and regulations should make it possible for private researchers to do that kind of work.

If the law on taxes and fees were to be amended to allow researchers from private organisations to access data from government institutions, that would make it possible for them to conduct more extensive data analysis not on the basis of the data that have been correlated already – these data limit opportunities for analysis – but rather on the basis of micro data about changes in a person’s employment status and paid taxes that would fundamentally expand opportunities to conduct analysis and design conclusions in research that is of key importance in the shaping of national policy. The use of secondary data would also reduce the amount of money that is needed to collect data, it would make it possible to spend more time on analysis, and it would make it possible to repeat research periodically. This would also lead to the use of a unified information base, and that is fundamentally important for various comparisons over a longer period of time.

Then we would make the same recommendations with respect to all areas in which there is data protection at the national level. In national research, private researchers should be allowed to analyse micro level data, because that would make it possible to use econometric and time series methods. These require time, resources and specific knowledge, and so it would be unlikely that the personnel of a single institution could do the job.

Calculations about the effect of an increase in the minimum monthly wage are available in the information reports of the Ministry of Welfare. The reports can be found on the homepage of the State Chancellery. Calculations prepared by the MF for other ministries with respect to wages are available at the ministries which did the calculations. Although the results of MF calculations with respect to the minimum monthly wage are available, there is no information about the calculation methodology used by the MF. Social partners and ministry representatives alike have limited opportunities to evaluate the results of calculations prepared by the Ministry of Finance when it comes to the possibility of increasing the minimum monthly wage, because no information is available about the method of the calculations and its impact on obtained result.

The Finance Ministry should prepare a detailed description about the calculations related to opportunities to increase the minimum monthly wage, and this description should be attached to the research result. Descriptions of the methodology and results of calculations must be made publicly available via the homepage of the National Chancellery, the MF or the MW as an appendix to the information report on the minimum monthly wage. If the FM were to describe its calculation methodology in an understandable way, that would reduce differences of opinion among partners in reaching agreement on the minimum monthly wage. The participation of the aforementioned government institutions will increase when the FM evaluations are accepted, and that will make it possible to discuss forecasts. Over the course of time, the amount of time spent on preparing reports will decline, and there will be greater understanding of the consequences of dealing with the proposals.

The Ministry of Economics predicts the average wage for the future and evaluates the effect of an increase in the minimum monthly wage on business environment. The ME calculations about increases in the minimum monthly wage are available in the information report of the Ministry of Welfare or in annotations attached to the report.
Ministry of Welfare prepares an information report on raising the minimum monthly wage. The data of State Social Insurance Agency are used to learn about existing and potential recipients of the minimum monthly wage. Only some SSIA data are available publicly. Data from some of the aforementioned institutions can be received from the homepages of the relevant institutions and in accordance with the law, while other data are confidential and not available at all.

Information about wages that is prepared by ministries consists only of data which reflect legal wages in Latvia. Ministries do not have access to information about under-the-table salaries, and according to experts, these represent 20-40% of all wages. Exemption is the Ministry of Economics which receives the calculations on amount of shadow economics provided by CSB. Another source, SRS data about violations that have been discovered reflect just a small share of the shadow economy’s effect on the economy, and these data cannot be seen as complete.

In 2002, the FM conducted a one-time calculation regarding the shadow economy in Latvia. These data can now be seen as out of date, but some of the interviewed employees of government institutions cited these data as the only source of information about the shadow economy. This indicates that there is a shortage of information and unawareness of other kinds of information.

The calculations about the shadow economy that were conducted by the FM in 2002 were meant only for the internal use of the ministry which suggests that there is a closed information environment within the institution. The Finance Ministry, commenting on the calculations that were done four years ago, said that such calculations are no longer in the competence of the ministry. Imprecise methods led to results which only partly reflected the true situation, and that, says the ministry, is why the results were not distributed among other interested users. It has to be noted, however, that the calculations were eventually received by other ministries.

Representatives of ministries basically mention two problems which, to a large degree, affect the quality of documents prepared by ministries (the problems here apply not only to the MW and MF, but also to the other surveyed government institutions – the ME, the CSB and the National Chancellery).

The first problem is workload. Ministry representatives who make the calculations, prepare the information reports and evaluate the documents submitted by other ministries have a great deal to work to do, and that has to do with the lack of young specialists and the low level of qualifications among new employees (university graduates have a low level of knowledge). Employees at government institutions also have to prepare a large amount of documentation for European institutions. The consequences to this problem are the following:

- a lack of time to produce calculations and prepare information reports;
- a lower level of quality in some of the documents that are prepared – some that are prepared with respect to wages do not include academically correct references to the source of information that has been used;
- decrease of time to do their basic job and that for evaluating the documents that are submitted by other ministries;
- problems in establishing and maintaining high-quality communications among institutions.
There is a high level of staff turnover at ministries and institutions, and that does not promote the use of specialists. Salaries are the main thing which leads to staff turnover – it is believed that in most cases, wages are not competitive with those paid in the state sector.

The consequences to this problem are high level of staff turnover makes it difficult for government institutions to ensure that the level of knowledge among employees is increased and preserved which, in addition, burden activities of state institutions in other several aspects. There is an increased risk that the preparation of reports and calculations may become a routine with the goal of doing all of the work on time. The lack of time and the high workload means that employees of government institutions have limited opportunities to engage in critical evaluation of existing information sources about the relevant subject and to find new ones. There is also an increased risk that sources of information that are well known but not always the most appropriate ones will be used, as well as attitude towards used sources and expressed opinions becomes uncritical gradually.

To serve above mentioned problem, competitive wages and career opportunities should be offered to new and existing specialists. A positive example in dealing with the problems of employment at government institutions is a new wage plan designed by the Finance Ministry that was approved by the Cabinet of Ministers on December 20, 2005 (Cabinet of Ministers 2005c). It speaks to the wages of those in the state sector. The aim is to offer competitive salaries to those who work in the state sector so as to reduce staff turnover.

3.2. Cooperation of social partners and order of decision making

The National Tripartite Cooperation Council is made up on the basis of parity by the Cabinet of Ministers, the Employers’ Confederation of Latvia and the Free Trade Union Confederation of Latvia.

The Council reviews concepts, programmes, draft laws, draft Cabinet of Ministers regulations, and other draft normative acts when these apply to issues that are of economic importance. The Council files recommendations with the relevant ministries on how these documents could be improved. The National Tripartite Cooperation Council meets to discuss wages at the initiative of the Ministry of Welfare. The Council is assembled to talk about increases in the minimum monthly wage, and this is required in Cabinet of Ministers Regulation No. 413. Other wage issues are not reviewed by the Council.

3.2.1. Decision making at National Tripartite Cooperation Council

The State Chancellery receives reports prepared by the Welfare Ministry on opportunities to increase the minimum monthly wage and then sends these out to the relevant partners – the Finance Ministry, the Economics Ministry, the Latvian Association of Local Self-Governments, the Employers’ Confederation of Latvia and the Free Trade Union Confederation of Latvia, and the meeting of state secretaries.
Institutions that are involved in National Tripartite Cooperation Council meetings to discuss increases in the minimum wage include not only the Welfare Ministry, but also the Finance Ministry, the Economics Ministry, and the Policy Co-ordination Department of the State Chancellery. These ministries and departments must prepare their evaluation of proposals made by the MW in seven days’ time after receiving those proposals. This is required by law. Where there are disputes, the issues are resolved at meetings of the National Tripartite Council. If agreement cannot be reached by the Council, the issue is next considered by the meeting of state secretaries and, if necessary, the Committee of the Cabinet of Ministers.

After receiving evaluations, the State Chancellery sends recommendations filed by other ministries and organisations back to the Welfare Ministry for additional evaluation. Once this is done, the Welfare Ministry, with the help of the State Chancellery, summons a meeting of the National Tripartite Council and one of the meetings of state secretaries to deal with any disagreements that have occurred. Once the final version of the report is designed, the State Chancellery makes sure that the report is in line with the Constitution, the law, and the regulations of the Cabinet of Ministers. Then the report is sent to the Committee of the Cabinet of Ministers or the prime ministers. The State Chancellery takes minutes at meetings and maintains the minutes and reviewed documents in its own database.

When speaking about participation of social partners within decision making process on increase of minimum wage, it should be noted that the FTUCL has weak influence in the taking of decisions. Only some of Latvia’s labour unions are a part of the FTUCL, and that reduces the organisation’s influence. The reason relates to norms in the law which say that in the case of strikes, representatives of various sectors are not allowed to ensure solidarity.

Social partners make use of only some of the data offered by the CSB, and some social partners did not know that the CSB has an electronic database. Social partners have better knowledge on information that is available at ministries and previous studies on wages conducted in Latvia; and it is due to work done by the State Chancellery. Social partners find it hard to evaluate the calculations of the Finance Ministry, because the ministry does not offer explanations about its calculation methodologies and relevant factors. The FTUCL has agreed with the Bank of Latvia on alternative calculations when assessing increases in the minimum monthly wage.

There are no strong traditions of dialogue and partnership among social partners, and that leads to mutual complaints about a lack of co-operation. The ECL, for instance, is accused of trying to deal with certain issues in bilateral negotiations with ministry representatives and without the participation of the FTUCL in the dialogue.

Although government institutions do not have extensive resources to develop the sector of non-governmental organisations, further work should be done in enhancing the competence and co-operation of employers and labour unions. Social partners must be more actively involved in the activities of ministries, the CSB and other institutions. They should receive information about the available information resources which are put to use by government in the taking of decisions. Social partners, for instance, could be invited to attend CSB seminars. It would be advisable for the FM to prepare a detailed description of the methodology which it uses in its calculations so that users of the calculations do not have to duplicate the MF functions. The advantage of alternative calculations is: in case of different results, partners should try to find compromise that can result as improvements of calculation method used by Ministry of Finance.
The more social partners are involved in the discussion of decisions, the less opposition there will be when it comes time to implement those decisions. There will be fewer arguments, and the civil society will be strengthened. Even a formal involvement of social partners in the taking of decisions and the improvement of knowledge will enhance the understanding of social partner with respect to that which is happening in the country. There will be more effective design of proposals.

3.2.2. Decision making at the government level

State secretaries meet to talk about wages if agreement has not been reached by the NTCC or if agreement has to be reached with the Latvian Association of Local Self-Governments. The state secretaries review draft documents and information reports with respect to which there has been no full agreement during the process of harmonisation. The goal is to reach agreement before the documents are forwarded to the Committee of Ministers.

According to Cabinet of Ministers rules, the Latvian Association of Local Self-Governments is represented at meetings of state secretaries and at meetings of the Committee of the Cabinet of Ministers. The Latvian Association of Local Self-Governments does not, however, participate in the work of the Tripartite Council. The Latvian Association of Local Self-Governments is charged with evaluating MW reports on increasing the minimum monthly wage. The process is based mostly on the budget needs of local governments. Local governments receive income from the personal income tax – 75% of those tax revenues are transferred to local government budgets, and the higher the minimum wage, the greater the income which local governments receive in that way. If the sum of income that is not taxed is increased, however, local governments face higher spending. Local governments also have to spend more money if the salaries of people who work for local government institutions have to be raised.

When the minimum monthly wage is raised, the Latvian Association of Local Self-Governments calculates the effect of this process on local government budgets, but similar calculations are conducted by the MF. Latvian Association of Local Self-Governments representatives have said that their calculations are not in line with those of the ministry, and this situation makes it difficult to take decisions. Differences in the calculations can be attributed to two factors – either different data are used, or there are different methodologies. Dialogue is the only way to resolve this problem. Both sides must describe their methodology and disclose their data and data sources. Then a mutually acceptable method of calculation can be determined.

The Committee of the Cabinet of Ministers consists of all of the members of the Cabinet, and its meetings are meant to reach agreement on issues and to prepare draft legal acts or information reports. It decides on the disposal of documents – approval (without objections, with objections), refusal, postponement or rejection.

Each document is thoroughly reviewed at Committee meetings, and all aspects of approving a report are debated. When there is imprecision, it is eliminated, and that is why the Cabinet of Ministers usually approved draft legal acts and information reports that have been approved by the Committee without any further debate. During Committee meetings, specialists from
various sectors have a chance to discuss all relevant issues and to help in harmonising views with an eye toward taking a decision.

The Committee of the Cabinet of Ministers deals with the issue of the minimum monthly wage only if state secretaries have been unable to disagree at their meeting or if the Latvian Association of Local Self-Governments wishes to present additional views. The same procedure applies to documents prepared by other ministries which include the MF’s wage calculations – the Committee of the Cabinet of Ministers reviews these only if no agreement has been reached at the meeting of state secretaries. The final decision to confirm or to reject proposals of ministries on wage issues is made by the Cabinet of Ministers.

3.3. Recommendations for improvement of information circulation

Performance of the State Chancellery – in most cases, its work was praised. Representatives of government institutions wish that the State Chancellery should establish a centralised database of information that is at the disposal of government institution also designing unified policies for research among the various ministries.

WIF research team observed that the main problems which led the surveyed respondents to make the proposals. First of all, employees of ministries have problems in finding information about research done by other ministries and the data which are the result of this work in the area of wage issues. Representatives of institutions, when preparing reports, have problems with finding alternative information resources – data and research provided by independent institutions. Second, the government does not have a unified policy on research, and that is made clear by the overall lack of research about problems that are important in the state. For instance, there has been no research to look at employment, the shadow economy and wage issues. The lack of research was mentioned by representatives of institutions and social partners alike.

It must be noted that the aforementioned research subjects were included by the Welfare Ministry in its new research programme, but there were complaints about the idea that guidelines for the research were not harmonised with social partners or representatives of other ministries. There is a possibility that these complaints indicate the specifics of the cooperation culture of the potentially involved institutions. These do not always have to do with the actual activities of the institution to which the complaints have been addressed, or with the interruption in information flows that is the result of staff turnover.

Observations by researchers suggest that government institutions have trouble in finding documents that are important for researchers, because the relationship between mandatory documents and those other documents which emanate from these is unclear. Government institutions, for instance, have problems in finding documents which emanate from the Lisbon Strategy or the National Development Programme. Similar problems exist with other documents – hierarchical relations are not defined. In order to solve above mentioned problems, database of documents and studies (research) is needed.

WIF research team suggests developing database which includes information on studies (research) which are important to the state and that is used in designing politics. In database,
not only ad hoc survey should be included, but also statistical information provided by Central Statistical Bureau (for instance, annual results, or, if possible, quarter results). Similarly, it is important to separate different surveys which improve statistical data and analytical or research papers which investigates and describes regularities. First case is surveys which results are shown within primary tables and figures. Second case is studies which includes statistical (or econometric) analysis of the results and contains description of regularities.

General suggestions for development of database are as follows:

- set priorities for the flow of information in the database so that the hierarchy can be seen and there is not an excess of information;
- add key words to documents for searching studies with help of programming (for instance, with words “wages”, “undeclared work” etc.);
- set up a mechanism which allows relevant institutions to order necessary information from the new database, along with descriptions of that information (references, data tables) and, if necessary, instructions for use;
- establish and co-ordinate mechanism for the regular updating of the information in the database;
- organise seminars about the effective use of the new database for institution representatives and relevant partners.

The State Chancellery should set up an electronic scheme of hierarchy in terms of the most important documents related to relevant areas such as the Lisbon Strategy, listing the ministerial documents that emanate from each of the documents at the top of the hierarchy. The same applies to the National Development Plan, etc. Documents which are in force and documents which have expired should be listed. A mechanism is needed which would allow institutions to note in a timely way that necessary information is missing and to check whether that information cannot be found within the internal work of other ministries. This applies to the State Chancellery and the secretariat of the minister with special portfolio for E-government.

Within period of research implementation, the State Chancellery presented information on database of studies and publications. WIF team tried to use the database, and it must be said that some of the research was not available electronically. In that case, someone who wants to look at the results of such a study has access to nothing other than information about the institution (ministry) which commissioned it. It would be useful, therefore, to include references at least to the division or department which has the research. If anybody is interested on results of study, he/she will have no information on contracting authority and availability of data is burden – it will take too much time to extract the data.

Although the database contains information on institution (contracting authority), there is no information on contractor. Similarly, the information of implementation of the study is more useful that date of reception in database. If the results of studies are available electronically, their form varies; and it complicates their extraction. For example, MS Word document can be opened on screen immediately; however, other reviews of research are available as archive files. It seems that for purpose of usage, possibility of choose type of a file of the results is needed. Although the titles of potential studies have been included into database, their status is unclear – whether budget is assigned for the study and it is prepared to be implemented or the study is on any stage of its implementation.
IV EVALUATION OF THE WAGE REGULATING METHODS

Application of different instruments for wage regulation depends on state social and economical policy. It can be rather liberal or rather socialistic; and it depends on state development vision and priorities. Currently, social policy implemented by government of Latvia is liberal one; and there are used some of instruments of income regulation. Within framework of WIF research, following instruments were analysed more detailed – minimum wage, labour taxes and tax relief (including untaxed minimum). In order to investigate opinions of employees, focus group discussion method was applied. In its turn, opinion of employers was investigated using both methods – that of qualitative and quantitative.

4.1. The evaluation of minimum wage and untaxed minimum

Minimum wage and untaxed minimum is the instruments which implementation can affect workers earnings, especially those of low-paid occupations. An optimal amount of both – minimum wage and untaxed minimum – is frequent theme of public discussions recently. The objective of this chapter is the analysis of opinions of both parts – employees and employers.

4.1.1. The impact of statutory minimum wage and untaxed minimum

The main policy instrument mentioned by all participants of WIF research focus group discussions in which national policy affects remuneration are: the minimum wage and the untaxed minimum. Participants knew that both of these indicators would be increased as of 1 January 2006. Although the minimum wage and the sum of untaxed income are increased from time to time in Latvia, participants in those groups with low and middle-level income think that the situation is still not appropriate for Latvia’s situation.

Only those in the group of people with lower income, however, were there a stable sense of possible alternatives, and those who spoke to alternatives did so only with respect to the untaxed minimum. They repeated an idea which has been heard in public – that the untaxed minimum must be equal to the minimum subsistence level in Latvia, or around LVL 100. In this context, some respondents pointed out that the minimum wage is also below the minimum subsistence level.

“The untaxed minimum has to be raised, at least to Ls 100. Then taxes will be lower. […] What kind of minimum is it anyway – if I received that money […] – Ls 26 [discussion was happened in the year of 2005], that is ridiculous.” (Low income, female, LV, outside Riga)

Employees think that government decisions to increase minimum wage impact their remuneration in two ways. In private sector, government decisions influence earnings if an
employee officially receives a sum which is close to the minimum wage. Then if the minimum wage is increased, employers increase only the official part of the salary accordingly. The part of the income that is paid unofficially does not change – “If someone receives the minimum wage on paper, then from the New Year, that person will receive LVL 5 more”.

Government policy is felt more directly by those who work in public sector. Depending on changes in the minimum wage and other regulations which have to do with the salaries of those who work for such institutions, salaries are occasionally reviewed.

Asked about decisions taken by national institutions in the area of labour law, employers offered laconic and general answers, rarely speaking of concrete decisions. Asked about specific changes to labour law, they were most likely to speak about changes which affect their specific area of operations. It is also noted that as of January 1, 2006, the minimum wage and sum of untaxed income were both raised.

Typically, a higher level of competence is found among managers of large and medium-sized companies and their representatives when it comes to government decisions in the area of labour law. Employers who represent micro companies have the lowest level of competence in this area. Some respondents could not cite any changes to the law. That may be because larger companies have employees who are specifically charged with monitoring changes in labour law and other national policies which have to do with business and the relevant sector. They inform company management about these changes. Quite commonly these are bookkeepers, company lawyers or personnel managers.

At small and micro companies, the manager performs numerous functions – they are often the company’s director, lawyer, bookkeeper, rank-and-file employee and janitor, all rolled up into one. Information about changes in the law is received by such people indirectly, and when they have to perform several functions simultaneously, they have less time to monitor changes in the law.

Asked to talk about gains and losses related to changes in labour law, employers said that these are usually focused on employees, not employers, although employers have to make sure that the changes are implemented.

“The problem is that the changes always affect employees, not employers and businesspeople. All of the changes relate to additional money that is needed to implement them.” (Riga, services, large enterprise)

No employer could mention a single benefit attached to changes in labour law. It is important to note that in discussing changes in the law, employers talked about their own companies and based answers primarily on the interests of their firm.

Changes in labour law are defined as problems because most employers and their representatives say that changes usually create additional difficulties and require greater investments, irrespective of the size of the company in question.

Employers had different things to say about the way in which increases in the minimum wage affect wages. At companies with a higher rate of productivity (these are usually large or medium companies, as well as small businesses in specific sectors), employee wages exceed
the minimum wage, and so a raising of the minimum wage does not have any influence on the salaries of employees, and employers have no need to find more money to pay wages.

Another common explanation for why increases in the minimum wage do not have any effect on salaries is that there are different principles and strategies for setting wages. For instance, if a salary is based on the amount of work that is done, then it is usually above the minimum wage. What’s more, the amount which the employee receives is then more dependent on his or her own productivity. The same is true when people do piecework and are paid on the basis of that.

At companies with lower productivity and turnover, by contrast, people are often paid the nationally dictated minimum wage, and so occasionally salaries have to be raised irrespective of whether the employer does or does not have the relevant financing. This situation is found most commonly in micro companies.

At those companies where some or all of the employees receive the minimum wage, increases therein have a positive effect on wages, but they also have a negative effect on company operations as such. This is particularly true among small and micro companies, which are seriously impacted by any changes to the law which require additional resources on the part of businesses.

Some of the managers of small and micro companies say that increases in the minimum wage are a good thing, because the wages of their employees go up, but there are those who have negative things to say about the matter – they still have to find additional money for the wage fund irrespective of their turnover or productivity. These employers do not think that they should increase the price which they charge for goods or services, because that would mean a reduced market share and lower turnover.

In looking at what employers have to say about increases in the minimum wage, we must differentiate between two different effects:

- a neutral or positive effect on wages (with employers usually saying that the employees of their salaries go up along with increases the minimum wage, although given the rate of inflation which prevails in Latvia, the actual increase is negligible);
- a negative effect on turnover and development (micro company directors say that their operations, their chance for further development and the number of people they can employ are all impacted negatively).

### 4.1.2. Optimal amount of minimum wage and untaxed minimum

The data of employers’ quantitative survey show that about a half of Latvian enterprises employs workers who receive minimum wage; however, at most cases, their amount is up to 20% from all number of employees at particular enterprise. In wholesales, retail trade, hotels and restaurants, amount of workers receiving minimum wage is considerable higher. Without reference to kind of activity, it is typical for micro and small (up to 19 employees) workers as well.
It should be noted that honesty of employers on level of wage at enterprise is would be lower than that of employees in another survey. Therefore, the results obtained into employers’ survey reflect the data of accounting in a greater extent. The aim of WIF research here was to obtain employers’ opinion on potential results of minimum wage increase.

Within employers’ survey of WIF research, approximately 90% of respondents considered that minimum wage should be increased. These respondents were asked to mention the appropriate level of minimum wage in Latvia. Most of employers mentioned sum up to 300 lats, while some of them denounced considerable higher amount.

Excluding those who suggested a minimum wage above 300 lats, the median of the minimum wage was 160 lats. The amount of optimal minimum wage and their distribution by various categories of employers varies a lot. Figure 3 shows answers of employers on minimum wage that depends on region and kind of economic activity.

Figure 3 is divided into six bars, each of them presenting the answers from one particular statistical region of Latvia. The name of the region is seen on the right from the bar. On the left of each bar, there is a measurement scale of lats, with the help of which the data in the bars can be read – the optimal size of minimum wage named by entrepreneurs. The amplitude of the measurement scale is 100 to 300 lats. Each bar contains answers of employers depending on the field of national economy of the enterprise. The field of national economy is indicated at the bottom of the table – in the bottom line. Figure 4 is formed analogically. It shows the amount of taxed minimum named by employers.

Each “box” and “tail” of the figure 3 (vertical line drawn upwards and downwards from the top of the box) shows the range of responsibility of employees. The bigger (higher) the “box” is and the longer the “tails” are, the more various the responsibilities of entrepreneurs are. The smaller (narrower) the “box” is, the more unanimous the answers are. The horizontal line in the middle of the “box” is a median or midpoint – a value above and below which there is an equal number of answers. Numeric value of the median can be read in the left side of the image.

In general, the most unanimous opinions on desirable amount of the minimum wage are seen among employees of Latgale – the most part of answers are placed close to the median in all fields of activities. The greatest diversity of answers was observed in the regions of Riga and Pieriga. In these regions, desirable minimum wage differs the most in the fields of agriculture and production, construction and trade, hotel service and catering services as well as in the fields of individual services. Probably these differences in opinions depend on the size of an enterprise – in Riga and Pieriga there are many large enterprises near which small and micro enterprises exist.

The lowest minimum wage median in Riga is in the field of construction, in the suburbs – in the sectors of state administration and production. In Vidzeme and Kurzeme the employers of all the sectors named approximately the same desirable minimum wage. In Zemgale the lowest minimum wage was named in the sector of construction, but in Latgale – in trade, hotel and catering service and in the sector of individual services.
Figure 3. Employers’ offered minimum wage range depending on region and kind of enterprise economic activity

What should be the monthly minimum wage in Latvia?

Type of economic activity (grouped)

Note: Figure shows distribution of ranges in quartiles (the individual points relate to observations that are significantly different from those of the relevant group). The central section of each graphic’s horizontal segment corresponds to the median of the minimum wage. If the upper or lower quartile is not seen, then it coincides with the median – in the construction industry of Kurzeme, for instance, there were seven observations, of which three were between LVL 100 and 150, while four employers stated a sum of LVL 200.

The results of regression analysis on factors affecting amount that employers consider to be the optimal minimum wage are shown in table 3 of the appendix. There were statistically significant differences in terms of the desired minimum wage in comparison to employers in Kurzeme, who stated a sum that was 12% lower, as well as in comparison to employers in Zemgale and Latgale, who cited sums that were 22% and 21% lower, respectively, than the sum which was proposed by employers in Riga. The differences among regions which are close to Riga is not significant.

Employers who are owners or co-owners of their company proposed a minimum wage that was 10% lower than the wage proposed by upper level managers. Employers with more than 250 employees proposed a minimum wage that was, on average, 11 – 12% higher. Employers who hire part time employees or contractual employees said, on average, that the minimum wage should be 5 – 6% lower than the sum which was cited by employers with no such employees.
If proportion of basic wage was below 41 – 60% of total workers compensation fund, then offered minimum wage was 9% lower than in cases if proportion of basic wage was above 60%. Those employers whose companies correlate information about the overall supply and demand of labour in their relevant sector proposed a minimum wage that was 8% lower, on average, than the sum offered by people from companies which do not collect such information.

Before the question on optimal minimum wage, employers were asked to evaluate whether significant decrease of employees is possible if minimum wage will increase. Potential influence should be evaluated in connection with minimum wage of 2006 which was 90 lats gross. Amount of minimum wage increase on 10%, 15%, 20%, 30% or 50% was mentioned. Respondent was asked to name increase up to which level would raise necessity to decrease the number of workers at enterprise.

Most of employers (89%) recognized that, in the case, significant decrease of workers would not expected, while 5% of employers indicated that number of employees would decrease. Significant differences among regions, kinds of economic activity and size of enterprise are not observed.

In general, the majority of employers admit that growth of the minimum wage even by 50% (i.e. up to 135 lats) would not cause relevant decrease in the number of employees, regions and fields, the employers from which named the lowest desirable minimum wage, would suffer the most. A swift growth of the minimum wage would influence the most the small employers of Kurzeme and Latgale.

Spontaneous responses given by employers indicate that increases in the amount of income that is not subject to taxation do not have much of an effect on company operations and employee salaries. Wages increase in that case, but the changes are too small to talk about any significant positive changes in the overall size of salaries. Employers say that increases in the amount of untaxed minimum basically improve the situation of employees.

Alike in case of minimum wage, employers were asked to evaluate an optimal amount of untaxed minimum. Within quantitative survey, approximately 90% of employers consider that untaxed minimum should be increased as well. The median of the untaxed minimum, as stated by employers, was 90 lats. Range of values was rather wide (see figure 4).

Figure 4 shows the answers of employers about the desirable untaxed minimum depending on the region and field of activities of an enterprise. Each statistical region is depicted in its own line. In the right side there is the name and in the left side – measurement scale that enables to read the untaxed minimum in financial terms. The groups of fields of national economy are named in the last line of the image. The altitude of the “box” and the length of the “tail” show the range of answer variations of employers. In the figure 4, we can see that a relatively wide amplitude of answers are given in the fields of state administration, education and health care, but in Riga, Pieriga and in the regions of Vidzeme and Zemgale – also in the sectors of trade, hotel and catering service and individual services. A comparatively greater unanimity in all the regions can be observed in the fields of transport, communication, finance mediation and commercial services as well as in the sector of construction.

The results of regression analysis on factors affecting amount that employers consider to be the optimal untaxed minimum are shown in table 3 of the appendix. At other equal conditions,
managers of large enterprises (those of more than 500 employees) have mentioned optimal untaxed minimum to 13% higher. If respondent’s owner of an enterprise then offered sum is by 18% lower; if it is bookkeeper – by 8% lower, on average. Optimal amount of untaxed minimum in Latgale is lower that in other regions – on average, it is lower by 14%.

Figure 4. Employers offered untaxed minimum range depending on region and kind of enterprise economic activity

Note: Figure shows distribution of ranges in quartiles (the individual points relate to observations that are significantly different from those of the relevant group). The central section of each graphic’s horizontal segment corresponds to the median of the minimum wage.

When proposing higher minimum wage, employers offer higher untaxed minimum as well. Approximate proportion of both figures is similar to the concept of the government – the untaxed minimum is about 50% of minimum wage.

4.2. Evaluation of labour income taxation

A second major way in which the government affects earnings is indirect. It is government policy concerning applying a personal income tax and social insurance contributions.
Employees, participants of focus group discussions of the research feel that the main reason for official and unofficial wages is the tax policy of the state. On one hand, it is said that the state facilitates the system, because the tax burden on companies is very significant. On the other hand, employees are prepared to work for the wages which they receive, because they think that it is better to receive more now than to hope for an “unknown future”. Respondents do not feel secure about their future or their lifespan, and so they are interested in receiving more now so that they can deal with important needs. This does not, generally speaking, encourage people to think about their future prospects.

“This is reality. You hurt yourself if you receive the wage under the table, but on the other hand, I don’t want to lose that much money in taxes.” (Medium income, male, LV, outside Riga)

“Taxpayer money just disappears. MPs travel all around the world; they take decisions which lead to Latvia having to pay millions in fines.” (High income, male, LV, Riga)

During the discussions, it has been pointed out that the average lifespan of Latvia’s residents is below the retirement age, and it is expected that as the demographic burden becomes more severe, the retirement age will be raised. These are two key arguments which respondents use to speak about motivations in paying the social insurance contributions – “I won’t live that long anyway”. Comparatively less often respondents spoke of the fact that people who make the social insurance contributions have access to unemployment and sickness benefits. The opposite argument is that “I can’t afford to be sick”.

“The average lifespan in Latvia is 63 years, the retirement age is 65. Why the hell should I pay the social tax if I won’t live that long according average statistics?” (High income, male, LV, Riga)

“In foreign countries they pay the social [contributions], but there’s a guarantee of benefits later – my kids, if not me. What happens here? Will I even live long enough to get a pension? And yet I’ve been paying the social [contributions].” (Low income, female, LV, outside Riga)

In quantitative survey of fulltime employees we asked a question for what part of the employee’s remuneration taxes were paid, by dividing answer variants in twenty percent intervals. Although it is possible that the quality of respondents’ answers might be affected by several side-factors, for instance, fear to admit that taxes are paid only for a part of wage, however, while analysing interconnection between employee’s wage value and part of wage the taxes are paid for, several interesting regularities were discovered.

In order to verify the assumption that additional effect on wage depending on relative amount of paid taxes is observed, we estimated regression model with included variables that characterized for what part of employee's wage taxes were paid. Comparing employees working in one profession group and one economic activity sector for which taxes were paid in amount of 41 – 80% from wage, statistically significant relationship was found that wage of these employees was by 13.4% higher. Even higher benefit in terms of remuneration the employee gets if taxes are paid in amount of 41 – 60% from wage (it is by 20% higher than wage of reference group).

If taxes are paid in amount of 0 – 40% from wage, possible positive effect on wage was smaller and its statistical significance did not meet the required criteria for data analysis of
this research. Possibly, in this situation wage is affected by contradictory effects. Taxes paid in amount of 0 – 40% include also those employees who do not have a contract of employment. If employee does not have a contract of employment, his wage is lower by 9.3% than analogous employee having a contract of employment (and having at least partial tax payment). Thus, we can assume that the statement that employee without the contract gets higher wage at the expense of unpaid tax is delusional. It is possible that employee without a contract of employment can not find a job, for instance, because he does not have necessary documents or due to any other reasons.

Analysing opinions offered in the qualitative research, we can assert that employees are not negatively biased towards tax payment in general but rather towards tax amount as it is considered that taxes in Latvia are too high. It should be admitted here that employees’ attitude towards taxes deducted directly from wage derive from several factors.

First of all, there are subjective feelings about tax rates, particularly among those who are paid lower salaries. This is based on the idea that the size of the gross wage is perhaps acceptable in terms of the individual’s ability to satisfy his needs (and often these are key physiological and existential needs). Then respondents look at the difference between the gross and the net wage and see that their ability to satisfy even the most elementary needs deteriorates, and then they believe that taxes are an excessive burden, given the life situation which prevails.

Second, there is the idea that the principle of justice is ignored, and that leads people to think that the tax burden is excessive. The principle of justice in the public arena would be manifested through convincing information to suggest that all taxpayers are the same before the law.

Third, some respondents argued that the spending of tax revenue is not sufficiently justified. Researchers found that overall knowledge among the residents of Latvia is at an inadequate level when it comes to this issue.

“The crazy thing is that we poor people pay the highest taxes. The budget is based almost entirely on our taxes. The lower and middle classes supplement the budget, not the rich people.” (Medium income, female, LV, Riga)

Most respondents are aware of the personal income tax rate in Latvia and have an overall sense of how much of their gross wages are deducted – approximately 30% of the wage goes to various taxes. Some employees know precisely that the social insurance contribution is divided up among the employee (25%) and the employer (9%).

The view exists that money paid in taxes (personal income tax and social contributions) all goes to the social budget and has to do with one’s future pension. These and other comments suggest that people do not have enough understanding of the difference between the personal income tax and the social contribution.

The study also shows that most employees are not convinced of the effectiveness of tax collections, and they are not sufficiently informed about what is done with the money that is collected. This creates additional dissatisfaction with the tax system in Latvia. It is possible, therefore, that if people were to believe that taxes are collected and supervised in an effective way that would encourage people to refuse illegal salaries.
Most respondents are generally aware of available personal income tax allowances and possibilities to reduce taxable income in Latvia. It seems that women are more informed than men and they have a greater interest in taking advantage of the tax relief that is available.

Although the aforementioned kinds of tax relief are in place, attitudes toward them tend to be quite negative. Participants of focus group discussions said that the sums that they recover through the tax relief are too insignificant to feel that they really are examples of relief.

Some respondents who had already taken advantage of the opportunities said that they are positive processes and that they are satisfied with the results. A comparatively larger group of respondents had insufficient knowledge about how to recover overpaid personal income tax, and so they had rejecting or at least cautious attitudes. Presumably, reasons for a distanced attitude vis-à-vis tax relief and possibilities to reduce taxable income are approximately the same as reasons for a distanced attitude vis-à-vis the tax system as such. In addition, there is the fact that getting a reimbursement requires a great deal of effort in comparison to the gains that are made. In calculating the benefits in actual sums, taking into account the time that is spent in collecting documents, in proving expenditures, and in filing papers with the State Revenue Service, respondents mostly think that the balance between benefits and effort is, in most cases, inappropriate.

It is also talked about sense or personal experience that the process of filing documents to receive tax relief is quite complicated and that State Revenue Service employees are not very responsive. Because the sums for which people wish to recover overpaid personal income tax are not too significant, many respondents think that the procedure keeps people from going through the process.

“Given the sum on the papers and the fact that the education tuition was not astronomical, [the sum that can be recovered] is ridiculous. I’m sorry of the time that I wasted.” (High income, female, RU, Riga)

“The situation in our country is that there is tax relief, but people have themselves to blame if they don’t take advantage of it. There’s no information about it.” (High income, male, RU, outside Riga)

“For a working person to get the relief – it takes so much time that it’s better just to waive the reimbursement. It requires a great deal of time, and the criteria are unclear. One person gets the money, the other doesn’t.” (High income, male, RU, outside Riga)

“I’ve never had any problems [in getting the reimbursement]. No queues, nothing of the kind. I was sick for a long time, I had no insurance. I paid a lot of money for everything. I decided to recover the money so that I get back at least a little bit of what I pay in taxes. (Low income, female, RU, Riga)

Some respondents expressed concern about the idea that if someone has tried to recover overpaid personal income tax, then the next time the State Revenue Service will take a closer look at that person and carefully monitor the way in which taxes are paid. In that case it is possible to face an administrative punishment quite quickly, and so it is better to refrain from seeking the reimbursement of the overpaid personal income tax.
Respondents in the discussions expressed the assumption that lower tax rates would reduce the incidence of salaries paid under the table. Another way of legalising compensation would be rules which insist on official and examined income, because income has everything to do with the amount of support that is received (for maternity, etc.), and with the ability of one to take out a loan. If income were always examined, employees would be less likely to agree to unofficial payments, they would insist on an official wage. We should admit that currently in most cases allowances depend on employee’s official wage from which social insurance contributions are made.

The things which employer say indicate that the way in which national tax policies affect wages and company development depend in large part on the size and turnover of each company. Representatives of large companies say that taxes do not, generally speaking, cause problems, they say that they obey all relevant norms. Managers of such companies also think, however, that the overall position taken by employers is that taxes in Latvia are too high, and this, in turn, has a deleterious effect on the rate and scope of company development.

Among managers of medium and small companies, one hears the view that company development depends less on tax policies and more on the company’s own activities, the extent to which employees are motivated, and the extent to which productivity can be enhanced. It seems that many employers have made peace with the fact that they cannot really influence national tax policy. In the answers given by directors of micro and small companies, one encounters a certain sense of fatalism – “What can you do? You pay what you have to pay”.

“Generally speaking, this is the government’s attitude: Everyone who does business is a tax evader, and everyone should be shot”. (Outside Riga, services, medium enterprise)

Managers of micro and small enterprises think that the worst tax policy influences enterprise of their size because tax rates are common for all despite of turnover. When analysing the experience of companies vis-à-vis the way in which national tax policies affect their development, it is indirectly possible to come up with a few assumptions about individual factors which, in this context, promote the payment of illegal, under-the-table salaries.

Representatives of large companies always say very openly and directly that they obey tax laws and regulations. Directors at medium and some small companies, however, often tend to be evasive when asked about the way in which tax policies affect wages. Answers are not always direct or specific, with respondents instead speaking of other factors which influence wages and company development. This suggests that there may be problems at these companies when it comes to obeying tax laws.

The most evasive answers came from some directors of small and micro companies. These respondents often expressed anger, disgust and desperation over the difficulties which occur if tax laws are obeyed scrupulously. Respondents who admitted that not all tax laws are followed were all representatives of small and micro companies. This allows us to conclude that small and particularly micro companies have the greatest problems in obeying tax laws. In order to reduce the overall tax burden, therefore, some employers, as can be judged from the interviews, evade taxes by paying some employees under the table.

Some businesspeople say that the government’s tax policies favour large, not medium or small companies. Respondents also say that the institutions which oversee business do not
encourage trust in the government. When company representatives seek consultations from the State Revenue Service on unclear tax-related issues, for instance, what instead happens is that the agency sends inspectors to the company, and the firm then gets punished.

Analysis of these qualitative data does not allow us to generalise, but it does seem that under-the-table salaries are paid more often at micro and small companies outside of Riga. Some respondents, in talking about the possibility of under-the-table wages, said things which showed that they do not know much about the personal income tax rates. In those cases when it was declared that salaries are paid under the table, the respondent could not name the rate precisely. In such situations, however, respondents typically say that this is a major problem in Latvia and that there are lots of companies which pay salaries under the table.

Most employers, when asked about how the personal income tax affects wages, said that the net wages of employees decline considerably. In some cases, it is said that a lower tax burden would mean higher wages. The personal income tax rate has not been changed for a same time, while social tax contribution rates were lowered a few years ago (only employers’ part as well).

Often it is the demand among employees for competitive wages which encourages tax evasion even if the employer is otherwise prepared to pay all taxes. This is most often true at companies where wages are based on the amount of work that is done or on piecework (in the construction industry, for instance). Wage funds can vary in terms of the proportion of taxes paid officially and unofficially, i.e., with respect to the share of wages for which taxes are paid.

Among employers from micro companies, a commonly stated view is that employees are not interested in paying the personal income tax. Employers say that employees receive their money and do not think about paying taxes – they just know their net wage. If the state were to raise tax rates, employers would cover the additional costs, but it would not have an effect on the amount of wages. In other words, changes in tax rates are viewed negatively by employers, because they hinder productivity and the development of companies.

“Taxes are a burden, what else can you say? But they don’t impact upon wages, because the worker doesn’t care how I pay the taxes – he needs to eat, doesn’t he? He has to pay his electric bill at home. Taxes are my problem, employees don’t care”. (Outside Riga, services, micro enterprise)

Some employees particularly lower-level ones often feel no motivation as a result of the fact that their employers make social tax contributions and personal income tax on their behalf. Such employees would often prefer a higher wage to the social guarantees which are being ensured.

There are also different situations – ones in which employees are interested in social guarantees, thus promoting the payment of official wages at the company. It has to be added, however, that employee demands in this context are not one of the key factors in promoting limitations on the payment of under-the-table salaries. Data show that it is more likely that this is affected by turnover, stability and the motivations and abilities of the employer to obey the law.
V IMAGE OF SOCIAL PARTNERS AND THEIR IMPACT EVALUATION

Economic security needs person relates to guaranteed work, insurance against accidents, and guarantees that biological needs will be satisfied (Omārova 1996: 105). At places of employment, this can be ensured by guaranteeing work and wages, health insurance and a pension fund. The sense of human security is also threatened by dependency on someone else. That creates concerns that the other person will force the individual to do things that are independent of the individual’s own desires. This is why labour unions have been established – their aim is to defend the interests of members (Praudze, Belčikovs 2001: 343). Alike organisations of employers establish – they are necessary to protect interests of other side.

Depending on level of organisation, labour unions and employers’ confederation can be powerful non-government organisations which, according to Labour law, can negotiate on work conditions at particular enterprise or even in whole industry. In Latvia, at enterprise level, sides can assign collective agreement, at industry level, general agreement can be signed. One of possibilities of the collective agreement is contract on more favourable salary, for instance, to state that minimum wage is higher than national minimum wage.

Currently, labour unions of different industries exist in Latvia most of which are united into Free Trade Union Confederation of Latvia (FTUCL). Associations of employers are united into Employers’ Confederation of Latvia (ECL). Both organisations participate in National Tripartite Cooperation Council representing interests of employees and employers. Activities of these organisations and their reflections into public sphere construct particular image. If it is positive, the image can help to organisation when engaging new members and influencing decisions of the government. If the image is negative or unsaid, then activity of organisation can be burden.

Thus, agreement between employees and employers organisations is one of additional factors which can influence the level of labour income. Within this chapter, the image and the results of actions, namely, impact on wage, of both social partners will be investigated. WIF team will pay more attention to labour unions instead of organisations of employers. It is caused by two reasons. The first one refers to history of trade unions – organisations of employees existed in soviet times and, possibly, their image is inherited. The second reason refers to possibilities to measure both factors – participation of an employee within labour union and wage level isolating the impact of labour unions from other factors.

The image of labour unions are described using qualitative research methods – results of employees’ focus group discussions and employers’ in-depth interviews. Within framework of WIF research, quantitative description of image of labour unions is not necessary – the arguments on participation and diversion of perception should be shown there. The impact of labour unions on earnings will be analysed using econometric methods; within employees’ quantitative survey, questions on existence of labour unions and collective agreement at enterprise have been asked.
When consolidating association of employers, Employers’ Confederation of Latvia is the “core”. Further, the image of ECL is analysed. It is characterised using the data of employers’ in-depth interviews.

5.1. Evaluation of impact of labour unions

The basic objective of labour unions is to protect employees and to provide them better work conditions. Time to time mass media inform about strikes in other European Union member states where labour unions of certain sectors protest against certain decisions of government or employers. When initiating the research, WIF team posed an assumption that the social image of labour unions maintains the features acquired during soviet time and that employees lack information and understanding about the role and potentialities of labour unions in market economy conditions, inter alia in the process of wage agreement. Therefore we considered that the image of labour unions mentioned above precludes involvement of employees in labour unions.

We verified the mentioned assumption by applying qualitative research, namely, using standpoints and percept acquired in discussions of employees’ groups which were also supplemented by standpoints of employers the results of which are currently described in separate review of results.

When investigating opinion of employees, we have seen that employees in the Latvian labour market feel unprotected. In all respondent groups people said that employees themselves are the only defenders of their rights (“just you yourself, tooth and nail”) or they are fully unprotected (“employees have no rights”). Participants were aware of the fact that there are government institutions which are supposed to oversee the extent to which labour rights are observed. Most respondents spoke of the State Labour Inspectorate (SLI), as well as courts to which employees can apply for help. The SLI is not seen among respondents as an institution which can really help when labour rights are violated. Negative attitudes are based on personal experience and that of friends and acquaintances. Respondents mentioned cases in which employees asked the SLI for help but received none. Respondents complain that the inspectorate has too formal an approach to matters and in fact has no real interest in achieving results.

“The State Labour Inspectorate, but it sends someone over only if a brick falls on my foot.” (High income, male, LV, Riga)

“If you tell them that Labour law is being ignored in relation to employees or that you’re dissatisfied about something at work, then they take a look at the labour contract and the salary. You can get a court to reinstate you at work, but anyone will understand that there will be no job for that person anymore.” (High income, female, LV, outside Riga)

“You can approach government institutions which deal with labour disputes, but you have to prove the evidence. It does not work – later you’ll get sacked.” (Medium income, male, RU, Riga)
“We understand that this is the situation, but we don’t go and defend our own rights.” (High income, female, LV, outside Riga)

Although there is distrust in government institutions, it also has to be said that employees themselves are not always prepared to fight for their rights. Employees admit that they do not have enough knowledge and information about their rights and about Labour law. A fear of losing one’s job also does not encourage people to defend their rights in unclear situations.

Employees in the private sector are more likely than those in the public sector to encounter actions on the part of employers which are out of line with Labour law. Because they do not want a conflict with employer, they do not approach government institutions for help. Instead, they try to resolve their problems on their own.

In this context, labour unions are not mentioned as organisations which could realistically help employees to defend their rights. Among employees who have not encountered any actual labour union activities, the view prevails that they cannot help people to defend their rights in labour situations. Employees’ association with concept “labour union” are shown in Figure 5.

**Figure 5. Employees’ associations with concept of “labour union”**

- **Protectors of employee interests**
  - Defend employee rights; there is some defence; a guarantee that your rights will be observed; they monitor observance of contracts and the law.

- **Functions of social protection**
  - Legal assistance in a dispute; invitations to Christmas parties for the kids; support if you’re sick or there’s a funeral.

- **Not active defenders of employee rights**
  - They yell a lot but accomplish nothing; we don’t have labour unions. In foreign countries, they’re active in protecting employee interests and achieving their aims, but not here.

- **Heritage of the past**
  - My associations from youth – they’re of no importance, there were treatments and travel, but they’re something of a Soviet heritage – you’re just supposed to pay the money.

Associations with the concept of labour unions constitute four contradictory sets of opinions (see figure 5). On one hand, it is mentioned that labour unions protects interests of employees, as well as offers social protection. On the other hand, it is mentioned that currently labour unions cannot provide their functions and defend rights of employees. Separate group of opinions constitutes perception that these organisations are “old fashion” or it is memories from the soviet time.

Opinion of employee is influenced by his/her experience in a great extent. If labour union does not exist at workplace, the opinion that there are no labour unions in Latvia dominates. However, theoretically, the necessity of labour unions is admitted. If labour union exists at workplace, opinion of employee depends on fact whether it has been protected their members and covered some results. In such case, opinions varies – part of employees think that they do not feel actions of labour unions, other note that labour unions perform functions of social
protection and some employees tell about situations in which labour union has been overtook significant result.

It is considered that there are industries which have active labour union, for instance, labour unions of seamen, teachers, medicine personnel are mentioned. If results of employees’ survey of WIF research are investigated, 28% of respondents say that labour union exists at their enterprise. The results show that labour union works more frequently at large enterprises and in a public sector. The larger enterprise is, the higher is possibility that labour union exists there. The difference between public and private sectors is seen clearly. Labour union exists at approximately 58% companies of public sector workers, while that is only for 14% of private sector workers.

Knowledge of employee does labour union exist at their company or not depends on group of occupation to which he/ she belongs. The higher is position of employee at the company (middle level manager, professional or associate professional), the more frequently he/she admit that labour union exists at company, as well as the smaller proportion of “hard to say” answers. Existence of labour union at workplace varies from 54% (professionals) to 16% (service workers and shop and market workers). There are two reasons for such variation of answers.

The first reason is concentration of particular occupations in certain industries. For instance, teachers and medicine personnel correspond to group of professionals and associate professionals, as well as belong to public sector. The second reason is possibility that low-qualified workers do not know about existence of activities of labour unions.

When returning to opinions expressed within focus group discussions, in general, the opinion dominates that labour unions do not exist in Latvia or their activities is too weak. It is needed leader or several leaders in order to promote labour union activities in Latvia.

“In practice, when “easing out” had started in municipalities, trade unions did not help. Who should leave departments, they did. The collective agreement had existed, but all lost at court. Trade union was too weak against political situation. There is no sense. Politics is stronger that anything else.” (Medium income, female, LV, Riga)

“In a private company, those who are in a labour union are sacked immediately”. (High income, male, LV, Riga)

When summarizing opinions on trade unions, there are four obstacles of their work in Latvia:

- Incredibility of employees that anything will change;
- Fear of employees to lose their job and the short-term benefits of under-the-table salaries;
- Persistent opinions from Soviet times;
- Opposition of employers to labour unions at their companies.

Following opinions of employees about the image of labour unions, we should note that one of the strongest links is with the soviet time. Although we can not declare that it is the main reason why Latvian employees do not join labour unions, the link of activities of these associations with the soviet time is considerably stronger than possible and expected associations with activities of powerful employees’ organizations in the European Union.
countries, for instance, with information on employees’ protests in Sweden or France which appeared during implementation of the research.

During discussion, several employees noted that survival of labour union in the enterprise since soviet time is the reason why it exists and functions, as it is easier to maintain the existent than to create organization from the first. However, in general only part of employees considers that labour unions are necessary in Latvia in order to fight for their rights more successfully; other employees do not need them.

“The fact is that relations between employees and employers in Latvia are insufficiently regulated. A lot depends on personal reasons, on the activities of the employee. We’re afraid of unemployment and lower wages, so we’re inactive.” (High income, female, RU, Riga)

If we consider that the proof of active activity of labour unions in work place is collective agreement with employer on working conditions and possibly the remuneration, then it was important to analyse the percept of employees not only about the labour union but also about collective agreements and their necessity. We should notice that during group discussions this link developed spontaneously – as one of the answers on question about image of labour unions.

Respondents had different levels of information about collective labour agreements, most often speaking to links between the agreements and labour unions – “there is a collective agreement where there is a labour union”. Those who work for companies where there are collective labour agreements had more information about them. Some respondents had heard nothing about any such thing. Those employees with a collective agreement speak positively about it, mentioning various benefits that are set out in the agreement and are thus received by employees.

Within employees’ survey, the question on existence of collective agreement at enterprise was asked. Approximately 27% fulltime employees admit that the collective agreement exists. Alike existence of labour union at enterprise, the collective agreements are more frequently signed at large enterprises (especially if number of employees is greater than 250), as well as public sector.

Those employees with a collective labour agreement speak positively about it, mentioning various benefits that are set out in the collective agreement and are thus received by employees. Usually, they are: regular premiums, additional payments and non-financial benefits, for instance, health insurance etc.

[If there is collective agreement] Then employees can make demands and employers don’t have the right to act as they please, they can’t sack anyone. That’s really necessary.” (Low income, female, RU, Riga)

Part of employees working in private sector consider that all their as employees’ requirements and rights are included in individual contract of employment therefore they do not see any necessity for collective agreement. In other cases, employee does not see any benefit from concluding collective agreement, because overall he feels quite helpless in communication with employer who can use his own discretion.
Considering rather sceptical attitude of employees towards labour union ability to improve conditions of employees, WIF research team has decided that it is important to verify the labour union effect on employees’ wage by econometric methods, i.e., by using regression analysis. For this purpose, WIF employees’ survey data was examined if the labour union activity had significant effect in working place of employee and if the collective agreements had significant effect on wage. Employees in WIF research were asked the respective questions about presence of labour union and collective agreement in the working place.

The regression analysis shows that the labour union activity in working place of respondents does not have significant effect on employees’ remuneration and this causation is not significant in any of subgroups of analysis as well. However, it appeared that collective agreements have significant impact on salary. Like it was mentioned before, salary included not only basic wage but also perquisites and premiums. As participants reported in the group discussions, regular premiums or perquisites as well as other complementary benefits (for instance, health insurance etc.) are usually provided in collective agreements.

It was observed that in cases when collective agreement was concluded in working place, earnings of employees was by about 5.8% higher than in working places where such agreement was not concluded. This result is derived from situation if we compare employees working in one profession group and one economic activity sector with and without collective agreement in working place. In this case, significant effect of collective agreement on male wage (by 9.5% higher) has been observed but it has no significant effect on female wage. The presence of collective agreement increases wage of employees in the public sector by 6.2%, yet it has no significant effect in the private sector. Similar tendency is observed regarding employees in cities and countryside – collective agreement has significant effect only on wage of citizens (by 7.0% higher). More detailed review of effect of collective agreement on wage is given in table 5 of the appendix.

Comparing to other studies where the positive effect of labour union in wage has been described (Antila, Ylöstalo 2003: 118-9), WIF research team concludes that activity of labour union can substantially affect employees’ wage only if collective agreement is concluded. If collective agreement is not concluded in the enterprise, labour union is too powerless to achieve some tangible result or its presence in the enterprise is formal.

When inspecting the opinion of employers, it should be admitted that part of employers does not have opinion on that issue. Associations of other employers are shown in figure 6.

Opinions of employers can divide into several groups. Part of employers thinks that labour unions represent employees and they are necessary for that reason. Other notes that in practice labour unions do not exist in Latvia or, in some cases, they are not real representatives of employees. Employers who have not heard about labour unions during last years remind about soviet times and activities of labour units then (see figure 6).

When comparing associations of employees (see figure 5) and those of employers (see figure 6) with concept “labour union”, it is seen that the opinion of both groups is quite similar. Both employees and employers think that labour unions should protect theoretically or they protect in practice the rights of employees and act as mediator within negotiations with employer. In addition, both groups point that activities of labour union are weak for the last ten years.
The third common group of perceptions consists of references to soviet times and experience of those times. Several employers were workers at the soviet period; therefore this reference is logical – that is their only experience in cooperation with labour unions. In contradiction to employees, part of employers is sceptical towards motives of participation in labour unions thinking that they can be selfish.

“A labour union is like a big scoop of ice cream. (...) It offers happiness, like for children. It suggests that there is justice in the world, although in truth there is no justice, and there never will be justice.” (Riga, services, large enterprise)

“I don’t feel labour unions as a separate force in Latvia, and the establishment of labour unions in our area of business is a very distant matter.” (Riga, retail, small enterprise)

The need for a labour union at a company is affected by company size – the larger the company, the greater the justification for labour union operations. At small companies, employers see no need for a labour union. That is particularly true among the representatives of micro companies. It has to be added, however, that respondents from large companies, too, are often sceptical about the point to labour union activities.

The role and activities of labour unions also depend on the area in which a company operates – the private or the public sector. Employers believe that the influence of labour unions is small or non-existent in the private sector, while in the public sector they are of comparatively greater importance and have greater chances to affect the situation in the company’s area or sector of operations.

Some employers say that labour unions are useful instrument at large companies in promoting communications between employers and employees. Labour unions are unnecessary at small and micro companies, because employers can discuss problems with each employee individually or in a group.
“At so small a company – what kind of labour union? Conflicts are always resolved through discussions.” (Outside Riga manufacturing, small enterprise)

“At small enterprise, worker can come to me and speak about his/ her problems. And we speak about and try to find any solution. At large enterprises, nobody can reach employer so easily and, theoretically, labour union is that which can do something and fighting. May be it does, but, according to my experience, it did not anything.” (Riga, sales, small enterprise)

“A labour union is needed, because that’s an organisation which speaks to the employer in the form of organised dialogue.” (Riga, services, large enterprise)

Employers think that labour unions are justified in certain sectors and professions which employ lots of people. In that case labour unions represent the interests of a large number of people – teachers, builders, medical personnel, etc. In narrower sectors and at small companies, there is no justification for labour unions activities. Also, there are various organisations which offer an alternative to labour unions and can be used to express views and defend interests and rights – professional associations, copyright agencies, etc.

Although regression analysis show that labour union affects earnings at enterprise, it does have to be said that in the so-called large sectors (medicine, education), respondents from such sectors were more likely to be sceptical about labour unions, arguing that labour unions have little influence on the decisions which are taken by government institutions.

Employers have little information about labour unions and their activities. One reason for this is that there is a lack of experience in working with labour unions. Directors from large and medium companies have more information, while directors from micro companies have much less knowledge. Some of these have no experience with labour unions at all. Company directors and their representatives had the following things to say about the possible and desirable functions of labour unions:

☑ identifying the problems of employees at large companies;
☑ informing employers about these problems;
☑ organising dialogue between employers and employees;
☑ influencing national tax policies on behalf of employee interests.

Most employers see no need for labour unions and cannot think of any advantages in co-operation with them. This may be because of a lack of information, the negative image of labour unions, and the fact that people have little experience with them. This thinking is found more typically among the representatives of micro companies. Employers did not, however, cite any significant shortcomings in terms of potential co-operation with labour unions.

Labour unions have few real opportunities to facilitate the observation of the rights and interests of employees. One company representative said that labour unions cannot propose any constructive solutions to problems; they can only offer social or psychological assistance.

One of the main accusations levelled by employers against labour unions is that their activities are formalities. This view applies to Soviet-era and present-day labour unions alike. It may be that associations concerning the Soviet era have an effect on the image of labour unions today.
The successes of labour unions, according to employers, depend on the true interests of those who work for them. Some employers said that labour union members use the organisations in their own interests, to facilitate growth in their public or political career.

“To me this is something like a starting line for people who go into politics, and I don’t believe that their goal is really to protect employees. Rather, these are the personal or popular goals of these groups of individuals.” (Riga, services, micro enterprise)

“There are no leaders, there are not positions at the national level, there is no influence which (...) really resolves issues. (...) There is little in the way of civil education and responsibility, people are insignificant – they do something, but without any real effect.” (Riga, services, large enterprise)

Employers admit that activities of labour unions will be more successful if they outgrow the level of single enterprise and unite employees of particular industry.

5.2. Image of ECL and evaluation of their impact

The second social partner which image and evaluation of impact has been analysed with the method of in-depth interviews is Employers’ Confederation of Latvia (ECL). All in all, the image of the ECL among employers is indistinct. There are two major groups of ideas here:

☑ ideas which are based on information about the LDDK and on cooperation with it;
☑ ideas which are rooted in the assumptions of respondents.

As a public organisation, the Employers’ Confederation of Latvia brings together smaller organisations and associations of employers, as well as a few major companies which are of significant importance in the Latvian economy. As a result, small and medium companies have no direct contacts with the organisation, and analysis of the data suggests that they do not have the capacity to demonstrate any interest in taking part in the work of public organisations. Data from the interviews, thus, suggest an entirely logical trend – the amount of information that is at the disposal of employers about the Employers’ Confederation of Latvia depends on the size of the company. The highest level of competence and information is found among the directors of large companies. The level among directors and representatives of small and medium companies is very low, indeed. People representing micro companies usually don’t know anything at all about the Employers’ Confederation of Latvia.

“It can present the views of employers to people who have the right to take decisions. When new laws are drafted, for instance, it can make sure that the views of employers are taken into account. (...) It is an intermediary between the law and the employer.” (Riga, services, large enterprise)

Employers who have experience in working with the Employers’ Confederation of Latvia spoke of the following areas of activity and the following functions for the organisation:

☑ serving as an intermediary between employers and the state;
☑ solving problems which are important to employers (including problems with the law);
defending the interests of employers in relations with employees or their representatives (labour unions).

Employers also spoke of the possible or desirable functions of the Employers’ Confederation of Latvia, and these can be seen as the main categories which determine the organisation’s image:

- providing consultations to employers (a possible and desirable function);
- influencing the legislative process (a possible and desirable function);
- influencing national tax laws in favour of the interests of employers (a desirable function);
- harmonising the interests of employers and employees (a possible function);
- helping employers to find and hire employees (a possible function).

Most employers, except those from large companies, had problems in describing their views about the Employers’ Confederation of Latvia, because they know nothing about the organisation. Answers were more in the way of guesses that are based on the name of the organisation.

Employers from micro companies had the biggest problems in characterising their views about the Employers’ Confederation of Latvia. Even if the businessperson was a member of the association of employers in his or her sector, and even if that association was a part of the ECL, the respondent was likely to have little information about the agency.

Employers from large companies have the clearest sense of the Employers’ Confederation of Latvia. That is largely because some of the employers from large companies who were interviewed are members of the confederation themselves. These respondents were able to describe the main areas of activity of the ECL and the goal of dealing with the problems of employers.

In some cases employers think that the Employers’ Confederation of Latvia is an organisation which helps employers to find employees – a goal which is not, at this time, included in the organisation’s statutes. In this context, the ECL’s image is negative – respondents are sceptical about whether this kind of organisation really can contribute anything positive to their companies.

In terms of the level of competence which employers have about the Employers’ Confederation of Latvia and the size of the companies which respondents represent, most employers think that the ECL has a minimal influence on the decisions of government institutions and that all it can really do is make recommendations.

Company directors who have no experience in working with the ECL are particularly sceptical about the abilities of the organisation to have much of an effect on the situation of employers and to resolve their important problems. Given the different interests which people from large and small businesses might have, this scepticism must be seen as appropriate in the current situation.

Difficulties to name particular results of Employers’ Confederation of Latvia have also met by those employers who have information about organisation and its activities. Those employers who work with the ECL say that the confederation can, at least to some extent, satisfy the expectations of employers.
Employers have little in the way of experience when it comes to direct co-operation with the Employers’ Confederation of Latvia. Even those employers with information about the organisation mostly said that they have not worked with it in any direct way. Representatives of large companies were more likely to have such experience. One of the main reasons for the lack of co-operation between employers and the ECL is that the sector in which the relevant company works has its own association, and it works to represent the interests of employers in the relevant sector.

Employers also have little motivation to work with the ECL for several reasons:
- employers do not really believe that the ECL can influence laws in accordance with the interests and needs of employers;
- the believe that the agency cannot affect the situation of employers in the private sector;
- employers work with their sector-based associations, and these have a better understanding of specific issues;
- ECL does not really ask employers to work with it;
- employers lack of time;
- ECL locates in Riga (this was mentioned by respondents outside Riga).

“If they could protect us in some way from higher taxes (..) given that we are a small company and don’t have much income.” (Outside Riga, services, micro enterprise)

All associations are based in Riga. (..) I’m not denying that perhaps they’re necessary, but it’s impossible for them to influence us directly and vice versa. (Outside Riga services, medium enterprise)

They couldn’t help us. In the private sector, the boss of a company has the last word on everything, and the state cannot intervene. The same is the case with organisations of this kind. (Riga, services, micro enterprise)

A lack of experience with and knowledge about the goals, operations and functions of the ECL – this explains why most employers couldn’t talk about advantages or shortcomings in relations with the confederation. Typically, and in line with the lack of ideas and information, most employers were sceptical about the idea that there are advantages to working with the ECL.
VI REMUNERATION FORMS AND WAGE STRUCTURE

Work can be rewarded in several forms. It can be fixed or variable basic wage, premiums and perquisites and miscellaneous other benefits. Although it is a compensation for employee’s effort and contribution, at the same time it can stimulate an employee to exert more to perform work. Entrepreneur is interested in productive employee; therefore he attempts to create wage system that would stimulate employee to work more fruitfully. For this purpose, employers offer to employees not only fixed and constant wage, but also relate at least part of wage to certain productivity indicators. Not always complementary remuneration is in financial terms. There are several reasons why employer may offer to employees non-financial remuneration or so called wage complementary benefits. The objective of this chapter of WIF research review is analysis of wage system and offered complementary benefits existing in Latvia.

Within the framework of the chapter, firstly, the structure of wage fund will be observed, by determining proportion of wage share in total wage fund. This information has been obtained during quantitative survey of employers. Similarly, the effect of different characteristic factors of enterprises on wage proportion was observed. Secondly, monetary remuneration forms the most common of which is basic wage complemented by various perquisites will be described. Here results of fulltime employees’ and employers’ quantitative survey obtained within the framework of WIF research will be compared.

Thirdly, significant role in WIF research is allocated to analysis of non-monetary remuneration. Standpoints of both employees and employers about each non-monetary remuneration form, its granting motivation and amount of employees’ benefit will be observed in the review.

6.1. Structure of workers compensation fund

Employers are interested in low labour turnover, by holding in enterprise stable, highly skilled, experienced, loyal and motivated employees, who promote efficiency of enterprise with their work, increase its turnover and profit. Moreover, at present in some spheres of activity of enterprises there are difficulties to find and attract appropriate employees. Usually employers deal with these problems by offering possible complementary benefits to the respective employees. Complementary benefits can be miscellaneous – both monetary (premiums, perquisites and overtime payment stipulated by the Labour Law etc.) and non-monetary (health insurance, service car, paid catering, coverall, support or allowances for receiving some service).

The structure of workers’ compensation fund is observed from the point of view of basic wage proportion in total remuneration. Its proportion is comparatively easy to describe as fixed or constant basic wage is a prevalent wage form. Date of employers’ quantitative survey show that most often basic wage constitutes the major part of total workers’ compensation fund in enterprises, however, under the influence of several factors, for instance enterprise
size, proportion of wage in total workers’ compensation fund diminishes leaving larger share to wage complementary benefits (see figure 7).

**Figure 7. Proportion of basic wage in total workers’ compensation fund in 2005**

![Graph showing the proportion of basic wage in total workers’ compensation fund in 2005.]

Note: The results of employers’ survey of WIF research, excluding “hard to say”.

In Latvian enterprises whose realized wage policy affects total indicators of the state to a larger extent, in 2005 basic wage in most cases constituted more than 71% of total remuneration. In almost one third of enterprises wage proportion in total workers’ compensation fund varies within 81-90% limits.

Basic wage share up to 70% of total remuneration was in about 20% of enterprises. In enterprises having up to 100 employees, basic wage ratios in 2005 were mutually similar. The data analysis shows that depending on basic wage proportion in total workers’ compensation fund, Latvian enterprises can be divided in two groups. Large basic wage proportion in total remuneration is specific to comparatively small enterprises (up to 99 employees). In comparatively large enterprises (more than 100 employees), basic wage proportion is smaller. Effect of different factors on probability of basic wage share in total workers’ compensation fund is represented in table 4 of Appendix.

Basic wage made whole wage fund in 16% of enterprises. More often such situation can be found in commercial, hotel and public catering and individual service sectors (in 22% of sector enterprises basic wage makes whole wage fund). Similarly, it is more frequently specific to Zemgale (in 35% of enterprises of the region basic wage makes whole wage fund) and Latgale (28%).

Employers usually offer all kinds of benefits to employees at all levels, but the experience of employers, as reported to the researchers, is that more extensive benefits are received by higher-level employees. These are quotes from the interviews with employers which clearly illustrate the motivations of employers and their representatives when they award benefits.

“If the person does good work, then he receives something. That depends on the quality of the work.” (Outside Riga, manufacturing, micro enterprise)
“Bonuses are mostly received by specialists in specific categories which seem unique to our company – such specialists, along with senior management.” (Riga, services, large enterprise)

“The first factor is that the wage alone does not keep the employee in place. If there is just the wage, then it is much simpler for the employee to jump ship to some other company. If he wants to do so and he has to think about losing everything else – the company car, insurance and many other things – then it becomes much harder to take the decision.” (Riga, services, micro enterprise)

“If you see that the person is doing good work, is looking for new solutions, is investing time (...) then the desire can be encouraged by offering materials stimulation. Benefits of various kinds are awarded.” (Riga, services, small enterprise)

The results of employers in-depth interviews shows that the most important factors in determining the range and volume of benefits awarded to employees are: the level/category and specific job of the employee, the amount of work that is done and the quality of that work the company’s productivity and turnover and the size of the company. The main reasons for offering additional benefits are: employees are motivated in a positive way and it helps to keep stable, highly qualified, experienced, trustworthy and motivated employees at the company.

6.2. Amount and forms of monetary remuneration

The compensation form used most often is financial remuneration; however, conditions of payment can be different. More or less, wage can depend on productivity (linked to the results of work). Different kinds of remuneration are investigated into this chapter.

6.2.1. Comparison of wage based on WIF research and CSB LFS

While describing Latvian wage system, WIF research team compared the results acquired in the research with the statistical data available in the state for the respective period. The objective of comparison is to describe observed differences in wages between official statistics and result acquired by independent research organization, considering generally known assumption about considerable proportion of unregistered remuneration in wage amount in Latvia and precaution of employees to disclose their real wage amount in researches related to state institutions.

In WIF quantitative research, fulltime employees aged 18-64 years were interviewed excluding high-level managers, owners of enterprises and self-employed persons if it is the main employment form of these persons.

The fulltime employees in WIF research are: employees who have paid employment and consider that they work fulltime load. It should note that to representatives of separate
occupations, such as teachers, fulltime load corresponds to less number of hours. In such case, the determinant elimination criterion of respondents was his individual time perception, i.e., if the person admitted that he worked fulltime load then he was asked to participate in the research and answer the questions of our prepared survey. For purposes of comparison, Labour Force Survey data of 2005 provided by Central Statistical Bureau was used.

The objective of Labour Force Survey of the Central Statistical Bureau (CSB LFS) is to get detailed information about situation in labour market and economic activity of population in Latvia. The survey is performed by interviewing persons at age 15 – 74 living in households.

Labour Force Survey includes larger part of population than it is necessary for correct comparison with WIF quantitative survey of fulltime employees. In order that the results of both surveys are comparable, their populations should be defined equal to the utmost. Otherwise it is possible that observed differences in distribution of answers of the interviewed is a result of discrepancy of populations. For this purpose, that part of respondents which corresponds to WIF employees’ survey population, i.e., fulltime employees at age 18 – 64, were selected from Labour Force Survey excluding high-level managers which we defined as subcategories 1.1 (legislators and senior officials), 1.2.1 (corporate managers) and 1.3 (general managers) of Occupational Classifier. More than 7000 employees were selected for comparison.

In order to get information on average wage levels in 2005, the respondents of WIF fulltime employees’ survey were asked a question about average monthly net wage of principal work within last 12 months. Such subject formulation in principle allows comparing data with statistics; however it should be considered that only the last month’s net wage is asked in Labour Force Survey.

**Figure 8. Comparison of NET wage of the data of CSB LFS and WIF research in interval form**

Note: Wage of principal work is shown in the figure excluding premiums and additional payments. WIF survey interval range is 0 - 70 LVL, LFS: 0 - 73 LVL.
Figure 8 shows the results of comparison of the net wages of WIF employees’ quantitative survey and CSB LFS (LFS 2005). Wages are grouped into intervals because data of LFS are available as interval observations. They are fully comparable except for lower wage interval which was not possible to summarize equivalently. In WIF employees’ survey the lowest average wage interval was from 0 to 70 lats but in CSB Labour Force Survey – from 0 to 73 lats. In the latter case, the upper margin of wage interval (73 lats net or “on hand”) corresponds to the minimum wage fixed by the government in 2005 after employee’s state social insurance obligatory contributions and personal income tax are subtracted from it.

While reading the figure, we can see that although wage intervals in WIF research tend to be higher than the results of LSF, the general wage interval distribution tendencies are equal in both surveys. In general, excluding the highest and the lowest wage intervals, the arithmetical mean of their midpoints in WIF research is by about 9% higher than it is in CSB LFS.

The wage of almost 10% of fulltime employees is at the minimum wage level or below it (below 70 lats – in WIF research; up to 73 lats – CSB LFS). The average net monthly wage in principal work of about one fourth of employees is in interval from 101 to 150 lats. LFS presents comparatively larger proportion of employees whose net wage is smaller than 100 lats, whereas fulltime employees have shown higher wage in WIF research – more respondents have mentioned wage corresponding to intervals from 101 to 150 lats, 151 to 200 lats and 201 to 300 lats.

The comparison of wages for private sector employees is shown in figure 9; that for public sector – in figure 10.

The official statistical reports show that wage at the level of minimum wage fixed by the government is characteristic to the private sector and it is assumed that the employee working in the private sector gets part of his wage informally. Figure 9 shows that in CSB LFS measuring, about 60% of fulltime employees in the private sector get wage up to 150 lats “on hand”, while in WIF measuring about 50% of employees receive wage in these margins. These differences of respondent number distribution across wage intervals are observed up to the margin of 300 lats. Excluding the highest and the lowest wage interval, the weighted arithmetical mean of their midpoints in WIF research is higher by about 12% than it is in CSB LFS.

The remuneration differences noticed in the chart could be explained, firstly, by unregistered employment existent in the state. Although the results obtained in our research indicate considerably higher real net wage, we can not claim that this research discloses all unregistered employment. Presumably, separate factors of survey organization hinder to obtain such information. For instance, respondents were interviewed at place of residence and after standard working hours (on working days – from 18:00 till 21:00, on holidays – from 10:00 till 21:00), however unregistered employment is related also to overtime job, as a result respondents might not be met at their place of residence during the survey.

Search for employment further from domicile could be characteristic to unregistered employees. During work these people are housed in temporary residences, for instance, service hotels. In accordance with survey standard, service hotels are not included in the rout of interviewer; therefore employees housed therein are not interviewed. That means that although during the survey we have obtained more complete data on wage in Latvia, the unregistered employment part might be represented insufficiently.
The comparison of net wage in public sector shows that the data of both surveys are the same in practice (see figure 10).

The results show that despite of different sampling method used by WIF employees’ survey and CSB LFS, the comparable results are obtained within WIF research, which improve current information substantially. If wages of public sector employees where illegal labour income does not exist in practice have been measured the same, it confirms the possibility of
comparison of the results. Wage differences of private sector employees show potential specific weight of non-declared remuneration in Latvia.

6.2.2. Forms of financial remuneration

Almost all employees surveyed in WIF research answered that in principal work they had higher or lower guaranteed (fixed) basic wage. In addition to that, part of wage consists of variable wage portion, perquisites and premiums.

The employers’ survey shows (see figure 11) that certain differences exist also in payment of basic wage. Firstly, in most cases (~90%) employees get fixed basic wage; however in about 40% of cases it is complemented or even fully replaced by variable basic wage. Secondly, fixed or variable basic wage is related to employee’s qualification – the higher is employee’s qualification by employer’s subjective criteria, the greater is possibility that this employee will get fixed and not variable basic wage. Thirdly, fixed wage is related to size of enterprise. In micro and partially small enterprises (up to 19 employees) fixed basic wage is paid more rarely than in other enterprises (more than 20 employees). In setting variable wage, no variations depending on enterprise size were observed.

When setting wage amount, about two thirds of enterprises (69%) follow calculated or gross wage, whereas 27% agree with employees on net wage amount. Following net wage is specific to private sector enterprises – in this way 35% of private sector and 11% of public sector enterprises are dealing. The results of employers’ in-depth interviews showed that wage received on hands for some employees is more important than wage payment manner and tax payment. Thus, it is reasonable to assume that part of enterprises using net wage as a benchmark, to more or less extent might evade tax payments for their employees.

One fifth of employees surveyed in WIF research admitted that they received perquisites in their principal work for results of individual work which included percentage of enterprise profit, execution of a monthly plan etc. and fewer admitted that they got irregular premiums that could be granted as remuneration according to their merits. Those were followed by perquisites for extra hours worked which also included remuneration for overtime work, work on holidays etc.

The employers’ quantitative survey shows that in terms of prevalence frequency next wage category is perquisites for overtime work followed by irregular premiums. Perquisites for overtime work more frequently refer to middle and low qualification rather than high qualification employees. We should note that in employers’ evaluation both overtime work payment and premium prevalence is larger than reported by employees.

Most often, premiums are granted in enterprises (34% of enterprises) followed by regular premium system – annual, semi-annual, quarterly premiums (17 – 20% of enterprises). Although results of employers’ deep interviews indicated that highly skilled employees receive premiums more often, results of quantitative survey did not confirm this hypothesis (see figure 11).
**Figure 9. Forms of financial remuneration and their distribution divided by qualification of worker**

<table>
<thead>
<tr>
<th>Remuneration Form</th>
<th>High qualified workers</th>
<th>Medium qualified workers</th>
<th>Low qualified workers</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed basic wage</td>
<td>86</td>
<td>76</td>
<td>78</td>
<td>89</td>
</tr>
<tr>
<td>Variable basic wage</td>
<td>23</td>
<td>35</td>
<td>28</td>
<td>39</td>
</tr>
<tr>
<td>Monthly, quarterly premium wages</td>
<td>15</td>
<td>16</td>
<td>15</td>
<td>17</td>
</tr>
<tr>
<td>Semi-annual, annual premium wages</td>
<td>19</td>
<td>18</td>
<td>17</td>
<td>20</td>
</tr>
<tr>
<td>Irregular, other premium wages</td>
<td>33</td>
<td>32</td>
<td>30</td>
<td>34</td>
</tr>
<tr>
<td>Additional payments for the enterprise results</td>
<td>18</td>
<td>18</td>
<td>16</td>
<td>20</td>
</tr>
<tr>
<td>Additional payments for work results of team/department</td>
<td>4</td>
<td>7</td>
<td>5</td>
<td>7</td>
</tr>
<tr>
<td>Additional payments for individual working results</td>
<td>20</td>
<td>20</td>
<td>16</td>
<td>22</td>
</tr>
<tr>
<td>Additional payments for additional duties</td>
<td>22</td>
<td>22</td>
<td>19</td>
<td>25</td>
</tr>
<tr>
<td>Additional payments for unhealthy work</td>
<td>7</td>
<td>10</td>
<td>9</td>
<td>11</td>
</tr>
<tr>
<td>Additional payments for overtime work</td>
<td>29</td>
<td>38</td>
<td>37</td>
<td>40</td>
</tr>
</tbody>
</table>

*Note:* The results of employers’ survey of WIF research (n = 800). Remuneration forms are multiple answers question. Therefore, the sum of all answers is greater than 100%. Qualification of employee is evaluated by subjective perception of employer. Bar ALL represents overall distribution of each form of remuneration: if for at least one category of workers the form is applied, then it is included into overall indicator.

As regards employee motivation, it is characteristic to enterprises to use individual motivation (for results of individual employee – 22% of enterprises; for additional obligation – 25%) or very general collective motivation (for results of enterprise – 20% of enterprises).

Perquisites for results of team-work or separate department are not common in Latvia. On the one hand, it is possible that work of one department is harder to evaluate and compare with work of other department, especially since targets and work tasks between divisions might be different. On the other hand, division or department is a small group where informal relations are also built, as well as collective work positively affect work productivity indicators. Possibly, awarding a premium would be a good instrument of productivity promotion.
Overall, enterprise size has positive effect to granting all kind of perquisites to employees. The larger is enterprise, the grater is a chance that premiums will be paid (especially – irregular premiums), perquisites for results of enterprise and individual work, additional obligations and overtime work.

During both employees’ focus group discussions and employers’ deep interviews, the attitude of both parties towards basic wage complementary monetary remuneration was widely discussed.

In group discussions employees admitted that premiums and perquisites are the most frequently used means of complementary remuneration. During the research, premium payment form was not specified (legal or premium in “envelope”); however comments of several respondents indicate that both payment forms are practiced.

If premiums are significant enough, employees think that they are an effective form of additional compensation. For employees having low remuneration the amount of premium is important. Partially it is perceived as compensation for lower wage. However, if the premium amount is insignificant, it is perceived with irony. Among those employees for whom the bonus depends on the amount of the work that is done or the amount of product that is sold, respondents specifically say that bonuses stimulate them to do the work to an even better degree.

There are places of employment with no clear criteria on premiums, and respondents are reserved about such bonuses, because they think that the principle of justice is violated. If the system of bonuses is unclear or if bonuses are paid irregularly, employees prefer a higher wage to the bonus. That provides them with a greater sense of security about the situation (existential needs are satisfied to a greater degree).

“There are no regular bonuses; bonuses at government institutions are confusing. If there’s money in the budget, then it’s a political decision.” (Low income, male, LV, Riga)

“There are no regular bonuses; bonuses at government institutions are confusing. If there’s money in the budget, then it’s a political decision.” (Low income, male, LV, Riga)

“Those who are closer to the bosses in terms of status and relations, they get more.” (Low income, female, RU, Riga)

Summarizing opinions, two advantages of premiums can be mentioned. Firstly, they facilitate sales and production volumes. Secondly, they are a way of praising and motivating the employee; premiums can be varied depending on productivity and the budget, thus creating a more flexible system of compensation. In its turn, disadvantage of premiums is uncertain criteria of determination of “value” of employee and possibility that the bonus can be affected by the subjective evaluation of the employer or his representative of the employee in question.

Employers’ in-depth interviews show the opinion of other side. Alike employees, employers think that premiums is the most frequent form of additional compensation. The regularity of premiums is specified by the employer on the basis of the company’s abilities and on the categories of various workers. It is very common to pay a bonus at least once a year, at Christmas. If variable pay exists at enterprise, sometimes it is considered to be bonus or premium of employee – it is higher in case of higher efficiency.
“There are categories of workers who [receive a bonus] each month or once per quarter, and everyone gets a bonus once a year.” (Riga, services, large enterprise)

“Bonuses are paid a few times a year. There are bonuses which could be called actions – the company has set six-month goals, and if the goals are achieved, then bonuses are paid. There are categories of employers such as buyers for whom wages depend on the success of the work that is done.” (Riga, retail, large enterprise)

6.2.3. Overtime work remuneration

One of important wage issues discussed in public is overtime work remuneration. Clause 68 of the Labour Law stipulates that it is to be paid in double amount – to receive a perquisite in amount of no less than 100% of fixed hourly or daily wage rate. Sector specialists indicate that this law standard in comparison to other European countries is rather strict and therefore employers are used to ignore it. However, the data reviewed in previous chapter of the survey show that perquisites for overtime work are listed as one of the most frequently paid complementary monetary remuneration forms (see figure 11). In order to inspect all presumptions heard, overtime work remuneration was estimated in regression analysis using results of both WIF employees’ quantitative research and those accumulated in CSB LFS over years.

Both hired workers of WIF and fulltime employees included in CSB LFS sample rarely work less than 40 hours per week, however about one fourth – more than 40 hours per week. Consequently, a question about wage dependency on worked hours to a great extent is a question about overtime payment, especially, regarding males and employees in private sector.

Wage dependency on worked hours is nonlinear in almost all models: as number of hours increases, marginal effect of extra hour on wage decreases. Models represented in annexed tables include number of hours and its square; for demonstrative purpose tables do not reflect separately effects of hours and squared hours but only average marginal effect of extra hour per week on wage. It can be admitted that marginal hour effect is larger when part-time employees are also included in CSB LFS sample. That indirectly affirms a decrease of worked hour effect by increasing number of hours.

In order to more precisely evaluate overtime effect on wage, models taking into account that overtime might be paid otherwise than regular hours were estimated. For this purpose, number of overtime hours was additionally included in models where professions were controlled for not at 9 basic group level of but at two-figure codes level (worked hour effect is most clearly explainable when representatives of analogous professions are compared).

Table 4 summarizes results on marginal hour effect on wage by increasing number of hours per week from 30 to 31, from 35 to 36, from 40 to 41 and from 45 to 46 in 2004 CSB LFS data in total and sample of WIF employees’ quantitative survey. Decrease of value of worked hours along with number of hours is observed in all groups of employees. As number of hours exceed 40, value of extra hour increases by leap and then decreases.
At 40 hours per week, one additional hour per week means increase of working time by 1/40, i.e., by 2.5%. According to the law, wage should grow by 5% but actually it grows on average only by 1.5% in 2004 CSB LFS sample and by 1.3% in WIF employees’ sample. In the same way, at 50 hours per week additional hour per week should raise wage by 4% but actually observed growth is only by 0.9% in 2004 CSB LFS sample and by 0.7% in WIF employees’ sample.

Table 4. Effect of number of hours usually worked per week on wage of fulltime employeesa (at other equal conditionsb) in 2004 – 2005

<table>
<thead>
<tr>
<th>Number of hours usually worked per week</th>
<th>CSP DSA, 2004</th>
<th>WIF employees, 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>30</td>
<td>0.6</td>
<td>0.6</td>
</tr>
<tr>
<td>35</td>
<td>0.3</td>
<td>0.3</td>
</tr>
<tr>
<td>40</td>
<td>1.5</td>
<td>1.3</td>
</tr>
<tr>
<td>45</td>
<td>1.2</td>
<td>1.0</td>
</tr>
<tr>
<td>50</td>
<td>0.9</td>
<td>0.7</td>
</tr>
<tr>
<td>Average number of hours worked per week</td>
<td>42.5</td>
<td>42.4</td>
</tr>
</tbody>
</table>

Note: a Fulltime employees’ sample includes those individuals who consider themselves as fulltime employees and usually work at least 20 hours per week (actually 97.3% of this sample work at least 35 hours per week). This definition differs from CSB definition in a way that the former does not include those employees who consider themselves as part-time employees even if they work more than 40 hours per week or more. Our definition is closer to Eurostat definition.
b Age, education, gender, nationality, sector and region of the place of employment, property sector, profession (27 categories), number of employees in local unit of enterprise.

It can be concluded that on average overtime is paid but certainly not in double amount as it is stipulated by the Labour Law. Overtime premiums are a bit higher for men than for women and public sector employees in comparison with private sector employees.

6.3. Forms of non-financial remuneration and their distribution

In accordance with the work task, in WIF research we had to study wage complementary values, namely, several nonmaterial benefits that employee can get working in certain place of employment. Depending on occupation there is an opportunity to use a car, mobile phone, laptop, to get health insurance, paid trip during leave as well to get other nonmaterial incentives.

Possible benefits of employee that are not paid in terms of money which were discussed in employees’ focus group discussions and employers’ in-depth interviews were studied further on within the framework of both quantitative surveys. WIF research team drew up a list of complementary benefits and remunerations and offered it to respondents. Further on respondents were asked to name from the list complementary benefits they received at principal work within the last 12 months. As during focus group discussions there was repeatedly stated opinion that granted benefit not always could be considered as benefit of employee, further on in WIF research respondent had to evaluate how much money he had saved from his budget during the year using each of benefits granted by employer. There was a possibility that employee would not save anything or a situation that employee would not
use this complementary benefit if the enterprise did not offer it to him. In such cases it was considered that employee did not save anything from his budget.

If in employees’ survey those employees were interviewed who held a position not higher than middle level manager, then in employers’ survey granting of non-monetary remuneration was observed in enterprise in general. During employers’ in-depth interviews in cases of micro and small enterprises it was admitted that many non-monetary benefits were available only to the owner of enterprise (and manager at the same time). In larger enterprises prevalence of non-monetary remuneration was greater and covered wider groups of employees. As comparison of results of employers’ and employees’ quantitative surveys indicate employees’ opinion about their benefit used to be remarkably more sceptical than data obtained in employers’ survey.

Studying further on non-monetary remuneration forms of employees, evaluation of their prevalence in both target groups will be compared. Evaluating benefit of employee, WIF team analysed in more detailed the results of employees’ quantitative survey. In theoretical part of the research it was emphasized that employee's understanding about wage and evaluation of its conformity to the accomplished responds to his work motivation and in such understanding employee’s opinion has a larger meaning.

6.3.1. Availability of non-financial remuneration at different categories of employees

Half of full time employees excluding high-level managers within the last 12 months have got at least one complementary benefit from the list made by WIF team. The received benefits in more detail are represented in table 5 showing that the structure of complementary benefits received varies depending on profession of employee. In its turn, employers’ survey shows that about 86% of enterprises have been awarded at least one benefit for the employees. Merely, micro enterprises (up to 9 employees) recognized that non-financial remuneration is awarded less (63% of that size of enterprises).

During group discussions there was observed opinion of employees that complementary benefits at place of employment depend both on employee’s initiative and common policy of enterprise. Receipt of complementary benefits may depend not only on work quality and functions of employee but also on other subjective factors, for instance, ability of employee to ask for complementary benefits. If any of benefits (most often service car, coverall, paid mobile phone) are necessary for employee to perform his duties, employees consider that employer should supply them with the mentioned.

Getting nonmaterial benefits in addition to wage was one of the issues on which the WIF research team when initiating the research had a presumption that to a greater extent it is specific to service sphere rather than other spheres of economic activity. Similarly, it was considered that availability of nonmaterial benefits increases with position held. Verification of these presumptions is the next task of regarding matters in this subchapter.
List of nonmaterial benefits received by full time employees at principal work within the last 12 months in more detail is presented in table 5. Mentioned forms are displayed by analysing the results of WIF employees’ focus group discussions and employers’ in-depth interviews.
Table 5. Types of received bonuses within last 12month by main groups of occupations

<table>
<thead>
<tr>
<th>Distribution of answers (%) in occupational subgroups</th>
<th>ALL EMPLOYEES</th>
<th>Middle level managers/head of branch/department</th>
<th>Professionals</th>
<th>Technicians and associate professionals</th>
<th>Clerks</th>
<th>Service workers and shop and market sales workers</th>
<th>Skilled agricultural and fishery workers</th>
<th>Craft and related trades workers</th>
<th>Plant and machine operators and assemblers</th>
<th>Elementary occupations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health insurance</td>
<td>20</td>
<td>34</td>
<td>28</td>
<td>29</td>
<td>22</td>
<td>12</td>
<td>9</td>
<td>17</td>
<td>18</td>
<td>11</td>
</tr>
<tr>
<td>Enterprise gifts</td>
<td>17</td>
<td>26</td>
<td>17</td>
<td>17</td>
<td>23</td>
<td>17</td>
<td>11</td>
<td>13</td>
<td>17</td>
<td>12</td>
</tr>
<tr>
<td>Training, participation in seminars/ conferences</td>
<td>14</td>
<td>34</td>
<td>34</td>
<td>26</td>
<td>16</td>
<td>9</td>
<td>0</td>
<td>5</td>
<td>5</td>
<td>1</td>
</tr>
<tr>
<td>Coveralls</td>
<td>14</td>
<td>17</td>
<td>5</td>
<td>13</td>
<td>11</td>
<td>16</td>
<td>19</td>
<td>20</td>
<td>18</td>
<td>13</td>
</tr>
<tr>
<td>Mobile phone calls paid by enterprise</td>
<td>9</td>
<td>36</td>
<td>13</td>
<td>16</td>
<td>11</td>
<td>4</td>
<td>0</td>
<td>4</td>
<td>7</td>
<td>2</td>
</tr>
<tr>
<td>Transportation expenses (including business car)</td>
<td>7</td>
<td>15</td>
<td>7</td>
<td>9</td>
<td>8</td>
<td>3</td>
<td>5</td>
<td>7</td>
<td>9</td>
<td>2</td>
</tr>
<tr>
<td>Food products, catering</td>
<td>7</td>
<td>6</td>
<td>5</td>
<td>5</td>
<td>3</td>
<td>14</td>
<td>11</td>
<td>3</td>
<td>7</td>
<td>5</td>
</tr>
<tr>
<td>Business trips</td>
<td>6</td>
<td>21</td>
<td>12</td>
<td>10</td>
<td>5</td>
<td>1</td>
<td>0</td>
<td>2</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>Fitness activities</td>
<td>5</td>
<td>12</td>
<td>6</td>
<td>6</td>
<td>7</td>
<td>4</td>
<td>2</td>
<td>3</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Compensation for using private car</td>
<td>4</td>
<td>15</td>
<td>4</td>
<td>6</td>
<td>3</td>
<td>2</td>
<td>2</td>
<td>3</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>Guaranties for bank credits</td>
<td>3</td>
<td>6</td>
<td>4</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>5</td>
<td>1</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Deposits in a private pension fund</td>
<td>2</td>
<td>6</td>
<td>3</td>
<td>3</td>
<td>3</td>
<td>1</td>
<td>0</td>
<td>2</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Enterprise credits for employees</td>
<td>2</td>
<td>6</td>
<td>2</td>
<td>2</td>
<td>3</td>
<td>2</td>
<td>0</td>
<td>2</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>Travels paid by enterprise</td>
<td>2</td>
<td>6</td>
<td>3</td>
<td>3</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>2</td>
<td>0</td>
<td>1</td>
</tr>
<tr>
<td>Business laptop/ computer at home</td>
<td>2</td>
<td>8</td>
<td>4</td>
<td>3</td>
<td>2</td>
<td>1</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Nothing of mentioned</td>
<td>49</td>
<td>25</td>
<td>37</td>
<td>39</td>
<td>45</td>
<td>56</td>
<td>64</td>
<td>58</td>
<td>51</td>
<td>66</td>
</tr>
</tbody>
</table>

| Total, n=                                      | 4040          | 220                                           | 537            | 635                                     | 298    | 752                           | 45                                       | 558                           | 514                           | 479                          |

Note: The results of employees’ survey of WIF research. For evaluation of size of target group, the number of respondents in sub-groups are shown (row “Total, n=”). Row “nothing of mentioned” shows single answers of respondents who have not received anything from remuneration forms listed within table. Other types of remuneration refer to multiple answer question. Taking into account statistical significance, benefits marked into read colour are assigned more frequently than benefits market into blue colour.
Table 5 should be read from top to bottom. The measured non-monetary remuneration forms are listed in the left column. Subdivisions of analysis – both employees in total (up to middle-level managers) and division by basic groups of occupations – are placed in columns of the table. Cells of the table present proportion (in percent) of target group which has received non-monetary remuneration listed in the row. For instance, table 5 shows that within the last 12 months 20% of employees received health insurance. Middle-level managers receive health insurance more often – 34%.

In general, question presented in table 5 provides various potential answers except for case when employee within the last 12 months has not received anything from the list. Then one of the answers was marked (“nothing from listed”). This row represents proportion of employees who have not received any of non-monetary remunerations. We can see that within the last 12 months about 49% of employees have got none of its forms in the principal work, besides this proportion increases with lower qualification of employee.

Consequently, the higher is level of groups of occupations the employee belongs to, the more often he gets at least one of the forms of non-monetary remunerations. That confirms the hypothesis stated in WIF research that availability of nonmaterial benefits increases with higher position held. In addition to the said in the employers’ in-depth interviews that owners and directors have the greatest potentialities to use non-monetary benefits this tendency clearly appears in WIF employees’ survey. In accordance with the latter, non-monetary remuneration most frequently is received by middle-level managers, professionals and associate professionals. Although craft and related trades workers, plant and machine operators are lower level employees, there is comparatively larger number of respondents among them who have got complementary benefits. However, reviewing the list of complementary benefits that each group of occupation get, we can see that representatives of these occupations as complementary benefits mostly get coveralls and health insurance policy paid by employer (see table 5).

WIF employees’ survey data show that employees most frequently have got health insurance policy paid by enterprise and enterprise gifts. Health insurance policy as one of the most frequently received forms of complementary benefits was noticed to employees in all groups of occupations, more frequently – middle-level managers, professionals and associate professionals. Enterprise gifts are mostly received by middle-level managers and skilled office staff.

Employees mention that they take part in training and seminars paid by enterprise and this opportunity is closely related to employee’s occupation. Most frequently in training and seminars take part middle-level managers and professionals, followed by associate professionals and skilled office staff (clerks). Representatives of other groups of occupations quite rarely improve their knowledge or participate in seminars. Currently, attendance of training and seminars is mostly characteristic to transport, communication, financial, commercial services, state administration, education and health sectors. We should note that in some sectors, like medicine, regular improvement of professional skills is mandatory.

The most specific non-monetary benefits are transportation expenses or service car and catering paid by enterprise (including foodstuffs). If service car was given to employees of higher groups of occupation, compensation of transportation expenses was specific to those enterprises where employees from more distant populated places were employed. Paid
catering or foodstuff is most characteristic to two economic sectors – agricultural sector and commerce, hotels and public catering sector.

Business trips where time is allotted also to private interests of employee, service computer at home and compensation for car exploitation is most frequently available to middle-level managers.

Guarantees to bank loans or enterprise loans to employees are rarely met forms of non-monetary remuneration and they are more related not to direct benefit of employee but to comfort they provide. Instalments to private pension funds currently are characteristic practically only to large enterprises (more than 500 employees). The employers’ in-depth interviews showed that directors of smaller enterprises currently are just getting acquainted with private pension fund system and consider potential benefits by remunerating their employee in such manner.

The results of employers’ quantitative survey demonstrate a bit different outlook – most frequently are mentioned such non-monetary benefits as training, studies paid by enterprise, participation in seminars and conferences, enterprise gifts, paid mobile phone, business trips and compensated transportation expenses or service car. That clearly illustrates effect of specific remuneration of enterprise administration on research results – in other cases rarely granted non-monetary remuneration forms get in top of the list.

Other relationships noticed in WIF employees’ quantitative survey indicate that probability to get non-monetary remuneration at principal work increases with size of employee’s place of employment (number of employees) and existence of collective agreement in enterprise. It means that with increasing enterprise size probability that employees will get at least one complementary benefit also increases. In their turn, those employees who have concluded collective agreement at their place of employment have higher probability to receive at least one complementary benefit at the enterprise. We should also note indirect relationship between enterprise size and collective agreement as collective agreements in Latvia most often are concluded in large enterprises. Across other characteristics (for instance, gender, regions, age etc.) no substantial differences in non-monetary remuneration forms have been noticed.

The presumption initially stated in the research on wider prevalence of non-monetary remuneration in service sphere enterprises shall not be considered as well-grounded if we consider total proportion of complementary benefits granted. Statistically significant differences are observed between at least one complementary benefit in commercial, hotel, public catering and individual service sectors (at least one complementary benefit is granted to 42% of employees) and other economic sectors (to 50 – 57% of employees). For other research, this hypothesis should be supplemented with presumptions on prevalence of various forms of complementary benefits among employees in certain economic sectors.
6.3.2. Value of non-monetary benefit

During group discussions wide discussions arose concerning advantages and disadvantages of wage complementary benefits granted by employers. Wide discussions are reflected also in the results of quantitative survey where respondents evaluated what amount in lats they had saved from their budget within a year by receiving or using complementary benefits or remuneration granted by enterprise. The obtained answers were grouped in intervals representing employees’ opinion on amount of financial benefit (see table 6).

Table 6 presents the subjective evaluation of respondents about granted non-monetary remuneration in financial terms. Although employer allocates certain resources to non-monetary remuneration, employee may consider that he saves nothing. If enterprise did not offer such opportunity and in that case employee did not use it himself, benefit was also assigned null value.

In the left side of table 6 non-monetary remuneration forms received at place of employment are presented at the same order as in table 5 and number of respondents who had received them. Further in the row evaluation of employee’s benefit is represented starting with a possibility that nothing was saved up to economy of several hundred lats per year. Evaluation of benefit in terms of money is given in interval scale. Percentage distribution of answers and how often each of benefits has given a gain within limits of certain money amount were presented in the row. Evaluation of financial value (including answers that there was no benefit and “hard to say”) for each non-monetary remuneration form in sum amounts to 100%.

The acquired data indicate that employees relatively sceptically evaluate their benefit – irrespective of the fact that employee has received non-monetary remuneration, in several cases respondents consider that they have saved nothing much from their annual budget or do not try to use an opportunity at all (for instance, in case of health insurance, sports activities paid by enterprise).

Within focus group discussions, opinion that health insurance is a good benefit has gained the advantage. It shows that the employer cares for his employees. Those employees with health insurance are happy about it, particularly if they have a low wage or have had health problems that have been resolved via the health insurance policy, thus spending much less in the way of personal money. This is a way of satisfying one’s need for security. It also has to be said that female were more likely than male to speak of the importance of health insurance. Male speak of health insurance if they work in dangerous conditions (work with specific manufacturing equipment, etc.)

“[Insurance] It is a healthy compromise. It doesn’t cost much for the company, but it’s very important for the individual. The health insurance policy provides more guarantees than the state’s social security system does.” (High income, male, LV, Riga)

“I think that the employer must insure his employees.” (Low income, female, RU, Riga)

When it comes to health insurance policies, respondents say that it is important for the employer to choose one which offers as much in the way of benefits as possible.
“Sometimes the company pays for the insurance, but it turns out that you have to pay some of the cost yourself. Then you don’t know whether it’s really a benefit.” (High income, male, RU, outside Riga)

Some respondents say that even though their employer offers health insurance, they use it seldom, and that, in turn, can lead the employer to think again about whether the resources that are invested in health insurance for employees are well spent.

“I don’t have insurance, but my husband does. He has never used it. We take care of ourselves.” (Medium income, female, LV, Riga)

Table 6. Financial value of used non-financial remuneration evaluated by employees

<table>
<thead>
<tr>
<th>Distribution of answers (row %)</th>
<th>Number of answers, n=</th>
<th>Amount of economised value (lats)</th>
<th>Distribution of answers (%)</th>
<th>Have not economised</th>
<th>1-20</th>
<th>21 – 50</th>
<th>51 – 100</th>
<th>101 – 150</th>
<th>151 – 200</th>
<th>201 – 250</th>
<th>251 – 300</th>
<th>&gt;301</th>
<th>Hard to say</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health insurance</td>
<td>810</td>
<td></td>
<td></td>
<td></td>
<td>26</td>
<td>17</td>
<td>18</td>
<td>11</td>
<td>3</td>
<td>2</td>
<td>0,2</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>Enterprise gifts</td>
<td>676</td>
<td></td>
<td></td>
<td></td>
<td>8</td>
<td>52</td>
<td>17</td>
<td>8</td>
<td>0,3</td>
<td>0,2</td>
<td>0</td>
<td>0,3</td>
<td>0,4</td>
</tr>
<tr>
<td>Training, participation in seminars/ conferences</td>
<td>593</td>
<td></td>
<td></td>
<td></td>
<td>22</td>
<td>9</td>
<td>20</td>
<td>11</td>
<td>4</td>
<td>5</td>
<td>1</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Coveralls</td>
<td>556</td>
<td></td>
<td></td>
<td></td>
<td>20</td>
<td>16</td>
<td>20</td>
<td>10</td>
<td>2</td>
<td>3</td>
<td>0,2</td>
<td>0,4</td>
<td>0,2</td>
</tr>
<tr>
<td>Mobile phone calls paid by enterprise</td>
<td>362</td>
<td></td>
<td></td>
<td></td>
<td>11</td>
<td>9</td>
<td>14</td>
<td>15</td>
<td>4</td>
<td>4</td>
<td>3</td>
<td>1</td>
<td>7</td>
</tr>
<tr>
<td>Transportation expenses (including business car)</td>
<td>268</td>
<td></td>
<td></td>
<td></td>
<td>14</td>
<td>11</td>
<td>14</td>
<td>12</td>
<td>8</td>
<td>6</td>
<td>3</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Food products, catering</td>
<td>268</td>
<td></td>
<td></td>
<td></td>
<td>9</td>
<td>9</td>
<td>16</td>
<td>12</td>
<td>14</td>
<td>6</td>
<td>4</td>
<td>2</td>
<td>11</td>
</tr>
<tr>
<td>Business trips</td>
<td>229</td>
<td></td>
<td></td>
<td></td>
<td>22</td>
<td>15</td>
<td>15</td>
<td>10</td>
<td>4</td>
<td>3</td>
<td>1</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>Fitness activities</td>
<td>184</td>
<td></td>
<td></td>
<td></td>
<td>26</td>
<td>11</td>
<td>15</td>
<td>7</td>
<td>7</td>
<td>7</td>
<td>1</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Compensation for using private car</td>
<td>144</td>
<td></td>
<td></td>
<td></td>
<td>15</td>
<td>6</td>
<td>8</td>
<td>7</td>
<td>10</td>
<td>4</td>
<td>4</td>
<td>6</td>
<td>16</td>
</tr>
<tr>
<td>Guaranties for bank credits</td>
<td>117</td>
<td></td>
<td></td>
<td></td>
<td>36</td>
<td>3</td>
<td>2</td>
<td>2</td>
<td>1</td>
<td>1</td>
<td>0</td>
<td>3</td>
<td>9</td>
</tr>
<tr>
<td>Deposits in a private pension fund</td>
<td>92</td>
<td></td>
<td></td>
<td></td>
<td>23</td>
<td>5</td>
<td>2</td>
<td>10</td>
<td>4</td>
<td>4</td>
<td>4</td>
<td>5</td>
<td>3</td>
</tr>
<tr>
<td>Enterprise credits for employees</td>
<td>90</td>
<td></td>
<td></td>
<td></td>
<td>28</td>
<td>2</td>
<td>7</td>
<td>10</td>
<td>5</td>
<td>10</td>
<td>1</td>
<td>4</td>
<td>12</td>
</tr>
<tr>
<td>Travels paid by enterprise</td>
<td>89</td>
<td></td>
<td></td>
<td></td>
<td>11</td>
<td>14</td>
<td>18</td>
<td>17</td>
<td>5</td>
<td>3</td>
<td>2</td>
<td>5</td>
<td>12</td>
</tr>
<tr>
<td>Business laptop/computer at home</td>
<td>69</td>
<td></td>
<td></td>
<td></td>
<td>17</td>
<td>7</td>
<td>7</td>
<td>26</td>
<td>10</td>
<td>4</td>
<td>0</td>
<td>4</td>
<td>10</td>
</tr>
</tbody>
</table>

Note: The results of employees’ survey of WIF research.
Regarding material benefit from using health insurance, about one fourth of employees who were granted such remuneration form considered that within a year they had saved noting. Similar evaluation was obtained in cases of sports activities paid by enterprise when they were not included in health insurance policy (see table 6).

Training and various studies, conferences and seminars are important to employees, for those are chances to improve own professional skills and competitiveness in labour market. However, it is considered that not all employers have understood significance of training and improvement of professional skills. The most fundamental deficiencies concerning studies and attendance of training are related to various constraints – employees are to study issues that employer considers important, in case of studies paid by employer employee has to work a fixed time at the enterprise, as well as the fact that employee has to spend his free time for studies, that is, studies take place in leisure time.

In case of training, studies, seminars or conferences paid by enterprise, 22% of respondents admitted they saved nothing (see table 6) which might be related to provision stated for evaluation, namely, if this training was not paid by enterprise, employees would not take part in them. For those who consider that they have got material benefit from training value of benefit mainly varies between 21 and 50 lats. In other cases benefit is even larger.

Business trips are not viewed unanimously as a benefit, because there are secondary conditions which occur for the employee while travelling. Attitudes depend on the employee’s desire and interest to travel. The frequency and duration of travel – that is the first important factor. If the employee has to travel a lot, and the schedule is tense, then this is not seen as a benefit.

“As long as it’s not too often. If you have to travel every two days and don’t see your family – that’s not a bonus. [...] It depends, too, on what you do there. When we had to work for 20 hours straight to do everything quickly – I don’t need that.” (High income, female, RU, Riga)

If trip is less frequent and allows the employee to spend some free time at the destination, then that is seen as a nice change. Business trip is considered as additional opportunity to travel then.

Researchers found that many employees are unaware of Cabinet of Ministers regulations on the financing of business trips. They think that material compensation in this regard depends on the employer alone.

“They send you, you have to get there, you have to eat – if the employer doesn’t pay for that, then it’s no benefit.” (Medium income, male, RU, Riga)

To considerably larger part of employees trips paid by enterprise are available. In such cases only 10% consider that they have saved nothing from their budget, at the same time the majority consider that saving from the trip is not large. Most frequently mentioned savings are relatively evenly distributed between 1 and 100 lats (see table 6). Although in the research we did not ask where the employee had gone during trip paid by enterprise and if he had to cover part of costs and what calculations he considered when estimating his savings, we see that subjectively the saving is evaluated quite modestly.
Foodstuff or catering paid by place of employment is rather specific benefit, as to a high degree it is characteristic to employees of commercial, hotel and public catering as well as individual service sectors. Total annual saving evaluated by respondents varies between 21 and 150 lats (see table 6).

Gain from enterprise gifts (or presents) is evaluated quite clearly – about half of employees who had received gifts evaluated gain between 1 and 20 lats and almost one fifth admitted that gain was between 21 and 50 lats. These answers render quite clear picture on the most prevalent budget used for gifts for one employee in the enterprise.

Such resources or equipment that employees can partially use for their own needs, for instance, paid mobile phone, opportunity to use service computer at home etc. are also included in complementary benefits. During group discussions there was found out that paid mobile phone (also service car and coverall) are not perceived as complementary benefits if they are necessary to perform direct job responsibilities. Regarding telephone and service car, it is sometimes noted that they are followed by risk that employer may phone in the evening and call to work considering that granted benefits allow him to act in such manner.

Employees not always are provided with coverall, although there are certain requirements about outfit at work place. In several sectors like construction, car service, medicine etc. coverall is a necessity and usually it is provided by employer. However, in group discussions that were hold outside of Riga it appeared that employers more rarely offer resources substantially necessary for work. There are situations when employer obtains instruments necessary for work at his own cost.

More complicated is to evaluate such possible employees’ benefits as enterprise guarantees to bank loans, work place loans to employees and enterprise’s instalments to private pension funds. In cases of bank guarantees and enterprise loans it is difficult to evaluate possible benefit as it derives from loan interest savings amount of which is hard to estimate and even harder – to establish during interview. In case bank does not give credit without having enterprise guarantee, benefit expressed in terms of money is impossible to evaluate. Therefore it is natural that it is easier to get a subjective evaluation, namely, that it is agreeably to employee that enterprise gives countenance to him by issuing guarantee, still such assistance is hard to evaluate in financial terms. Consequently, comparatively large number of respondents considers that they have not got any savings or it is hard to evaluate.

Although private pension funds abroad keep developing, employees in Latvia find it hard to evaluate the possible benefit from enterprise instalments to private pension funds. 40% of employees of those enterprises that have made instalments to private pension funds could not evaluate the possible benefit. That might be related to both our definition, namely, evaluation of saved amount that is possible only if employee himself desired to make savings, and possible poor awareness of employees about amount that is transferred to enterprise pension fund within year. However, evaluating rather high popularity of private pension funds and savings abroad, we assume that in the course of time its significance in remuneration of employees might increase.

Although employees in focus groups did not consider that work place improvement might be included in wage complementary benefits, in employers’ interviews it was emphasized that premises are part of offering.
“To be in nice rooms, in a nice office (..) – that naturally affects results (..) and that certainly has an effect on the entire process.” (Riga, services, small enterprise)

“[Our facilities] are renovated and improved, but that does not affect wages, because wages are a separate line item in the budget, apart from other expenditures.” (Riga, services, medium enterprise)

Summarizing the analysis, we can see that the most common and most highly evaluated benefits are health insurance and enterprise gifts. Significant wage complementary benefit is foodstuffs or catering paid by enterprise although those are available only to employees in certain sectors.
VII EMPLOYEES AS HUMAN RESOURCES

The objective of this chapter is to evaluate wage differences at individual level by determining relationship between wage and employee’s education, age, experience, career history as well as other factors. Described regularities are observed when conducted econometric analysis of data of the WIF research and CSB LFS 2003 – 2004. At this section, the concept „salary” (earnings) includes basic wage together with premiums and other additional payments.

Within chapter, it will analyse various wage affecting level factors of individual by paying particular attention to significance of education, group of professions, age and other similar aspects. Most important regularities will be shown within gender, age, education and earnings profiles. The impact of ethnicity and Latvian language skills on earnings, as well as public and private sector workers will be examined.

7.1. Impact of education, age and gender to labour income

Data analysis of WIF employees’ quantitative survey show: the higher employee’s education, the higher his average wage. Comparing employees of one profession and sector, employees having higher academic education earn on average by 24% more than employees having general secondary education. Existence of higher education gives larger impact on female remuneration than male remuneration. Effect of first level higher vocational education is a bit smaller – it raises employee’s wage by about 14%, other conditions being equivalent. Educational level below elementary education causes wage decrease on average by 12.8% compared to secondary education, but elementary educational level – on average 11.0% decrease.

Comparing results with model where professions are not controlled but sector control is left wage differences of all educational levels increase. Wage of employees having higher academic education is on average by 54% higher than wage of employee having general secondary education. Greater effect of higher education is noticed for wage of female and employees in public sector. Negative effect of elementary education on wage also increases. Comparing employees employed in one sector without profession control wage of employee having elementary education is on average by 15% lower than wage of employee having general secondary education. If employee does not have elementary education, his wage is lower on average by 21%. Review on results of econometric analysis of WIF employees’ quantitative survey is presented in appendix tables 5.1 and 5.2. Similar regularities are noticed working with CSB LFS data of 2003 and 2004 where review of results of econometric analysis is presented in appendix tables 6.1 and 6.2.

Reason of various effects of education described above is the double effect of education described in method section of research analysis. In case if both sector and profession are controlled, comparison is made versus employee having secondary educational level who is employed in the same sector and the same occupation. If occupations are not controlled,
comparison is made within the framework of whole sector. It is easy to understand that employees having higher educational level are mostly employed also in highly paid occupations.

In order to assess the relative value of various higher education spheres in labour market, separate wage equation for employees having higher education was estimated using combined basis of CSB LFS 2003-2004 (see appendix table 6.4). As control variable in analysis was included time passed since education was acquired (in other words, year of education acquirement is controlled). Besides, indicators of occupations, employment sectors and enterprise size were not included in the model. Accordingly, full return of education sphere was evaluated which expresses through possibility to find a job in “best” sectors and enterprises, opportunities of profession choice, through professional achievements within sector and group of professions.

In the first column of appendix table 6.4 results regarding only persons who acquired higher education after 1991 (1417 respondents) are presented. Noticed effect of education sphere is presented in figure 12.

**Figure 10. Wage index (teacher education = 100) of persons with higher education acquired after 1991 depending on field of education (at other equal conditions) in 2003 - 2004**

<table>
<thead>
<tr>
<th>Field of Education</th>
<th>Index</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mathematics and statistics</td>
<td>143</td>
</tr>
<tr>
<td>Transport</td>
<td>130</td>
</tr>
<tr>
<td>Engineering and industry occupations</td>
<td>130</td>
</tr>
<tr>
<td>Architecture and construction</td>
<td>126</td>
</tr>
<tr>
<td>Private services</td>
<td>125</td>
</tr>
<tr>
<td>Business activities and administration</td>
<td>125</td>
</tr>
<tr>
<td>Social sciences</td>
<td>119</td>
</tr>
<tr>
<td>Computer sciences</td>
<td>119</td>
</tr>
<tr>
<td>Biology and environment sciences</td>
<td>118</td>
</tr>
<tr>
<td>Humanities</td>
<td>117</td>
</tr>
<tr>
<td>Health and social work</td>
<td>114</td>
</tr>
<tr>
<td>Civil and military defence</td>
<td>114</td>
</tr>
<tr>
<td>Justice sciences</td>
<td>111</td>
</tr>
<tr>
<td>Physics and chemistry sciences</td>
<td>100</td>
</tr>
<tr>
<td>Medicine and pharmacy</td>
<td>100</td>
</tr>
<tr>
<td>Manufacture and processing</td>
<td>99</td>
</tr>
<tr>
<td>Agriculture, forestry and fishing</td>
<td>97</td>
</tr>
<tr>
<td>Art, music and un choreography</td>
<td>94</td>
</tr>
<tr>
<td>Information and communication sciences</td>
<td>86</td>
</tr>
<tr>
<td>Veterinary science</td>
<td>72</td>
</tr>
</tbody>
</table>

**Notes.** Effects of transportation, computer sciences, health and social care, physics and chemistry sciences, medical and pharmacy, manufacturing and processing, agriculture and art specialities have been estimated with smaller precision that all the rest. * Year of acquiring education, gender, nationality, contract form, tenure, number of hours usually worked per week, work place region, rural or urban territory.
Figure 12 shows that absolute leader among fields of education acquired after year 1991 is “mathematics and statistics”: graduates of this program receive, at other conditions held equal, by 43% more than persons with teacher education. Mathematics is followed by engineering science, architecture and construction, transportation, personal services and business and administration with indices in interval from 125 to 130. It should be noted that effects of transportation, architecture and construction sectors have been estimated with smaller precision.

The next group consists of social and human action sciences, computer sciences, biology, the soft sciences, health and social care, civil and military defence and legal sciences with indices in interval from 110 to 120 points. Admittedly, effects of computer sciences, biology, the soft sciences, civil and military defence as well as legal sciences are estimated have been estimated with smaller precision than the rest.

The next group consists of educational fields, indices of which are close to the reference group – teachers. These are physics and chemistry, medical and pharmacy, manufacturing and processing, agriculture, forestry and fisheries, as well as art and music. The lowest wages among those who acquired education in “the new time” was observed to graduates of information and communication sciences, as well as veterinary programs.

In the second column of table 6.4 of the review appendix are reflected results of persons who have acquired higher education before year 1992 (1912 respondents). The most significant positive effects compared to teacher education have been discovered in fields of computer sciences, mathematics and statistics, transportation and legal sciences.

Combining all respondents in one sample, one more rating was formed (see column 3 of table 6.4 of the appendix) where the “old” higher education system could freely compete with the “new” one. In the first place with the largest positive effect is mathematical and statistical education where graduates on average receive by 60% higher wage than teachers. In the second position are computer sciences and graduates of this program receive by 40% higher wage than teachers. In the third position is education acquired in transportation sector (positive effect on wage is approximately 27% in comparison with reference group).

The last two columns of table 6.4 of the appendix exhibit wage equation for male and female with higher education (number of respondents does not allow do divide in the sample also by period of acquired education). Considering only statistically significant effects, among male the highest wage is received by those who have acquired speciality in mathematics and statistics, computer sciences and transportation. In its turn, educational top of female is the following: transportation, mathematics and statistics, computer sciences, legal sciences and social and human activity sciences.

One of the most interesting comparisons is comparison of employees’ income, education and age profiles, as significant differences between observed wage – age profile in Latvia and other countries were established also in previous studies. Age earning profiles for males are shown in figure 13, for females – in figure 14.

Figure 13 shows that male income level reaches its maximum between age of 30 and 35 at all educational levels. Comparing levels of higher education, we can conclude that there is practically no difference between profiles of first level higher education and academic higher
education. Both educational levels on average cause higher income to employee compared to other educational levels.

**Figure 11. Age and education earnings profiles for males**

<table>
<thead>
<tr>
<th>Lats, LVL</th>
<th>Primary education</th>
<th>Vocational education after all-round primary</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>50</td>
<td>100</td>
</tr>
<tr>
<td>150</td>
<td>200</td>
<td>250</td>
</tr>
<tr>
<td>300</td>
<td>350</td>
<td>400</td>
</tr>
</tbody>
</table>

*Note:* The results of employees’ survey of WIF research.

**Figure 12. Age and education earnings profiles for females**

<table>
<thead>
<tr>
<th>Lats, LVL</th>
<th>Primary education</th>
<th>Vocational education after all-round primary</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>50</td>
<td>100</td>
</tr>
<tr>
<td>150</td>
<td>200</td>
<td>250</td>
</tr>
<tr>
<td>300</td>
<td>350</td>
<td>400</td>
</tr>
</tbody>
</table>

*Piežime:* DAIF algoto darbinieku kvantitatīvās aptaujas rezultāti.
Figure 14 shows that in most cases maximum point of female income is reached between age of 30 and 33. Although this tendency is similar to earnings profile for male, there are some differences. Age, gender and education profiles of female differ from that of male for two reasons. Firstly, the earnings of female are lower and therefore earning – age curves are placed lower. Secondly, first level higher education shows significant difference from other education levels as reaches its maximum point later, at age of 45.

Age, education and gender income profile show that the wage of employees above 40 gradually reduces. The most rapid wage reduction is for employees above 50, which is a pre-retirement age. Employers indicate that despite the fact that skills and abilities of each person should be judged individually, it has been observed that people of the pre-retirement age master new things slower and there are physically weaker. If the wage within an enterprise depends directly from working efficiency, then as the result, the wage for elderly people is lower. For example, in enterprises of construction and wood-processing elderly people are not able to do definite jobs and this lessens opportunities of gaining more.

“Age doesn’t affect salaries, but at my sawmill and elderly person cannot work with the timber (..) it is physically demanding work.” (Outside Riga, manufacturing, micro enterprise)

“Age doesn’t affect salaries, but there are times when we need a younger person who can do the work better than an older person could.” (Riga, services, small enterprise)

The results of employee poll supplement opinions of employers and show that employees of the pre-retirement age are more compliant as to the wage and working conditions because of the fear of losing job. These results affirm a part of the hypothesis that representatives of the risk group have fewer demands in the labor market. As the risk group is constituted not only by pre-retirement age persons, but also by other categories of employees, it is not possible to state that the hypothesis is completely proven.

Although WIF team expected that the maximum income age should grow compared to observations of previous years, data of WIF research show very similar distribution. Similar results were obtained when analysing data of CSB LFS. In general, it can been said that the utmost income point in Latvia still is far from average level of the European Union countries, where it is known that male income grows up to age of 50 – 52, while female get their utmost income a bit earlier.

Observing results of our research by gender, we can see that, after controlling for professions and economic sectors, female wage is on average by 21.5% lower than male wage. Gender wage differences are significant by urban and rural division as well as depending on employment sector. In cities female wages are on average by 21.9% lower than male wages but in rural areas – by 20.0% lower. Female wage in private sector compared to public sector is lower (respectively, by 23.4% and 18.4% lower than male wage).

If professions are not controlled for, effect of employee’s gender on wage increases. One of the reasons is profession segregation to which indicates also a fact that value of wage difference coefficients increase if profession control is not included in the model. However, this increase is not large – in models without profession control female wage was on average by 24.4% lower than male wage.
When analyzing wages of women who have children younger than two, there were no statistically relevant differences from the rest of the group found. It is important to note here that the hypothesis of the low demands of young mothers in the labor market foresee the situation that the young women do look for a new job rather than stay at the previous place. This means that the observed regularity is not a sufficient proof to question the hypothesis. The discussions of employees show that a low wage is more characteristic for situations when a person is returning to the labor market, i.e. the first year of employment. The data analyzed in the next chapter show that the length of employment relationships is a relevant factor that influences the wage.

### 7.2. Impact of tenure

Tenure in the particular enterprise characterizes acquired specific experience of employee. Moreover, employees working in enterprise for a long period of time have lower tendency to look for other place of employment, and employer can quite certainly count on them also in the future. For these both reasons, wage increases with tenure. It is important to note that usually effect of tenure decreases with longer tenure: the largest wage increase is related to the first year worked in the enterprise, and increase with each next year is smaller and smaller. Overall, relationship is nonlinear which was easier to estimate by analysing CSB LFS data with larger number of observations (see table 7).

#### Table 7. Tenure and wage, CSB LFS. Fulltime employees, year 2004

<table>
<thead>
<tr>
<th></th>
<th>TOTAL</th>
<th>Male</th>
<th>Female</th>
<th>Private sector</th>
<th>Public sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>[1] Average tenure in years</td>
<td>7,6</td>
<td>6,7</td>
<td>8,6</td>
<td>5,9</td>
<td>10,8</td>
</tr>
<tr>
<td>[2] Wage increase (%) for one extra tenure year (at other equal conditions(^a), without profession control) at average tenure(^b)</td>
<td>1,15</td>
<td>1,22</td>
<td>0,95</td>
<td>1,20</td>
<td>0,93</td>
</tr>
<tr>
<td>[3] Average wage increase (%) on one tenure year (starting with the second)(^c) (at other equal conditions(^d)): with profession control</td>
<td>0,87</td>
<td>0,93</td>
<td>0,76</td>
<td>0,76</td>
<td>0,81</td>
</tr>
<tr>
<td></td>
<td>0,50</td>
<td>0,66</td>
<td>0,32</td>
<td>0,42</td>
<td>0,42</td>
</tr>
<tr>
<td>[4] Wage difference (%) for employees with tenure up to one year (at other equal conditions(^e)): with profession control</td>
<td>-8,7</td>
<td>-7,4</td>
<td>-10,5</td>
<td>-8,6</td>
<td>-8,1</td>
</tr>
<tr>
<td></td>
<td>-6,8</td>
<td>-5,7</td>
<td>-8,4</td>
<td>-6,4</td>
<td>-6,9</td>
</tr>
</tbody>
</table>

Notes: \(^a\) Age, education, gender, nationality, number of hours usually worked per week, work place sector and region. \(^b\) Estimated from the model where tenure and tenure squared are included. \(^c\) Estimated from the model where only linear for of tenure is included (see tables 6.2 and 6.3 of the appendix), as well as indicator for employees with tenure up to one year, see tables 6.2 and 6.3 of the appendix.
In row [2] of table 7 one can see that employee’s with average tenure wage increase for extra year of tenure is 1.15%. This result is obtained from the model where tenure and tenure squared are included. However, wage difference between employee working in the enterprise for 21 year and employee working only for 1 year (at other equal conditions, except for profession) will be much smaller than $20 \times 1.15\% = 23\%$. This difference can be simply estimated from the model where tenure is included only in linear form (and additional indicator for employees with tenure up to one year, see tables 6.2 and 6.3 of annex). Results of this model are shown in row [3] of table 7. In our example wage difference will be equal to $20 \times 0.87\% = 17.4\%$. In its turn, if employees also belong to one group of professions, wage difference will be only $20 \times 0.50\% = 10\%$ (row [4] of table 7). This last difference may be interpreted as a “loyalty premium”, but $17.4\% - 10\% = 7.4\%$ corresponds to additional promotion opportunities related to long term tenure.

“Penalty” for employees with tenure under 1 year is rather large: almost 9% of wage if profession is not controlled and almost 7% within one group of professions. It means that wage difference between employee with 20 years long experience in the given enterprise and just hired employee with similar age, education etc. characteristics will be on average $20 \times 0.87\% + 8.7\% = 26.1\%$, but if employees belong to one group of professions, wage difference will be only $20 \times 0.50\% + 6.8\% = 16.8\%$.

According to data of focus group discussions, observed earnings differences for the fist year at enterprise is not only objective (lack of particular experience), but also subjective. It expresses as lower level of demands to employer – while the employee is not shown himself/herself at workplace, there is no reason to request higher wage.

### 7.3. Impact of part time employment and type of contract on earnings

As we see in table 8, even controlling for number of hours worked and excluding effects of other factors, wage of part-time employees in 2003 – 2004 was almost by quarter lower than wage of fulltime employees. This difference has increased, compared to year 2002, when it was equal to only 15%.

Inclusion of occupation control does not change result substantially, indicating that even within one group of professions part-time employees receive disproportionately low remuneration. It might be one of the reasons why part-time work in Latvia is less common than in the old European Union member states and is less used in order to balance work and family life.

As regards employees having limited duration contract, wage inequality in the course of time decreases. On average in 2004 – 2005 such employees received by approximately 9% lower wage than employees similar by education and demographic features and having limited duration contract in the same sector and region.
Table 8. Influence of part-time and limited duration contract on wage in percent (at other conditions) in 2002 – 2005

<table>
<thead>
<tr>
<th>Year</th>
<th>Data</th>
<th>Occupation control</th>
<th>All employees</th>
<th>Fulltime employees</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>Total Female</td>
<td>Total Female</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Male</td>
<td>Male</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Female</td>
<td>Female</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Private</td>
<td>Public</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>sector</td>
<td>sector</td>
</tr>
<tr>
<td>Part-time</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>LFS</td>
<td>No</td>
<td>-15.3</td>
<td>-15.7</td>
</tr>
<tr>
<td>2003</td>
<td>LFS</td>
<td>No</td>
<td>-23.8</td>
<td>-16.2</td>
</tr>
<tr>
<td>2004</td>
<td>LFS</td>
<td>No</td>
<td>-24.9</td>
<td>-21.2</td>
</tr>
<tr>
<td>2004</td>
<td>LFS</td>
<td>Yes</td>
<td>-23.6</td>
<td>-18.4</td>
</tr>
<tr>
<td>Limited duration contract</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>LFS</td>
<td>No</td>
<td>-13.0</td>
<td>-12.6</td>
</tr>
<tr>
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<td>LFS</td>
<td>No</td>
<td>-17.4</td>
<td>-17.2</td>
</tr>
<tr>
<td>2004</td>
<td>LFS</td>
<td>No</td>
<td>-9.1</td>
<td>-9.5</td>
</tr>
<tr>
<td>2004</td>
<td>LFS</td>
<td>Yes</td>
<td>-6.6</td>
<td>-6.7</td>
</tr>
<tr>
<td>2005</td>
<td>LFS</td>
<td>No</td>
<td>-8.5</td>
<td>-7.4</td>
</tr>
<tr>
<td>2005</td>
<td>LFS</td>
<td>Yes</td>
<td>-2.5</td>
<td>-2.4</td>
</tr>
<tr>
<td>2005</td>
<td>WIF</td>
<td>Yes</td>
<td>-1.4</td>
<td>-2.1</td>
</tr>
</tbody>
</table>

Notes: * Age, education, gender, nationality, number of hours usually worked per week, work place sector and region, rural or urban territory. In brackets are given effects that are not statistically different from zero.

Sources: data source of years 2002 and 2005:
Years 2003 – 2004: CSB LFS econometric analysis, year 2005: WIF employees’ quantitative analysis data

If comparison is made within one group of professions, observed wage difference becomes even smaller and statistically insignificant. The only exception is public sector where according to CSB LFS data contractors in 2004 received by 13.5% and in 2005 even by 20.7% smaller wage. In 2005 this difference even after profession control inclusion remained significant and decreased just slightly. Most likely, this phenomenon can be explained by fact that contractors do not receive different perquisites (for instance, according to managerial contract).

7.4. Occupation and labour income

Figure 15 illustrates full effect of occupation on wage (controlling for only education not sector of activity). As a reference group, to which the other groups of occupational classifier were compared, the ninth basic group was used – elementary occupations where should be the lowest wage and therefore wage differences in other categories would be easier to describe.

It is natural that the highest wage is observed to middle-level managers who belong to subgroup 1.2 of occupations. Similar wages are observed to professionals of social sciences, natural sciences and health care (on average by 63% higher wage than to representatives of elementary occupations).

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Next group where wages are on average by 49 – 54% higher than in elementary occupations is professionals of educational institutions, associate professionals of social sciences, physicists, chemists and professionals of kindred sectors, as well as mining industry and construction employees (see figure 15). These are followed by occupations where higher education is usually necessary. Among groups of occupations named above, employees of mining industry and construction, whose wage is comparable with mental work professions, stand out remarkably.

Figure 13. Wage index by occupations (elementary occupations = 100) (at other equal conditions\(^a\)) in 2005

Notes. \(^a\) Age, education, gender, language skills, type of contract, experience in profession, number of hours usually worked per week, work place sector and region, rural or urban territory.
Associate professionals of natural sciences and health as well as specialists of physics and engineering sciences have by approximately 42 – 43% higher wage than that of elementary occupations. Further, equal wage has been observed to employees of the following professions: metal working and machine building employees, officers, specialists of educational institutions as well as managers or operators of automotive machines and equipment. Representatives of these professions have wage on average by 31% higher than in elementary occupations.

Next group consists of professions where wage is on average by 17 – 26% higher than in elementary occupations. These are: qualified agricultural employees, industrial equipment operators, customer service staff, other workers and craftsmen, operators and assemblers of stationary equipment, as well as individual services and security employees (see figure 15). Models, demonstrators of garments and commodities as well as workers of precision products practically received similar wages to representatives of ordinary professions.

In the WIF study, the data collected during discussions with employers on employee selection and professional offer show that difficulties in finding labor force mainly depend on the sphere of activities of an enterprise and the necessary education (profession) of potential employees. The offer of high-qualified employees is wider and it satisfies the needs of employers. But the offer of low-qualified labor force is insufficient in the labor market despite the unemployment in the country. As to the mid-level employees, this problem does not emerge.

Challenges that an employer has to overcome when looking for and attracting new labor force are mainly connected with the requirements for employees. In other words, it is hard for employers to find appropriate employees that would meet the requirements – education, knowledge, qualification, experience and motivation.

There are also problems in the fields of production and construction as to low-qualified labor force. The employers in these areas think that it is difficult to find employees with the corresponding formation and will to work. An insufficient wage is rarely mentioned as the problem in attracting labor force.

In general, employers mention the following problems with labor force:
- lack of motivation and problem of dependency among potential employees;
- manpower drain abroad;
- low qualification or lack of experience for young workers;
- weak motivation of young employees to master technical specialties.

Employers note that there is a grater change of staff among low-qualified employees than among employees with high-qualification. But sometimes high-qualified employees may have typical inadequate ambitions to the employer.

“Many people think that a good job is one with a warm place, a good office, and the ability to spend half the day on the Internet, to chat with friends for free – and for this they want money.” (Riga, services, micro enterprise)

“Factory work has not been prestigious for the last 15 years because everyone wants a higher education, everyone wants a large salary right from the start.” (Outside Riga, services, medium enterprise)
“Despite the fact that we have little turnover, it’s hard to find good specialists.” (Riga, services, small enterprise)

“Largely the problem is that workers are going abroad (..) Those who remain have a good education and a good job. (..) The average person who wants to progress and can adapt to circumstances and take decisions – that person is gone.” (Outside Riga, retail, micro enterprise)

“As soon as we need an employee, we find one.” (Riga, retail, small enterprise)

7.5. Kind of economic activity and labour income

Observing wage differences by economic sectors, in models of econometric analysis (see table 5.1 and 5.2 in appendix) as a reference group were used employees working in wholesale and retail sector (group G). Two models were estimated. For the first model, both occupation and kind of economic activity were controlled. It means that wage differences are compared between sectors by analysing employees adherent to one basic group of professions (for instance, bookkeepers, engineers, qualified workers etc.). For the second model, only kind of economic activity was controlled. It means that employees of different kinds of economic activity despite their occupation are compared. In both cases, education, age, gender and other individual and enterprise characteristics are controlled for.

If professions of employees are not controlled for, namely, if employees are compared between economic sectors without distinguishing by group of professions (second model), the most high earnings are observed for four kinds of economic activity. They are: construction, electricity and power supply, finances, as well as public administration and social security. The same business activities in different order are the leaders of earnings range when analysing data of CSB LFS for the year of 2004 (see table 6.2 of the appendix).

Next, rather high income group forms such fields: transport, storage and communication, manufacturing, as well as agriculture and forestry. When separating agriculture and forestry (see data of analysis of CSB LFS in table 6.2 of appendix), it is seen that earnings is lower for agriculture, but rather similar for forestry and manufacturing.

Last group with lower labour income forms rest fields. They are: sales and trade, hotels and restaurants, other business activities, education and social and individual services.

In those regression models where professions of employees were controlled for, only in some economic sectors wage differed substantially from the reference group – wholesale and retail sectors. (see table 5 and 6 of the appendix).
7.6. Ethnicity, knowledge of the Latvian language and labour income

Unlike Labour Force Survey of Central Statistical Bureau our survey included question about employees’ knowledge of Latvian. As it is impossible to apply objective criteria to language knowledge (there is no any accepted level system the employees are aware of), in this survey subjective evaluation of employees about their language knowledge is used. Initially it was divided into six levels where the best knowledge of Latvian was denoted as “mother tongue” but the lowest language knowledge by comment “know poorly/do not know at all”.

In several previous studies, it was noted that the considerable wage differences between nationalities observed in Latvia might be explained by knowledge of language and not person's nationality. In regression analysis our primary six language knowledge levels were merged into four levels from which the highest level (mother tongue) was used as a reference group. Other language knowledge groups were good language knowledge, average language knowledge and poor language knowledge.

Controlling for professions of employees and economic sectors, good knowledge of Latvian lowers wage of employee on average by 4.3%. Average language knowledge (employee has some reading, speaking or writing difficulties) indicates to wage decrease by 9.2%. Poor language knowledge parameter is not significant if professions of employees are controlled.

If professions are not controlled, good language knowledge lowers wage by 5.3% compared to people for whom Latvian is a mother tongue, average language knowledge lowers wage by 10.7%, respectively. In such a case poor language knowledge gets its significance which effect coefficient is almost as large as coefficient of average language knowledge – wages are by 10.7% lower compared to employees having Latvian as mother tongue. Although effect of knowledge of Latvian is not large, it becomes very significant if professions are not controlled. That means that language knowledge causes profession segregation – employees having certain knowledge of Latvian concentrate in such professions where language knowledge is not so significant, for instance, work mostly is done in Russian or English, as well as communication during work execution does not play essential role.

In order to check connection between the ethnicity and the wage, representatives of the Russian nation and other nations (including other representatives of nations living in Latvia were included into the models. Two models were evaluated. In thee first model only the variable of the nationality was included. In the second model, the variables of both, the nationality and language skills that are interrelated (i.e. these are characterized by multi-co-linearity) were included. If a strong connection of two variables is observed, only one variable is to be included into the model - the one that explains the best the differences between wages.

In the first model (variable of the nationality), the wage of Russian employees was by 5.2% lower that the wage of Latvian employees (see: Table 5.4. in the appendix). The wage of the rest employees having non-Latvian nationality did not differ form the wage of the group of reference (Latvians) while controlling the rest of parameters.

In the second model with both, the variable of non-Latvian ethnic identify and variable of Latvian language skills, do not show any significant influence on the wage.
Comparison of Latvian language skills and ethnical identity influence on the wage shows that the first factor explains the best the variations of the wages rather than the second does. Although the differences observed do not exclude separate cases of discrimination, is may be assumed that in general employees are not discriminated as to their nationality, and differences in wages arise because of their language skills which is a factor characterizing efficiency.

Importance of the Latvian language skills is brought forward by employers in partly deep interviews while talking about the selection criteria of employees.

“There are virtually no demands for janitors and loaders; they just have to want to work. (..) The demands increase in the higher categories, beginning with Latvian language skills, computer skills, etc.” (Riga, retail, large enterprise)

“There are demands vis-à-vis employees, they must be craftspeople, they must not be drunks. (..) At the higher level there are many requirements – qualifications, education, at least three languages.” (Riga, manufacturing, small enterprise)

In order to continue development of this observation in future, it is recommended to Central Statistical Bureau to include in Labour Force Survey issues on the Latvian language knowledge of employees. Taking into consideration the necessity of foreign language skills, one should also study the level of skills of the English language, the Russian and other foreign languages and their influence on the wage.

7.7. Regions, uzņēmuma lieluma un citu faktoru ietekme uz darba samaku

In econometric analysis of both data that of employees’ survey of WIF research and that of CSB LFS, effects of other factors were examined. Effect of such factors were described: region, size of enterprise, as well as its enterprise activity and possibilities to change workplace of employee.

The data of employees’ survey of WIF research shows that employment in public sector has significant but negative effect on wage of employee – controlling for professions, wage of employees in public sector was on average by 13.3% lower than wage of employees in private sector.

Enterprise size was controlled by standard enterprise size classification – micro (less than 9 employees), small (10 – 49 employees), medium (50 – 249 employees) and large (250 employees and more). Admittedly, respondent indicated number of employees of his direct work place which means that in case of subsidiaries of large enterprises the employee might have mentioned inaccurate enterprise size, i.e., smaller number than it actually is. Therefore, the acquired results, perhaps, would differ if we had opportunity to establish exact number of employees at work places of respondents. Small enterprises (10 – 49 employees) were used as a reference group. In general, our analysis shows that all group parameters of enterprise size have significant effect on wage of employees.
Wage of employees in micro enterprises was on average by 4.8% lower than wage of reference group, and if occupations are not controlled, wage difference is even larger – by 6.4% lower than in small enterprises. Wage in medium enterprises in general was by 5.8% higher than in reference group (without profession control – by 5.3% higher), but in large enterprises – on average by 9.0% higher (by 6.2% if occupations are not controlled).

WIF results of employees’ quantitative survey show also relationship between results of enterprise activity and employees’ wages. Respondents were asked a question if place of their basic work is growing and developing, working without significant changes or are in certain difficulties. Although description of enterprise situation is respondent’s subjective evaluation, its relationship with wage has been observed. Comparing to those enterprises that are growing and developing (reference group), wage in enterprises that work without significant changes is by 9.4% lower. If enterprise is in certain difficulties, wage there is on average by 17.7% lower than in reference group.

As WIF results of employees’ quantitative survey show, if it is very easy for employee to change place of basic work, his wage is by 8.6% higher than of employees for whom it is hard to change work place, other conditions held constant. If it is rather easy to change work, wage is by 4.0% higher than of those for whom it is hard to change.

Regional effects on wage in 2003 – 2005 years period compared to Vidzeme are shown in table 9. It shows both CSB LFS and employees’ survey of WIF research data.

<table>
<thead>
<tr>
<th>Regional effects (versus Vidzeme)</th>
<th>Total Male</th>
<th>Total Female</th>
<th>Male</th>
<th>Female</th>
</tr>
</thead>
<tbody>
<tr>
<td>Riga</td>
<td>31.3</td>
<td>34.4</td>
<td>35.8</td>
<td>35.5</td>
</tr>
<tr>
<td>Pieriga</td>
<td>21.8</td>
<td>21.9</td>
<td>16.7</td>
<td>26.0</td>
</tr>
<tr>
<td>Zemgale</td>
<td>(4.3)</td>
<td>18.3</td>
<td>9.4</td>
<td>9.7</td>
</tr>
<tr>
<td>Kurzeme</td>
<td>(3.8)</td>
<td>(0.7)</td>
<td>(-1.2)</td>
<td>(6.3)</td>
</tr>
<tr>
<td>Latgale</td>
<td>-10.8</td>
<td>(-1.8)</td>
<td>(-6.6)</td>
<td>-14.0</td>
</tr>
</tbody>
</table>

Notes: a Following actual location of enterprise. b Fulltime employees’ sample includes those individuals who consider themselves as fulltime employees and usually work at least 20 hours per week. This definition differs from CSB definition in a way that the former does not include those employees who consider themselves as part-time employees even if they work more than 40 hours per week or more. WAF research definition is closer to Eurostat definition. c Age, education, gender, nationality, contract type, sector of the place of employment and property sector, rural or urban territory. Effects that are not statistically significantly different from zero are given in brackets.
In three regions of Latvia – the city of Riga, Pieriga (district of Riga without Riga, districts of Limbaži, Ogre and Tukums) and in Zemgale (districts of Aizkraukle, Bauska, Dobele, Jēkabpils and Jelgava) the average wage is higher than in the region of Vidzeme (group of reference). Taking into consideration the fact that during the last two years wages in Kurzeme (districts of Kuldīga, Liepāja, Saldu, Talsi and Ventspils) and in Latgale (districts of Balvi, Daugavpils, Krāslava, Ludza, Preiļi and Rēzekne) is not statistically relevant in comparison with Vidzeme (districts of Alūksne, Cēsis, Gulbene, Madona, Valmiera and Valka), it implies that there are two regional groups formed as the wages. The first group includes Riga, Pieriga and Zemgale. The second group includes Vidzeme, Kurzeme and Latgale. Although each large city in all the regions has a definite influence on wages, it is not considered in further details within the framework of the WIF research.

During the last three years wages of employees in Riga exceeded stably the wages in Vidzeme by about one third (see Table 9). Amount of a premium wage of Pieriga, as comparing to Vidzeme, diminishes but is still notable. Comparing with 2003, the position of employees in Zemgale has raised in the “Top of Wages”. It has risen due to the increase of wages in public sector. Wage gap between Latgale and Vidzeme or Kurzeme is not statistically relevant during the period of last two years, but still wages in Latgale remain considerably lower. In general, the wage difference between the district of Riga and the rest of Latvia has a tendency to diminish.

When considering wages in the private sector in each region, there are three main groups formed. The first group includes Riga and Pieriga that is characterized by higher wages. The second group includes regions, the wages of which in the private sector are not statistically relevant. These regions are Vidzeme, Kurzeme and Zemgale. In Latgale, wages in the private sector are considerably lower than in Vidzeme and it constitutes the third group.
VIII WAGE INCREASE

With increasing cost of living and work productivity employees expect wage raise. In this subchapter of the research wage raise in enterprise within last 12 months and affecting factors will be analysed. In order to describe increase of wage fund within last year, data of employers’ quantitative survey were analysed. Changes of wage fund in 2006 were compared to wage fund in 2005, as well as wage raising factors in enterprise were analysed.

Using data of employees’ quantitative analysis, wage growth depending on most significant characteristics of employees and characterizing features of their enterprises were described. Assumption about effect of higher education on wage growth rate was tested. In addition, effect of other discovered factors was described. Using results of employees’ group discussions, attention was paid to person’s potentialities to affect his wage basing on individual qualities.

Opinions mentioned during focus group discussions show that the ability of the employee to influence his wage is not assessed unanimously. Wages depend on subjective and objective factors, but these are of different importance in various sectors and companies. The subjective factors that were mentioned by employees cover two aspects – the quality of the employee as a labour resource and the ability of the individual to stand up for his rights and desires. The goal in the focus group discussions was largely to spend more time on the subjective factors, and as a result of this, these were the factors which were the focus of the greatest attention. Objective factors that were mentioned include supply and demand for labour, including the value of labour productivity. This was mentioned by people with a higher level of income – they are better qualified and have a better sense or understanding of the overall mechanisms through which salaries are determined.

In lower-income groups, respondents were more likely to say that the employee cannot influence his salary that everything depends on the decisions of the employer. Those in the public sector, too, have problems in influencing their salary, because it depends on wage rates at each institution, as well as the national budget. Employers in the private sector have a greater chance to impact on the employee’s salary, but quite often the employee must be self-confident to ensure a good and acceptable wage. Here the importance of dialogue between employer and employee is seen clearly, both sides must reach agreement on mutually accepted circumstances. Some focus group participants spoke of this directly, while others spoke of it indirectly, speaking of their position and experience.

“I got two pay raises in three years. First it was because a new employee asked for a higher salary, his initiative led to higher wages for everyone. After we joined the EU, everyone’s salary was raised by 15%, because the economic situation had changed.” (Medium income, male, RU, Riga)

In some cases a higher wage can be achieved through blackmail, threatening to quit the job. That is effective if the employer appreciates the employee but does not think about the fact that a pay raise is needed or that existing wages become insufficient as time goes by, thus causing dissatisfaction in the employee. Some employees have found that employers who appreciate initiative and proposals award bonuses or other material benefits.
“You can’t ask for money, you have to do a good job. The boss will see that the work has been done well and will pay you not to leave. Compromise is needed. [...] I go to the boss with my proposal. He looks at it and asks what I want in return.” (Medium income, male, LV, outside Riga)

Other focus group participants think that if they ask for a higher salary, they will be sacked, because the employer is not interested in paying higher wages. Pointing to unemployment as an argument, the employer can say that “if you don’t like it, you can leave” and “no one is irreplaceable, we’ll find someone else.” It should be admitted that focus group discussions took place in September of 2005. At that time, the news of lack of labour force and their going to other EU countries had not arisen yet.

“I don’t want to talk to the boss about a higher salary, because then he will raise a fuss about petty things – you were a bit late yesterday, etc. I want to insist on my rights, but I don’t want to lose my job. I’m waiting for him to understand this.” (Medium income, male, RU, Riga)

When it comes to demands for a pay raise, the personal properties of the employee must be taken into account (self-confidence, ability to present arguments) – “not everyone can go to the boss and demand a raise”.

“You have to be able to talk about [the salary] with the boss, lots of people can’t even speak to management about this.” (High income, female, LV, outside Riga)

When talking about wage increase, employees mentioned spontaneously that, as a matter of form, such is validation of undeclared salary, i.e., situation when employer decides to resign “envelope wages”. If an employer decides to change the way in which wages are paid, that is probably his own initiative and decision, and the consequence is usually a slower increase in wages at the company. This result can be dissatisfactory to the employee, if the rate at which wages increase does not cover increased costs (e.g., inflation).

“We had a comical situation. Everyone received wages under the table. The survival minimum went up. I earned LVL 300; the survival minimum was LVL 90. The official wage was increased, but it was taken away from the unofficial wage. The official wage increased, but the overall salary remained unchanged or maybe even declined.” (Medium income, male, RU, Riga)

From the perspective of employees, under-the-table salaries represent a choice between the desire to satisfy one’s needs at a specific level (e.g., only at the level of the official salary) and the level of complaints, and the pressure of unsatisfied needs (the level of discomfort), as well as the system of personal values which permits or does not permit an agreement with the employer. In other cases, also of importance is the nature of informal relations between employee and employer and the level of involvement, which increases the possibility that the difficulties of the employer (competition, a sense of instability, etc.) will be comprehended.

When increasing wages, employers often place greater demands on employees, sometimes arguing that there is a need for greater productivity. Those in the lower-income group spoke of instances when a wage review led to a lower, not a higher salary, and of cases when wages do not change, but work duties are increased.

There are some people who do not want a pay raise, because they think that in that case they will have more work to do – If I’m paid more, then it will be easier to manipulate me. Such
employees usually have other needs or interests – ones which at the moment seem to be more important than a better job or higher wage.

“If your salary is low, then that’s how much you work. If they paid me more, I’d have to do more. You regulate yourself in this regard. You don’t want to work too hard. If my salary was three times higher, I could think about work at home. Now I go home and don’t think about work.” (Low income, female, RU, Riga)

In all groups there were participants who at one point or another worked for a lower salary. Employees spoke of the following situations:

☑ they could not find a job for a long time, they were desperate, and then one does not care what one does;
☑ internships during studies – the first job as long as there is no work experience;
☑ returning to work after child care leave if the previous job has been lost;
☑ changing sectors – until experience in the new profession is accumulated.

However, work for lower wage than a person would like to receive is perceived as “transition period” and in most cases it was for short time.

In WIF survey of both employers and employees, questions were asked about wage raise within the last 12 months. In about one fifth of cases employees had difficulty to answer if wage had been raised. In their turn, majority of employers admitted that wage fund increased in 2006 compared to 2005. In figure 16 it is seen proportion of wage fund in 2005 budged of 2006 amounts to. Main differences are observed by division of region. In Riga, Pieriga and Vidzeme workers’ compensation fund grows more frequently than that of Kurzeme, Lagale and Zemgale.

**Figure 14. Proportion of workers’ compensation fund of 2006 to the fund of 2005**

![Graph showing proportion of workers’ compensation fund](image)

*Note: The results of employers’ survey of WIF research, all employers.*

In about one fourth of enterprises wage budged remained the same or slightly increased. The most characteristic proportion of wage fund increase against previous year is 110% (in 28% of cases). Data of WIF employees’ quantitative survey show that average wage raise was 9.2%. This value was calculated considering both employees whose wage was not raised
within the last 12 months and those whose wage was raised, as well as amount of raised wage. The estimated figure is smaller than average gross wage raise in previous year calculated by CSB. Thus, we can assume that proportion of declared and undeclared wage have slightly changed and real wage has grown less than statistics shows. However, WIF employees’ survey data show that to employees who did not have contract of employment wage was raised considerably more rarely than if contract of employment was concluded. In its turn it means that unofficial wage is legalized when contract of employment is concluded with employee.

Figure 17 shows wage raise criteria named by employees depending on qualification of employee.

**Figure 17. Wage increase criteria by categories of employees**

<table>
<thead>
<tr>
<th>Criteria</th>
<th>High qualified workers</th>
<th>Medium qualified workers</th>
<th>Low qualified workers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rise of the minimum wage in our country</td>
<td>53</td>
<td>55</td>
<td>67</td>
</tr>
<tr>
<td>The official inflation in our country</td>
<td>53</td>
<td>51</td>
<td>53</td>
</tr>
<tr>
<td>Increase of amount of work</td>
<td>36</td>
<td>40</td>
<td>34</td>
</tr>
<tr>
<td>Advance in worker’s qualification</td>
<td>29</td>
<td>29</td>
<td>18</td>
</tr>
<tr>
<td>Increase of working quality and efficiency</td>
<td>26</td>
<td>26</td>
<td>18</td>
</tr>
<tr>
<td>Remuneration at other enterprises</td>
<td>21</td>
<td>20</td>
<td>15</td>
</tr>
<tr>
<td>Job tenure of employee</td>
<td>19</td>
<td>18</td>
<td>10</td>
</tr>
</tbody>
</table>

*Note:* The results of employers’ survey of WIF research. Criteria are shown for enterprises where workers of particular qualification exist. Wage increase criteria are multiple answers’ question.

Figure 17 shows that minimum wage raise in the state is the most significant factor in case of remuneration of low qualified employees. Increase of qualification and work productivity of employee are the most significant factors to wage raise of employees with high and medium qualification.

Data of WIF employees’ survey show that little positive effect of certain educational levels on wage raise is observed. Compared to general secondary education, higher education and industrial education after elementary education had significant positive effect on possibility that wage has been raised within the last 12 months, at other conditions being equivalent. The positive effect of industrial education might be caused by necessity to raise wage if minimum wage grows, as well as labour shortage in certain sectors. Considering proportion of raised wage, sustained effect of several educational levels was observed. Little still statistically significant effect is characteristic to higher education, vocational education after secondary
education and industrial education after elementary education compared to general secondary education.

Initiating the research, it was assumed that more positive effect on wage raise is given by higher education. Data of the research show that several educational levels have positive effect, although there might be different reasons for wage raise. For lower skilled employees it might be labour shortage in certain economic sectors, raise of minimum wage and increasing cost of living. Raise of qualification would be additional motive for wage raise of highly qualified employees.
IX CONCLUSIONS AND RECOMMENDATIONS

Fixed basic wage is a relevant component of the salary in the Latvian enterprises. Other kinds of monetary (additional payments, premium wages) and non-monetary remuneration (health insurance, training courses paid by the enterprise, coverall, equipment, etc.) are used mainly in medium and large enterprises.

The results of the WIF research show that in the majority of cases (~90%) employees receive fixed basic wage, but in 40% of cases it is supplemented or substituted by a variable basic wage. Paying fixed and variable basic wage depends on the qualification of an employee and the size of an enterprise. The higher the qualification is, the greater the possibility of receiving fixed basic wage is rather than variable basic wage. Fixed basic wage in micro and small enterprises (fewer than 19 employees) is paid more seldom than in the rest of enterprises.

For the majority of enterprises, basic wage constituted 71% of the total workers compensation paid in 2005. Almost in one third of enterprises the specific weight of the basic wage in the total workers compensation fund varied from 81% to 90%. Almost in the fifth part of enterprises the basic wage constituted the entire payment of wages. A situation like this can be more frequently observed in the sector of trade, hotel and catering service and in the field of private services. When considering regions, this characterizes also the regions of Zemgale and Latgale. The portion of the basic wage that reaches 70% from the total remuneration was observed in the fifth part of enterprises.

Depending on the specific weight of the basic wage in remuneration, enterprises of Latvia fall into two groups. Comparatively small enterprises are characterized by high specific weight of the basic wage in the whole labour remuneration. In comparatively large enterprises, the proportion of the basic wage in the entire payment of wages is smaller.

After the basic wage, the next most popular category of labour remuneration is additional payment for extra hours, and these are followed by occasional premium wages. Workers with a medium and low qualification receive additional payment for extra hours more frequently than high-qualified employees. It is important to note that the subjective perception of remuneration for extra hours and premium wages differ between employers and employees: these payments are higher when evaluated by employers rather than by employees.

Analysis of premium wages and additional payments show that the application of individual motivation or common collective motivation is popular. Additional payments for the results of a team or a department are not spread in Latvia. Additional payments for the work of a team or department are rarely practiced in micro and small enterprises for evident reasons, i.e. the number of employees usually corresponds to the number of employees of one department in a medium or large enterprise. However, medium and large enterprises are not very much characterized by addition payments for work of team.

In general, the size of an enterprise has a relevant influence on all kinds of additional payments for employees: the larger an enterprise is, the greater the possibility is that premium wages, additional payments for the results of an enterprise and individual work, for performance of additional duties and extra hours will be paid. Although the data show that
extra hours are mainly remunerated, it is not paid in a double amount as the Labour Law provides. Remuneration of extra hours is paid to employees of a relatively higher public sector in comparison with the employees in the private sector.

Employers usually indicate that the requirements that are set for extra hours are too high and they propose to lessen the requirements of this norm of the Labour Law. Practically, remuneration of extra hours does not correspond to the legislation at the moment. This is why it would be advisable for the Ministry of Welfare in cooperation with social partners to agree on the most appropriate conditions. When elaborating an optimal order of remuneration of extra hours the tendencies, the average amount of extra hours (overworked hours) described in the WIF study and the operative administrative order should be taken into consideration.

When favouring the wage in correspondence with efficiency of work, it is advisable for the Ministry of Welfare and its social partners to popularize practicing of variable basic wages, hourly pay and additional payments for productivity of work in enterprises of Latvia.

The hypothesis of the WIF study that additional payments that are paid for the productivity of work or in accordance with the financial indices of an enterprise is one of the mechanisms how to legally and flexibly react to deterioration of activity indices or macroeconomic environment of an enterprise is proved only partly. In the in-depth interviews of employers, it was recognized that attaching of the wage to the productivity of work motivates employees of an enterprise and ameliorate productivity of work as well as permit to reduce wages and deterioration of activity indices within an enterprise. In the analysis of quantitative surveys of employees, the remarkable statistical regularities between financial indices of an enterprise and the structure of remuneration were not discovered. However, other regularities observed in the study that characterize productivity of an enterprise indirectly show that the assumption of the hypothesis might prove. A variable basic wage which is attached to productivity is a rather popular form of remuneration. A fixed basic wage is less characteristic for micro and small enterprises, the position of which in the labour market is not stable. The econometric analysis of the data of quantitative survey of employees shows that the wage in enterprises that grow and develop is higher than in enterprises that operate without considerable changes or undergo certain difficulties.

The data of the WIF research show that one forth of employers considers the net wage to be the basic when defining wages within an enterprise. Analysis of this practice in various groups of enterprises as well as data on the number of the minimum wage receivers let to draw the conclusion that a part of small enterprises tend to evade taxation for their employees. It is more difficult to follow the national tax policy for small and micro enterprises. At large extent, it is caused by inadequate requirements of the legislation as to the resources of employers to keep the regulations and to ensure the possibilities of enterprise existence and development, which, in its turn, favours “pay-envelope” remuneration form.

There is a tendency that “pay-envelopes” are more widespread in micro and small enterprises that are situated outside Riga as well as in enterprises with frequent staff change. They are usually paid to the low or middle level employees as well as to seasonal workers.

The wage of employees who have not concluded labour contract is statistically lower than for employees who have the labour contract. Thus an employee gets benefit from partly paid taxes only in case if he has at least a formal labour contract. Thus the affirmation that an
employee without the labour contract receives higher wage at the expense of unpaid duties is delusive.

The hypothesis of the study that the amount of unregistered remuneration reduces due to the growth of an enterprise is not statistically proven. However, in the data of quantitative survey of employees there is regularity between the probability of undeclared wage payment and evaluation of situation within an enterprise. If an enterprise grows and develops or it operates without considerable changes, then the probability of illegal wage practice within an enterprise is lower. Whereas, if an enterprise undergoes difficulties, the probability of unregistered wage practice is higher. All the above mentioned results of the research confirm once more that providing enterprises with favourable environment for them to develop should be the most important political aim.

In addition to the wage and different additional payments, about a half of employed people receive at least one non-monetary form of remuneration. The most frequent non-monetary remuneration forms are: health insurance policy, presents for employees of an enterprise, refunded trips, education or participation in training courses, compensation of mobile phone expenses, transport and feeding as well as other kinds of support for an employee. Availability of non-monetary remuneration is closely related to the profession of an employee and his/her position within an enterprise.

Qualified employees, operators of equipment or machinery and low-qualified employees receive coveralls refunded by an enterprise, health insurance and present the most frequently. Employees in service rendering and trade receive also feeding compensation and provision in addition to the three above mentioned remuneration forms. The largest range of non-monetary remuneration is offered to middle level managers, for the professionals of a particular field as well as to associate professionals. The representatives of these occupations may receive health insurance, refunded training courses, formation and participation in seminars, presents from an enterprise, compensation for mobile phone talks as well as there is a possibility of using a part of a business trip for personal purposes.

The most important factors that define the amount and range of non-monetary remuneration for employees are as follows: category of an employee and the position, the amount of the fulfilled work, its quality, turnover and the size of an enterprise, positive motivation of employees and the desire of an employee to hold stable, high-qualified, experienced, reliable and motivated employees in an enterprise.

The category and position of an employee is closely related to his/her education. The higher the education is, the higher his/her wage is. Moreover, employees with higher education work in better remunerated work. A greater positive impact of higher education has been observed on the wage of female and employees occupied in public sector. However, generally the wage of female is for about one fifth lower than the wage of a male when comparing people working in the same occupation of the same field of national economy. At other equal conditions, the wage of employee occupied in the public sector is by 13% to 14% lower than of employee working in the private sector.

The hypothesis of the study on regularities in non-monetary remuneration was proven only partly. On the one hand, the assumption that availability of non-material values increase along the growth of the position was confirmed. On the other, the assumption that benefiting from non-material values in addition to the wage is more characteristic for the sphere of service
rendering than for other sectors of the national economy turned out to be false. No significant
differences in the offer of additional benefits as to the sphere of the national economy were
noticed. It is more likely that there is a link between additional benefit and qualitative
(substantial) differences not only considering the sphere of activities of an enterprise but also
the occupation.

Other regularities found out in the quantitative survey of employees carried out in the
framework of the WIF study witness that the possibility of receiving non-monetary
remuneration is promoted by the size of the enterprise where he/she works (the number of
employees) and existence of concluded collective agreement in it. This means that together
with the growth of an enterprise, the possibility that an employee will be granted at least one
benefit supplementing the wage also rises. The collective agreement concluded in an
enterprise increases the possibility that the employees of an enterprise will be granted at least
one supplementary benefit. It is to be noted that there is regularity between these two
observations, for collective agreements are the most frequently concluded in large enterprises.

Considering other factors that influence the wage, the importance of ethnic factor was
mentioned in studies. The results of the WIF research show that the wage difference among
representatives of various nationalities in Latvia can be explained by language skills not their
nationality. Language skills also create segregation of occupations – employees with a lower
level of the Latvian language skills are concentrated in the occupations where the language
skills are not relevant, for example, work is mainly done using the Russian or the English
language as well as communications does not play great role in work. Although these
differences do not exclude cases of discrimination, there still is the reason to affirm that no
direct ethnic discrimination was observed as to the wage. Difference in wages occurs because
of the Latvian language skills which in many cases is the factor that ameliorates productivity.

In order to analyze and understand this regularity, it is advisable for the Central Statistical
Department to include questions on the Latvian language skills if employees into the Labour
Force study. Taking into consideration the necessity of using foreign languages in work, the
English and the Russian language skills as well as skills of other foreign languages and their
influence on the wage should also be analyzed.

The data of the study prove the hypothesis that belonging to so-called “risk groups” diminish
the level of demands of an employee in the labour market by agreeing on the wage with the
employer. It is proven by opinions expressed in the discussions of different groups of
employees and econometric analysis.

The highest point of labour remuneration or the highest wage both, for male and female is
attained comparatively fast in all levels of education – in average this is the age of 30 to 35.
Although the WIF team expected that the age of employees then they receive the highest
wage would grow in comparison with the previous year, the WIF study shows a very similar
division. In general, it can be admitted that the point of maximal income is still situated far
from the average index of the EU. This means that education and experience obtained earlier
still has a greater market value. The flexion of income and age profile show that as the age
grows, incomes reduces.

In general, when comparing female earnings, the remarkable statistical differences of those
which have children under the age of two years were not discovered. However, WIF team
advanced a hypothesis when considering that female searching a new workplace after child
care leave; then her level of demands would be lower than in other cases. This assumption was proved within focus group discussions where female told that they accepted to work for lower wage when searching a workplace after child care leave. However, it should be noted that, in general, for all employees who work at company for the first year labour income is lower.

Employed people frequently say that they reduce the level of their demands as to the wage in the situation when they have become unemployed due to various reasons. Work with small wage is considered as a transitional period by all except for employees of pre-retirement age and separate groups of employees, during which one can obtain experience, definite success, to prove oneself and to find a better remunerated job.

Concerning the factors that influence wages within an enterprise, one of the most important one is the size of an enterprise. Regularity has been observed that as the size of an enterprise grows, the average wage within it becomes higher.

The influence of the kind of economic activity of an enterprise on the wage is analyzed not separating belonging of an employee to a definite group of professions. In this case the highest wage in Latvia was observed in the following sectors: construction, energy and power supply, finance as well as state administration and social insurance. These are followed by the sectors of transport and communications and manufacturing industry.

The hypothesis that the phenomenon of labour units is greatly related to the soviet times was proven in the study. But this relation is greater than that of possible alternative and activities of powerful employee associations in the Western Europe. However, in relation to the traditions of the soviet time, not always they were the weak point of labour unions. Though this association was considered a negative phenomenon, a labour union as association for protection of employed people could be called a benefit.

According to the viewpoint of employees both, the state institutions and labour unions are too weak these days in order to defend employees. This is why the latter have to rely on themselves by agreeing on the wage with their employer. High-qualified employees are more confident about their ability to achieve higher wage.

In the majority of Latvian companies the wages fund has increased during the last year, but the rate of increase in alternate enterprises is small which can be compared to the rise in prices in the country. Opinions expressed by employers confirm that macroeconomic factors (inflation and increase of the minimum wage in the country) influence more the rise of wages than success of a particular employee of the remuneration rate within the sector does.

Rise of the minimum wage in the country is the main factor that is taken into account by employers when increasing wages for low-qualified employees. Qualification of an employee and rise of productivity are more important factors for rise of wages of medium qualification and low-qualified employees.

The hypothesis that the quality of education and its regular improvement has a positive influence on the wage and the rate of it is growth is partly proven. The higher education the respondent has, the higher his/her wage is. In general, all levels of higher education bring a positive effect on the wage of employees as compared to the secondary education. However, the rate of wage increase at the moment is similar in several levels of education. This most
probably is related to the present situation in the labour market. The rise of the statutory minimum wage and labour force drain to foreign countries favours the rise of the wage for employees with different levels of education.

In the WIF study, it can be observed that employers accentuate that they are in need of appropriate labour force at the moment. This phenomenon has three reasons. The first is the labour force drain to other member states of the European Union, the second is lack of motivation and inadequate demands, and the third is lack of interest about particular definite occupations. It is considered that the first two reasons create the rise of wages that does not correspond to rise of work productivity. It is observed that here is lack of employees in the fields that have comparatively high wages (for instance, in construction and industry). It is advisable for the Ministry of Welfare and social partners to participate in informing the society about the factors that influence the wage as well as forming an adequate conception of the proportion of wages and prices of services and goods in the Western World. There should be understanding created that in the EU member states there are not only wages higher but prices of everyday goods and services, too.

Despite the fact that rise of minimum wage makes enterer rises to increase the wage within it, it will not diminish the number of employees in the Latvian enterprises according to the opinion of employers. The optimal rate of minimum wage and untaxed minimum named by employers differ considerably from that proposed by the state. In 2006, the minimum wage in Latvia is 90 lats and the untaxed minimum is 32 lats. The employers’ survey that had been conducted at the beginning of 2006 showed that the majority of employers supported both, increase of the minimum wage and untaxed minimum. The median of the suggested minimum wage was 160 lats and that of the untaxed minimum – 90 lats.

Evaluation of the minimum wage and the untaxed minimum varies as to the region of activities and its size as well as to other parameters. Opinions on the rate of the minimum wage differ the most when considering regions. In Kurzeme, Zemgale and Latgale, the wage that is considerably lower than that in Riga, the Pieriga and Vidzeme is optimal one. Although the majority of employers admit that the rise of the minimum wage by 50% (i.e. up to 135 lats) would not decrease the number of employees in their enterprise, but those of regions and sectors of activities that have mentioned lower optimal minimum wage would suffer the most. The rise of the minimum wage would affect the small employers in the regions of Kurzeme and Latgale the most. The obtained result let to assume that idea of minimum wage differentiation or differentiation of the increase rate is to be encouraged.

In other research and in the WIF study, differences in wages and remuneration structure were observed considering the statistical regions. As to the rate of wages, there are two main groups of regions. Them being rather different, the first group comprises Riga, Pieriga and Zemgale where the wage rate is comparatively high. The second group includes Vidzeme, Kurzeme and Latgale, between which there have been no relevant statistical differences as to the labour income observed. When considering wages in the private sector in the regions, there are three groups of regions formed. The first is Riga and Pieriga having a higher level of wages. The second is formed by three regions between which the wage differences are not statistically relevant. These regions are Vidzeme, Kurzeme and Zemgale. The wage in Latgale in the private sector is considerably lower that in Vidzeme, and it forms the third group.

Considering the proportion of the basic wage in the total workers compensation, there are two groups of regions formed. A relevantly higher portion of basic wage is in Zemgale and
Latgale. The wages fund has increased in Riga, Pieriga and Vidzeme lately. In Kurzeme, Latgale and Zemgale, the rise has not been so drastic.

In general, the wage in Riga and Pieriga differs considerably from the wage in other regions. However, the optimal minimum wage suggested by employees in Riga and Pieriga differ less from that of the other regions than the variations of wages. The reason for such a prudent evaluation could be the fact that an enterprise operates not only in Riga of the Riga basin but also in other regions of Latvia.
X FIELD POLICY ALTERNATIVES OF WAGE CONTROL

The purpose of the research “Wages and Their Impacting Factors” (WIF) was also to conduct cost benefit analysis and to develop the promotion plan for the three alternatives chosen by the Ministry of Welfare (MW). For deeper analysis, it was selected the following solutions:

1. The determination of the most suitable algorithm according to The Concept Paper of the Minimum Wage promotion in the year of 2009 so that the minimal wage during the next 5 – 6 years would reach 68% ratio of the national average salary considering the rate of the productivity increase;
2. The differentiation of the minimal wage for the three industries of the most non-declared employment risk (construction, retail and timber work) considering the amount of income within the limits of non-declared employment;
3. The analysis of the promotion of the practical implementation of Article 18 regulations of the Labour Law.

WIF work group would like to pay attention that contracting authority’s chosen alternatives are not the only regulative mechanisms of the certain industry and that one of those mechanisms must be established in Latvia. In the summary several solutions are analyzed which gives us the opportunity to handle the labour market environment in Latvia from different point of view. They can encourage the new discussions or other retrievals for the suitable mechanism of the regulation of wages in Latvia.

10.1. Determination of minimum wage and algorithm for its increase

The first alternative raised by the Ministry of Welfare is the determination of the most suitable algorithm according to The Concept Paper of the Minimum Wage promotion in the year of 2009 so that the minimal wage during the next 5 – 6 years would reach 68% of the national average wage considering the rate of the productivity increase.

10.1.1. General case study

Ideas about the amount of the minimum wage that is based on the average wage in the country come from the book by Lenia Samuel *Fundamental Social Rights Case Law of the European Social Charter*, where Chapter 4 is dedicated to the notion of fair remuneration. The author analyses mechanisms how to introduce in practice the right of employees to remuneration set out in the Social Charter that would ensure them and their family adequate living conditions. The author has worked on the Management Committee of the European Social Charter and has dedicated a publication to the case law of the Committee of Independent Experts of the European Social Charter.
L. Samuel points out that the recommendation for a desirable amount of the minimum wage arises from the studies analysed by the committee of independent experts regarding the amount of “decency threshold” (poverty threshold) of the earnings. This analysis was based on two studies performed in the mid-1970s, which concluded that the “decency threshold” was 66% of the national income per individual or about 68% of the average earnings in the country (Samuel 1997: 78). Both mentioned studies were not available to the WIF team therefore it is impossible to assess concomitant circumstances which could have affected the result – the definitions of the notions “average earnings” and “poverty (decency) threshold”, the countries where the analysis was performed, the socio-economic situation in these countries and other relevant factors.

Here the notion “average earnings” has a particular importance in order to calculate the proportion of the minimum wage versus the average wage in the country. For instance, the Central Statistical Bureau of Latvia (CSB) provides statistics for the average earnings that are calculated including not only the basic wage but also bonuses and premiums. The proportion of the minimum wage only versus the gross basic wage will be higher than versus salary. L. Samuel does not give a precise definition what indices (basic wage, salary, including bonuses) should be used to calculate the minimum wage and here is a ground for discussions about the point of reference.

L. Samuel indicates that analysing the introduction in practice of the system based on the above mentioned calculations, the management committee in co-operation with the governmental representatives of the states summarised data on tax relieves and state-allocated allowances (family allowances, household allowances, etc.) in order to decide on the necessary minimum income for the below mentioned employees. The information was gathered about low-paid employees of three categories – (1) married employees with two children, (2) single parents with two children, (3) unmarried employees and without children. If as a result of material and social changes the wages of low-paid employees increased up to 68%, then, according to the experts, “fair remuneration” would be achieved. Further on, the author states that the opinion of governments of the involved countries on this issue was more cautious. They held a view that a more flexible approach would be a development of a special tax policy for taxation of income of the low-paid employees. Another approach is an application of additional instruments if fair remuneration is not achieved. Here the WIF team would like to add that the cautious approach of governments is reasonable because a relatively high minimum wage, what the level 68% of the national average wage is considered to be, is an inflexible instrument regulating the remuneration system.

It should be noted that none of the European Union member states has introduced this idea. It is demonstrated by the so-called Kaitz index that sets the minimum wage as a proportion of the average monthly gross earnings. The comparison of the index shows how far the countries are from the full introduction in practice of the discussed idea. Analysing the Kaitz index for EU member states and applicant countries, where law prescribes the minimum wage, they can be theoretically divided into three groups (Funk, Lesch 2005). The first group, where the Kaitz index varies between 29% and 38%, includes the following countries: the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania and Spain. The second group, where the index varies between 40% and 44%, includes Bulgaria, Cyprus, Malta, Slovakia, Slovenia and the United Kingdom (Great Britain). In the third group the Kaitz index is higher than 45%, yet its maximum actual limit is 51%. This group includes Greece and Ireland and, referring to older data, we may also include Belgium, France and the Netherlands (Funk, Lesch 2005).
Over the last ten years the dynamics of the Kaitz index is not steadily growing. Its value is relatively stable for France, Ireland, the Netherlands and Slovenia. In other countries the legally established minimum wage grows more rapidly than the average gross earnings and thus, the proportion of the minimum wage versus the average wage increases (for Estonia, Latvia and Great Britain). In some countries the proportion of the minimum wage is decreasing. It is characteristic of Belgium, Malta, Poland, Romania and Spain. In some other countries dynamics of the minimum wage has been changeable – some years faster, some years slower. It is characteristic of Bulgaria, the Czech Republic, Hungary, Lithuania, Malta and Slovakia (Funk, Lesch 2005). The viewed data shows that neither in the old, nor in the new EU member states, nor in the applicant countries the idea set out in the policy alternative has been implemented during the last ten years. Practically, the highest observed proportion of the minimum wage versus the average one in 2004 was in Ireland (51%) and in 1995 – in Belgium and Malta (52%).

On the basis of the viewed statistics the WIF team concluded that assessing the policy alternative several scenarios of results should be considered. They represent several alternative tempos of the minimum wage raise and a comparison of scenarios helps assess both the necessary investments and the social benefits.

Determining the most appropriate algorithm for increasing the minimum wage according to The Concept Paper of the Minimum Wage elaborated by the Latvian Ministry of Welfare and approved on 28 May, 2003 by Order No. 356 of the Cabinet of Ministers of the Republic of Latvia for introduction in 2009, at first the existing government’s achievements in defining the minimum wage had to be assessed. The concept envisaged that after 2009 the minimum wage would have reached 50% of the national average wage. However, considering the existing situation when the average salary in the country grow much faster than it was initially planned and when so far social partners have had difficulties agreeing on a raise of the minimum wage, the working group assumed that the aim set by the Concept will not be achieved till 2010. The summary of the situation is reflected in Table10.

| Table 10. Forecasts of the Concept Paper of the Minimum Wage and comparison of their implementation |
|-------------------------------------------------|----------|----------|----------|----------|----------|
| Average gross earnings and minimum wage expected in the Concept Paper of the Minimum Wage |
| Forecast average gross earnings of employees per month, LVL | 198 | 212 | 227 | 243 | 260 | 278 |
| Forecast minimum wage, LVL | 88 | 97 | 106 | 116 | 127 | 139 |
| Minimum wage versus average gross earnings, % | 44% | 46% | 47% | 48% | 49% | 50% |

| CSB data and average gross earnings forecast by Ministry of Finance |
|-------------------------------------------------|----------|----------|----------|----------|----------|
| Forecast average gross earnings of employees per month, LVL | 211 | 246 | 279 | 313 | 348 | 385 |
| Forecast minimum wage, LVL | 80 | 80 | 90 | - | - | - |
| Minimum wage versus average gross earnings, % | 38% | 33% | 32% | - | - | - |

Note: Forecasts are unpublished materials of the Ministry of Finance on development of macroeconomic indices.
From 2004 till 2005 the changes in the minimum wage have not been implemented according to the Concept Paper while the average gross earnings have increased more rapidly than it was planned in 2003 (see Table 10). As a result, the minimum wage instead of approaching 50% of the average gross earnings in the country is declining from this level. In the further analysis it is assumed that from 2007 till 2009 the aim of the Concept Paper will be partially attained – the minimum wage will constitute 140 lats. However, on the basis of the currently available prognoses such an amount of the minimum wage will only correspond to a 36.4% level of the average gross earnings in 2009.

The next important aspect is a scenario of the national economic development till and after 2010. During the assessment of alternatives much attention was paid to the discussions of governments, social partners and various experts about the necessity to reduce the personal income tax and about the possible consequences of this action. Therefore one of the tasks of experts’ inquiry was to find out what scenario of Latvia’s development is most likely to come true. Overall experts were asked to assess the probability of the following scenarios:

- starting from 2010 the minimum wage in Latvia will reach approximately LVL 140 and the untaxed minimum – LVL 70 if the personal income tax rate remains the same at 25%;
- starting from 2010 the minimum wage will reach approximately LVL 140 and the untaxed minimum – LVL 70 if the government implements the approved conceptual decision and the personal income tax rate till 2009 falls to 15%;
- till 2010 the minimum wage will increase constituting 50% of the average gross (legal) earnings of employees in the previous year if the personal income tax remains at 25% and the untaxed minimum grows at a set pace (to LVL 70 per month);
- till 2010 the minimum wage will increase constituting 50% of the average gross (legal) earnings of employees in the previous year if the personal income tax decreases to 15% and the untaxed minimum increases at a set pace (to LVL 70 per month);
- till 2010 the minimum wage will increase to LVL 140, the untaxed minimum – to LVL 70 and the personal income tax rate will be reduced to 22%.

The last scenario was added starting from the second round of expert interviews because several specialists believed that the personal income tax would not be reduced as planned. When the Latvian government has gone through the first stage of personal income tax reduction, it will feel the consequences of this action – decrease of income in the state budget. Although politicians will be eager to show their willingness to reduce the personal income tax, there will be great obstacles to balance the national general budget. As a result, reduction of the personal income tax rate will be interrupted and the minimum wage and the untaxed minimum will have to be increased in order to restrict migration and to compensate for inflation effects.

Experts considered that it was 60% probable that in 2010 the minimum wage will reach LVL 140, the untaxed minimum – LVL 70 and the personal income tax will remain at 25%. Evaluating several other scenarios of changing the minimum wage, untaxed minimum and personal income tax, two possibilities, which differ only in the amount of the personal income tax, seemed to be most probable. Experts believe that both possibilities - that the personal income tax will be 25% or that it will decrease to 22% - are plausible. It is estimated that a larger reduction of the personal income tax is not possible.

The main reasons why the other scenarios are less probable are the rapid increase of gross earnings of employees, the fiscal goals of the state (necessity to introduce the Euro), the
decline of corporate competitiveness and possible problems related to the reduction of the personal income tax as well as possible problems related to the legally established fines that are pegged to the minimum wage.

If the growth rate of the average gross earnings remains the same, an attempt to increase the minimum wage to a 50% level of the average gross earnings in the national economy till 2010 will fail. It would inflict too rapid a raise of the minimum wage that will have a negative impact on employment and entrepreneurial activities in less economically developed regions of the country where the minimum wage due to low efficiency of the labour force is binding both for employees and employers (see experience of other countries, e.g. Hungary).

If the minimum wage was increased faster than the labour efficiency of these companies, they would have to be forced to cease their operation, to falsify accounts of labour working time (to register employees as part-time workers in order to avoid the minimum wage level for full-time workers) or to terminate official employment relations with their employees.

Before the introduction of the Euro it is necessary to ensure a reasonable inflation level in the country. Currently, the inflation level considerably exceeds the set inflation criterion: the average inflation level in the last 12 months must not exceed the average level of three leading member states by more than 1.5 percentage points. According to this criterion, in March 2006, the permissible inflation level was 2.6% while in Latvia the inflation almost reached 7%. The rapid increase of the minimum wage would affect the prices of goods and services (cost inflation) while retaining the inflation at the level existing in the country or even increasing it and thus preventing the country from the planned introduction of the Euro.

Speaking about the personal income tax, currently it is the most important source of income for state municipalities. Its reduction from 25% to 15% may considerably decrease municipal budgets, thus also limiting ability of municipalities to perform their functions.

Although publicly there are many references to the example that when the corporate income tax was reduced the income rather increased than decreased, it should be pointed out that the reduction of the personal income tax and the corporate income tax cannot be compared as two similar cases.

The ownership structure of Latvia’s enterprises and corporate tax rates in the EU may be the main reasons accounting for a positive effect. The most part of profitable Latvia’s companies are subsidiaries of foreign enterprises and their owners may have various considerations whether to keep or not the profit and in which country. The low corporate income tax rate in Latvia may appear appealing if the laws in another European country provide for a higher corporate income tax rate. The reduction of this tax rate could have affected the decision to keep the profit in Latvia if the corporate income tax was smaller than in another country.

The cited reasons do not exist in case with the personal income tax, therefore the increase of income cannot be facilitated from the personal income tax. The only incentive for individuals may be a psychological factor implying that it is not worth risking and hiding the real income if it is taxed at such a low rate.

In the research of the Ministry of Finance “Information on Reduction of Personal Income Tax and Related Financial and Socio-economic Aspects” (Ministry of Finances 2006), a considerable decrease of the collected personal income tax is expected what is the main
argument against the introduction of such a reduction. Yet, despite that the Latvian Parliament (Saeima) has conceptually supported the amendments elaborated by the Budget and Finance (Tax) Commission to the Law on Personal Income Tax (the draft law has not been adopted yet), providing for a reduction of the personal income tax rate from 2007 till 2009 (from 2007 reducing the personal income tax from 25% to 22%, in 2008 – to 19% and in 2009 – to 15%).

The compensation from budget resources for public sector employee wages that are pegged to the minimum wage, e.g. teacher wages the amount of which must not fall below two minimum wages, may exert much greater pressure on the state budget. A rapid increase of the minimum wage may lead to a situation when provision of appropriate funds in the budget for compensation of these wages will be problematic. Taking into account the probability that the personal income tax may be reduced, it is necessary to consider a possibility to depart from the existing practice when teacher salaries are pegged to the minimum wage. On the other hand, while teacher salary is low, compared to other occupations where higher education is required, the slowing down of the teacher salaries growth rate may have a negative effect – a more severe shortage of teachers.

10.1.2. Base scenario of minimum wage increase

Base scenario is a situation based on which the basic algorithm for the increase of the minimum wage will be developed and against which several other scenarios for increasing the minimum wage will be compared.

According to expert evaluation, the highest probability had a scenario in which minimum wage in 2010 would be 140 lats, untaxed minimum – 70 lats and personal income tax rate – 25%. Hereafter, these conditions are assumed as base scenario. All assumptions and further calculations are shown in Table 7 of the Appendix.

As part of all scenarios their impact on the forecast of the state tax revenues will be looked at (both the personal income tax and the mandatory social insurance contributions). The base scenario envisages further increase of the minimum wage with a view that the gross minimum wage in 2010 will be 140 lats and that in 2020 it will reach 50% of the gross average earnings in the country during the previous year. To that end the proportion of the minimum wage should grow by 10% per year on average by 2020. Initially, during the last phase of the expert assessment, most specialists were unanimous that the minimum wage could reach 68% of the average earnings as soon as in 2020. However, developing in practice of that scenario reveals that the growth rate of the minimum wage has to be so rapid that it is impossible to implement.

Those experts who disagreed with the proposal to set the minimum wage at 68% of the gross earnings in the country cited two reasons for it. The first reason coincided with the estimates carried out by the WIF research team, namely, that it is not possible to raise the minimum wage to 68% of the gross average earnings in such a short while. The second reason was rejecting in principle by experts of the idea being studied: such a scenario is not appropriate for Latvia and should not be introduced altogether. They added that a development scenario whereby the minimum wage would reach 50% of the average gross earnings is a good enough target.
At present the minimum wage increase, as envisaged under the base scenario, complies with the estimates on increase of the gross average earnings as elaborated by the Ministry of Finance. The growth rate of the gross average earnings may differ as a result of deviations from the values of variables provided under prognosis (changes in personal income tax rate, faster increase of the minimum wage) – it may accelerate if the minimum wage grows faster than provided under the base scenario while decelerate if the minimum wage grows at a slower pace.

In all models for estimating the personal income tax account is being taken of both the untaxed minimum which is pegged to the minimum wage at 50% of its level and dependency allowances, pegged to the untaxed minimum at 75% of its level (the concept worked out by the government envisages that tax alleviation level to be reached in 2010 will amount to 53 lats with the minimum wage being 140 lats).

The WIF team assumes that both the untaxed minimum relative to the minimum wage and the personal income tax dependency allowances for each dependent person of the employed person relative to the untaxed minimum will be retained after 2010 because those values should trail the change of the minimum wage. Both abovementioned instruments are being used to alleviate tax burden for low paid employees and representatives of certain risks groups (families with children) and there are grounds to believe that such support policy will continue after 2010.

In order to establish the average number of dependent persons per employee the present analyses will use the ratio of the number of pre-work age people against the total number of employed persons. According to data of the Central Statistical Bureau (CSB) (CSB data base in the internet, table “Main Age Groups of Permanent Residents at the Beginning of the Year”) there were 832,600 people below work age early in 2005 which results in 0.3 dependent persons per employee. This ratio will be taken as a constant for the purpose of further analyses. Although the demographic forecasts suggest the number of dependent persons per employee could decrease the character of this change can not be predicted unambiguously.

The estimates of the tax revenues use the prognosis depicted in Table 7 of the Appendix on the breakdown of the number of employees by levels of gross earnings, which has been worked out for the purposes of the present research. The reference breakdown used to draw up the estimates is the data of the CSB of October 2004 depicting the breakdown of the number of employees by gross average monthly earnings (CSB data base in the internet, table “BREAKDOWN OF THE NUMBER OF EMPLOYES BY AVERAGE MONTHLY GROSS EARNINGS IN PUBLIC AND PRIVATE SECTORS”).

Prognosis of the breakdown has been acquired by iterative means, ensuring calculation of the gross average earnings for the intervals forecast. The calculations use the middle points of the intervals with the exceptions of the lowest interval (below 80 lats), where the value of 70 lats is being used, and highest interval (above 1,000 lats) where the value of 1,100 lats is used. Using of mathematical methods for the breakdown forecasting is not possible for two reasons.

The first reason is that the breakdowns of wages during the previous periods do not match those used today. The analyses is based on the breakdown by levels of gross earnings used by the CSB in 2004 whereas data for earlier years were published using different breakdown by levels, thereby denying a possibility to compare them directly. For that reason a part of the
levels should be merged because in earlier years the maximal level of wage was “above 700 lats” while in 2004 it was “above 1,000 lats”. The lowest levels used previously (in 1997 the lowest wage interval was “below 38 lats” while in 2004 it was “below 80 lats”) also have vanished from the breakdown.

The second reason is that the breakdown of employees by levels of gross earnings fails to match distributions of standard probabilities (normal distribution, logarithmic normal distribution and others) envisaging selections of the highest probabilities or general clusters for the average value with the probabilities decreasing evenly while drawing further away from the average value. The breakdown of employees by gross earnings is not homogenous with the second zone of high probability breakdown forming, standing close to the value of the minimum wage. For that reason, the prognosis of breakdown is being made manually with the portion of employees within the levels of gross earnings being adjusted in correspondence with the changes in the minimum wage (the portion of employees with the earnings below minimum wage equalling zero) and the general compliance of the breakdown to the average gross earnings in the country so as to ensure that the weighted average (as calculated according to breakdown of employees by intervals of earnings by their middle points) equals that provided under the assumption. In addition to breakdown of all employees by levels of earnings, a prognosis for breakdown of employees of the state budget institutions by levels of gross earnings is made for each of the scenarios under consideration in order to assess the impact on budget spending for wages of the minimum wage policy.

A note should be made that the breakdown prognosis is characterized by a medium precision for the period after 2010 when the portion of employees with gross earnings above 1,000 lats could increase considerably resulting in the middle point for the wage interval of above 1,000 lats (at 1,100 lats) ceasing to be sufficiently representative. However, considering the limited information, the prognosis shows the most essential, namely, the dynamics in breakdown of employees by levels of gross earnings alongside changes in the minimum wage.

The impact of the scenario on tax revenues and net earnings of employees has been estimated based on prognosis of the number of employees and the breakdown of their earnings. Those estimates will serve as a reference point for the assessment of scenarios analyzed below.

The state budget revenues are estimated considering the share of the mandatory social insurance contributions paid both by employer (24.09%) and employee (9%) as well as the personal income tax (25% according to the base scenario). While calculating the income subject to the personal income tax and the subsequent tax payment the effective procedure established under the law was being followed. It stipulates that, as the first step, the amount paid as the employee’s mandatory social insurance contribution is being deducted from the gross earnings of the employee, after which the untaxed minimum is being deducted and the tax benefit for each dependent person. The remaining amount thus acquired is subject to the personal income tax. The resultant net wage of an employee is obtained by deducting the amount of personal income tax thus calculated from the gross earnings of an employee from which the employee’s social insurance contribution has already been deducted.

The costs an employee involves for the employer are obtained by summing up the gross wage and the mandatory social insurance contribution paid by the employer. It is assumed that 10% of the employees are employed part time. Based on data of the CSB as many as 10.4% of employees were employed part time in 2004 (CSB data base in the internet, table “RESIDENTS AGES 15-74 WITH FULL AND PART-TIME PRIMARY EMPLOYMENT,”
RS Group Wages and Impacting Factors 2005 – 2006

BROKEN DOWN BY QUARTERS”). This portion has been rounded up to full numbers for the sake of making the analyses simpler. It is being assumed as a constant value for the period until 2020. While it is known that employees are more inclined to work part time amid welfare standards improving it is not possible to assess precisely the expected growth in the part time employment. The expert assessment dealing with the increase in use of flexible forms of working hours shows that the indicator could grow up to 20%, however, the dynamics of the possible growth remains unclear and the same applies to timing when forms of arranging working hours could start growing more diverse at a faster pace.

Assessment of the base scenario analyzed by the WIF provides comparison of the results obtained to the actual situation in the country. For that purpose the estimates made under the base scenario are compared to the personal income tax revenue collected in 2004. The comparison uses information of the CSB about the collection of the personal income tax into the state budget in 2004 (CSB data base in the internet, table “CONSOLIDATED GENERAL BUDGET OF THE STATE” and “TAX REVENUES INTO THE CONSOLIDATED GENERAL BUDGET OF THE STATE AS BROKEN DOWN BY TYPES OF TAXES” (in percentage)).

While comparing the results, the WIF team concluded that the personal income tax revenues to the state budget under its estimate are 9.9% higher than according to the official statistical data. It may have been a result of influence of factors that are difficult for the research working group to predict for the future. Those factors include repayment of personal income tax to employees who have filled in their tax returns and submitted to the State Revenue Service a statement of eligible expenses. The activities of residents and their willingness to reduce the taxable income in a more distant future (after 2010) are hard to predict. Although the results of the estimates are more optimistic the method of calculation also has to be taken into account, keeping in mind that the results have been obtained from the average values and are based on several assumptions that are incapable of fully describing an economy of a country. The team holds that a deviation of 10% should be seen as admissible and hence the assessment obtained as a result of the estimates can be used to analyze the differences in tax revenues while considering various scenarios for determining the minimum wage.

The review does not analyze the impact on employment of the minimum wage increase, namely, it assumes that the number of employees corresponds to forecasts of the Ministry of Finance for the employment growth rate. The only exception is the scenario analyzing reduction of the personal income tax rate whereby, according to forecasts of the Ministries of Finance and Economy, the number of employees will increase..

Although the increase of the minimum wage may leave negative effects on the level of employment a research carried out by Estonia’s central bank (Hinnosaar, Rõõm 2003: 28) suggests that the impact could be rather small – an increase of the minimum wage by 10% is reducing by 0.43% to 0.66% the level of employment within the group that previously received the wage below the level of the new minimum wage. According to those results, in the case of Latvia, the increase of the minimum wage by 12.5% as of 2006 would entail a decrease by 630-965 employees of employment in the group with gross earnings between 80 and 90 lats. This estimate has been made based on research of Estonia’s central bank and changes of the minimum wage. The minimum wage increase of 12.5% answers to a drop in employment by 0.54% to 0.83% among directly affected group of employees. If the group of employees receiving wage of 80-90 lats in 2004 accounted for 11.3% or 117,000 people the subsequent drop in employment in that particular group should be 630 to 965 employees.
Account being taken of the expected gradual increase of the minimum wage the decrease in employment every year is not possible because employers will still be in need of employees, which leads to increasing probability that rather the work load of employees will be changed instead of dismissing them.

10.1.3. Influence of reduction of the personal income tax rate on the Base scenario

At the moment, reduction of the personal income tax to 15% planned by the government is conceptually supported by the Parliament. The results of the analysis drawn by the experts within the framework of this alternative analysis show that the scenario on reducing the personal income tax to 22% in 2007 is more likely to be fulfilled, but further changes will not be supported due to the swift decrease in tax funds. As the result, the personal income tax rate will remain 22%. The evaluation of the experts for the scenario, in which the tax is reduced to 22%, the minimum wage reaches 140 lats and the untaxed minimum is 70 lats in 2010, showed 65% realization probability. This is the second scenario examined by the WIF team when analyzing presumptive wage increase.

When analyzing the development of the situation with the personal income tax rate of 22%, some complementary assumptions for the basic scenario are used (see Table 7 of Appendix). Primarily, in 2007 the gross earnings rises by 1.5% more than the basic scenario prognosticates, but since it is not followed by the reduction of the tax rate, the average rise of the gross salary in 2008 and 2009 is esteemed only by 0.5% higher than in the basic scenario. In the following years, the rate of earnings growth corresponds to the basic scenario. Secondly, in 2007, the number of working population grows by 1% more than it is foreseen in the basic scenario, but since it is not followed by the reduction of the tax rate, the changes correspond to the basic scenario in the years to come.

According to the above mentioned assumptions, the minimum wage in the second scenario rises faster, for there is a small rise in the average gross earning due to the reduced tax rate. The minimum wage should be fixed higher than in the basic scenario so that it would attain 50% of the average gross earning of the previous year. In the case of the second scenario, the average gross earning is 2.3% higher than it is planned in the basic scenario for 2010 and 2.2% higher for 2020. This small rise of gross wage corresponds to the generally accepted conception about the incomes to become legal. The average gross earning of state employees in the case of the present scenario was 2.3% higher in 2010 and 2.3% higher in 2020 in comparison with the basic scenario.

The discounted cash flow value of the day is used in order to compare the cash flow created by the present alternative – total of net salaries in the national economy, the amount of personal income tax funds and the amount of collected social insurance contribution. It is calculated as 10% nominal financial discount rate for years 2007 to 2020. This kind of financial discount rate is used in the calculations of influence on finance for the projects co-financed by the EU Cohesion Fund. Though it is advised to use the 8% discount rate in financial calculations for smaller projects that are co-financed by the European Regional Development Fund, the WIF work group still used the 10% discount rate in these calculations. As the prognosis for the future have a small credibility level, the usage of a higher discount rate reduces its influence on the cash flow value of the day.
In the case of the present scenario, the total of received net salary is 5.8% higher than predicted in the basic scenario, which shows that the reduction of the personal income tax rate by 3% (from 25% to 22%) is advantageous for the working population. The gross earning value of the day for state employees is 5% higher in comparison with the basic scenario. Whereas the discount value of the day of employers’ expenditures on employees (gross earning together with social insurance contributions) is only 3.1% lower than in the case of the basic scenario. This shows that a positive effect will be produced – the wages of working population will grow more than employers’ expenses on employees, although the budget expenses to cover wages will also grow. Here and further in the analysis, the state and municipal enterprises will not be distinguished, for the wages of employees in these enterprises do not depend on the state or municipality budget. Instead, attention is paid to the dynamics of wages for state employees.

When comparing the amount of tax funds, one can conclude that the personal income tax discounted value of the day is 9% lower than in the case of the basic scenario. This means that although the amount of personal income tax funds will increase within the prognostication period, this amount will be smaller than in the case of the basic scenario. In comparison with the basic scenario, the social security contribution discount value will increase by 3.1% in the case of the second scenario, thus providing the social budget with additional resources.

Although no significant change of the minimum wage can be seen in the present scenario in comparison with the basic scenario, it is possible to give a review of the impact of personal income tax rate reduction on budget incomes related to the labour market. Change of the personal income tax rate reduces tax funds.

The overall influence on the national budget is determined when the gross earning of state employees is taken from the incomes of personal income tax funds and state social insurance contributions. The difference shows the change of net incomes of the national budget because the proportion between the change of incomes (tax revenues) and change of expenses (wages for state employees) is considered. A negative quantity shows that the increase of incomes do not exceed the increase of expenses. When comparing the second scenario with the basic scenario, the conclusion is that in the case of the second scenario the cash from discount value is 5.1% lower than in the case of the basic scenario. This means that in the case of the second scenario, the national budget will have less income than in the case of the basic scenario if the income growth from increased tax contribution will be less than increase in net wage for state employees.

In order to compensate decrease in personal income tax revenues in the state budget, it is possible to change the amount of untaxed minimum by adapting a slower rate of increase than it is planned at the moment. A higher untaxed minimum diminishes tax basis, which is taken into account when calculating personal income tax. Thus the situation with decease in personal income tax funds may be compensated by a “freeze” of untaxed minimum. Average wages growing and untaxed minimum remaining at the same level, the tax basis increases, thus compensating the impact of personal income tax rate reduction. But this policy creates conditions for slower growth of net income of employed people, especially for low-paid employees. This is why actions like these are not advisable, except for the case if the reduction of tax rate causes too great decease in personal income tax funds. But even then the non-increase of untaxed minimum can only be a temporary solution.
10.1.4. Optimistic scenario of the minimum wage increase

The third examined scenario of an alternative implementation is optimistic and it predicts that minimum wage will reach 50% of the average national gross earning as to 2010, and 68% as to 2020. The personal income tax rate remains 25%. This scenario corresponds the most to the political alternative elaborated by the Ministry of Welfare – to increase the minimum wage to make it 68% of the national gross earnings in 5 – 6 years after implementation of the Concept Paper on Minimum Wage in 2010. Although a supplementary assumption is made while analyzing this scenario, it still can not be considered as realizable in practice because it requires a considerably faster increase in minimum wage within the period of 2007 and 2020 than in the case of the basic scenario. Nevertheless, the third scenario may serve as one of the means when choosing an optimal tempo of increase in minimum wage.

For the analysis of this scenario, the following supplementary assumption is made – an average gross earning in the national economy increases by about one percent point more within the time period from 2007 to 2020 than in the case of the basic scenario because a swift increase in minimum wage raises the average level of the gross earning in the national economy. It is supposed that the level of employment corresponds to the basic scenario.

Taking the basic assumptions of alternative evaluation into account, one can see that the third scenario provides the fastest growth of minimum wage. In this case, the minimum wage is 42.9% higher as comparing to the basic scenario in 2010 and 51.3% higher as to 2020. Besides, the average gross earning is 3.7% higher than in the basic scenario as to 2010 and 13.8% higher as to 2020, if compared to the basic scenario. Wages of state employees represent respectively 3.6% and 13.8%. The fact that the amount of gross earning growth for state employees is close to the common increase in gross earning in the national economy indicates that in the case of the optimal scenario, the pressure of minimum wage growth on state employees’ wage is as strong as on the whole national economy.

In order to compare the following cash flows of the present alternative – the total net salary of employed persons in the national economy, the amount of personal income tax revenues and social insurance contribution revenues – the present cash flow discount value is used. In the case of the third scenario, the common net salary for employed people is 10.9% higher than in the case of the basic scenario, which indicates that a swift increase of minimum wage will favour the growth of net incomes. When comparing the discount value of employers’ expenses on employees with that corresponding to the basic scenario, one can conclude that it has grown by 7.6%.

If the efficiency of employed people will grow with the same speed, then this kind of minimum wage policy may cause a significant decrease in total income of employed people working in less developed fields of national economy and in regions of the state, because the labour force expenses may grow faster than the efficiency of the labour force.

When comparing the amount of tax revenues, one can conclude that the personal income tax present discount value is by 7% lower than that in the case of the basic scenario. This is an explanation with an assumption that the untaxed minimum and personal income tax relief for each dependent person is calculated proportionally to the minimum wage, thus reducing the taxable income. It permits to draw conclusions that too rapid increase of minimum wage and untaxed minimum has similar effect on the national budget as the reduction of personal
income tax rate reduction has. In comparison with the basic scenario, in the case of the third scenario the revenue of social insurance contributions present discount value will raise by 7.6%, thus providing additional resources to the social budget.

When comparing the common influence of the scenario on the national budget (personal income tax revenues and social insurance contributions minus state employees’ net wage) with the basic scenario, one can conclude that the discount value of the acquired flow is 1.9% less. This means that in the case of the present scenario, the national budget will have less income than in the case of the basic scenario, for the increase of income form the increased tax payments will be lower than the growth of state employees’ wage. However, this indicator is smaller than that in the case of the second scenario (reduced personal income tax rate).

In the case of implementation of the optimistic scenario, the “protection” of interests of low-paid workers using a high minimal wage is provided; however, it is done at the expense of the national budget (mainly – reduction in personal income tax revenues) and at the expense of high-paid workers “costs” (education, qualification, personal capacities, etc.) and motivation. It is not possible to credibly prognosticate the reaction of employers to these radical changes – a grater interference of the state in the maintenance of the labour market may cause a stronger resistance from the part of employers.

10.1.5. Pessimistic scenario of the minimum wage increase

The fourth examined scenario is “pessimistic” regarding the possibility of fixing the amount minimal wage of 68% of the national average salary, because it foresees a slower development of the minimal wage than it is foreseen by the Concept Paper on Minimum Wage – the proportion of the minimum wage against the average gross wage in the state is preserved at the present level (33% to 37%).

Several experts admitted that the maintenance of the minimum wage at the present proportion against the average gross wage in the national economy can be evaluated as a realistic scenario. In this case, an even rate of the minimum wage growth is ensured, which, on its part, provides with an even growth of all values that are related to the minimum wage (fees, wages, other values) that is proportional to the average wage in the national economy.

As the minimum wage is increased gradually, it is assumed that the average gross wage within the time period from 2007 till 2010 will grow by one percent point slower than it is prescribed in the basic scenario, bet after 2010, the growth will correspond to that of the basic scenario. This assumption is introduced because the minimum wage limits less the labour market, and thus the decrease of undeclared employment takes place slower.

In fourth scenario, the minimum wage has the level as foreseen in the case of the basic scenario as to 2010 and it is 33.3% lower as to 2020. Average gross wage is 3.5% lower than that in the basic scenario as to 2010 and 8.4% lower as to 2020, but for state employees – 3.6% and 8.4% respectively.

In order to compare the cash flows of the present alternative – the total of net wage of employed people in the national economy, the amount of personal income tax revenues and
amount of social insurance contribution revenues – the cash flow present discount value is used. In the case of the fourth scenario, the total of net wage of employees is by 4.5% lower than in the case of the basic scenario, which shows that a slow and proportional increase of the minimum wage will favour less the growth of net income. It is difficult to prognosticate what will be the impact of this minimum wage scenario on undeclared income of employed people. When comparing the discount value of the day of employer’s expenses on labour force with the basic scenario, one can conclude that it has reduced by 4.0%.

When comparing the amount of tax funds, one can make a conclusion that the personal income tax revenues present discount value is 1.9% less than in the case of the basic scenario. When comparing with the basic scenario, in the case of the present scenario, the social insurance contribution revenue present discount value will diminish by 4.0%.

When comparing impact of the fourth scenario on the national budget, the conclusion is that the present discount value flow is by 2.0% lower than in the case of the basic scenario. This means that in the case of the fourth scenario, the national budget will receive fewer revenues than in the case of the basic scenario, because the growth on income from increased tax payment will be lower than the increase of state employees’ net wage. This decease is considerably lower than that in the case of the second scenario (-5.1%) and it is relatively close to the result given in the optimistic scenario (-1.9%).

The pessimistic scenario corresponds more to the preservation of the present situation – the minimum wage is raised at the extent that would help to maintain the present proportion to the average gross earnings in the state. This is the safest scenario from the point of view of employer, for the slow growth of minimum wage allow them to adjust to the situation.

10.1.6. Social and economic consequences of the increase of minimum wage

It was indicated previously that the idea about the 68% specific weight of minimum wage out of the national average earnings originates from the studies of early 1970-s about the amount of poverty line of a wage; however, there is no detailed information about the circumstances, in which this conclusion was drawn. The WIF research team would like to mention that, at the moment of recommendation elaboration, the targets that dominated in the EU differed from those nowadays, as well as the social and economic situation was slightly different. There is a remarkable time interval between today and the moment of recommendation elaboration, and the targets recently set by the EU that are described in the Lisbon Strategy make us think that today another wage regulative mechanisms that would be more flexible could be found. In addition, none of the EU member states where the statutory minimum wage exists has practically implemented the investigated idea.

When speaking about the consequences of increase of the proportion between minimum wage and national average wage, two opposite groups of arguments are mentioned. On the one hand, increase of the above mentioned social welfare should be considered as a positive result. It is clear that wages will grow for low-paid workers, bet they will diminish for highly remunerated ones. This is equalization of income difference that is particular for social democratic vision of the world and the correspondent strong social protection. On the other hand, equalization of wage among different groups of employed people is not regarded as a
quite positive result. WIF research results show that higher labour income has unbiased evidence – higher efficiency that is manifested through higher education, better skills, which are not possessed by a lower-qualification labour force. When approximating the proportion of the minimum wage to the national gross earnings, the opportunity to offer a considerably different wage decreases.

Mathematically, there should be a great amount of observation containing one and the same value in order to approximate the minimum wage to the state average earning. Thus the majority of employed people receive a salary that is approximated to the minimum wage in order to realize the analyzed idea. The calculations in the optimistic scenario show that in order to attain the minimum wage of 68% from the national average earning, about 50% of all employed people should receive a salary approximated to the minimum wage and the rest – not more than a salary that is 50% bigger than the minimum wage. Consequently, in reality income of the majority of employed people (both high and low-qualified) would represent the amount of one to two minimum wages.

In this situation, the motivation for high-qualified employed people that results in efficiency of working would diminish. The fall in motivation may be substantiated by one argument. If a person who invests time and money in improvement of professional skills do not receive compensation for the efforts in the form of a salary, he or she lost interest in investing into the human capital.

If the entrepreneur will be interested in motivating employees, he will have to look for solutions how to remunerate their contributions. At the same time, the entrepreneur could try to avoid such choice of remuneration that would create an inversed effect referring to order of state average wage calculation – repetition of minimum wage increase (in the case if the government ensures that the minimum wage preserve at the rate of 68% from national average wage). Another solution that an entrepreneur could take is reduction of low-qualified labour force, replacing it by usage of technologies in the enterprise.

One of the mechanisms that could diminish the pressure to approximate the difference in wages is rise of demand for part-time employment. Another solution is to adapt such contract form that is not subjected to the traditional relationships between an employer and an employee, e.g. high-qualified employees feel the necessity of becoming a self-employed person that would let them earn more (it is not included into the calculation of state average earning). Yet, another solution is offering of non-monetary (health insurance, service car, feeding, travelling, etc.) or other kinds of remuneration (business shares, contributions into private pension fund, etc.) to the most “valuable” employees of an enterprise. Non-monetary remuneration is not included into the calculation of national average earning, which would favour entrepreneurs to motivate high-qualified employees of an enterprise.

In the situation when the minimum wage specific weight is relatively high in comparison with the national average earnings, this will create difficulties for the existence of the majority of small enterprises, because, at present, they employ low-qualified labour force and they produce goods (offers services) that have small added value. The “reserves” of these enterprises are small and a high minimum wage may lead these enterprises to bankrupt. In larger enterprises new technologies may be introduced. This will diminish necessity for comparatively low-qualified labour force (work of a man will be substituted by technologies).
One of the arguments that say why the minimum wage should be high enough in the state is the observation that the executives of foreign companies, especially if the companies operate in less developed areas, provides the potential labour force only with the statutory minimum wage.

Within the framework of the inquiry, the experts had to name consequences that would arise in the case if the minimum wage of 68% from national average earning would be introduced, foresee the possibility of consequence occurrence and their calculations and mention the number of persons affected by these consequences. The expert evaluation was dependant on the statistic data provided by the WIF team, on experts’ knowledge and vision of the world. In the majority of cases, the experts had difficulties with evaluating the possibility of possible consequences, for this phenomenon was interrelated with other circumstances that could not be prognosticated. Similar difficulties arose when evaluating the number of employed people to experience the directly consequences, because it requires very detailed data on the number of employed people in different sub-groups. Because of the mentioned difficulties, the average values of possibility and number of employed people were classified. There were five groups of probability evaluation: high (81% - 100%), relatively high (61% - 80%), medium (41% - 60%), relatively low (21% - 40%) and low probability (up to 20%). A similar model was used to classify the specific weight of the number of affected employed persons: high (81% - 100%), relatively high (61% - 80%), medium (41% - 60%), relatively low (21% - 40%) and low specific weight (up to 20%).

Consequences or results illustrated in the Table 11 are ranked, firstly, due to the possibility of their occurrence and, secondly, due to the specific weight of affected employees in a numeric value.

It is to be noted that several possible consequences are contradictory, for they conform to different groups. E.g. the experts admit that, on the one hand, employment in low-qualified groups will rise. But, on the other, the tempo of new working place creation will diminish, there will be a delay in employment rate increase and unemployment of low-qualified labour force will rise. This means that in general a high minimum wage would create dislike for poorly-remunerated working places (social and rational considerations), however, the number of there work places could be limited (economical considerations). A high minimum wage will make en employer consider whether it is worth creating additions workplaces, taking into account the expected expenses on labour force. This, on its turn will hinder increase in workplaces.

The experts did not agree whether the specific weight of minimum wage as to the national average earning will diminish or on contrary, favour undeclared employment. It is associated to different factors, e.g. capacity of state institution control and competition situation in the fields of national economy. However, it is assumed that the probability of undeclared employment reduction is higher than the probability of its increase.

Although the experts think that implementation of other political alternatives could favour the return of the Latvian labour force now working abroad, however a high minimum wage specific weight could also be one of the means of solving the problem of labour force need. Thus it has double effect. On the one hand, a high minimum wage would attract labour force from other countries. On the other, departure of Latvian labour force would decrease and probably if would favour the return of the Latvian favour force working abroad.
Table 11. Rise of the minimum wage to the rate of 68% of the national average wage. 
Prognosticated consequences of the policy

<table>
<thead>
<tr>
<th>Consequences/results</th>
<th>Evaluation of impact</th>
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<td></td>
<td>Probability</td>
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<td>Increase in expenses on labour force</td>
<td>High</td>
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<tr>
<td>Increase of service expenses</td>
<td>Relatively high</td>
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<tr>
<td>Decrease of rate for new working-place creation</td>
<td>Relatively high</td>
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<tr>
<td>Amelioration of social security for inhabitants</td>
<td>Relatively high</td>
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<td>Increase of flexible working forms (including part-time work)</td>
<td>Relatively high</td>
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<td>Increase on employment within the groups of poor-remuneration</td>
<td>Relatively high</td>
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<td>Increase of financial involvement of an employee to an enterprise (shares includes)</td>
<td>Relatively high</td>
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<tr>
<td>Delay in employment rate development</td>
<td>Relatively high</td>
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<tr>
<td>Unregistered employment (pay envelope included) diminishes</td>
<td>Medium</td>
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<td>Low-paid will receive more, high-paid – less in the result of that</td>
<td>Medium</td>
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<tr>
<td>Bankrupt of micro and small enterprises</td>
<td>Medium</td>
</tr>
<tr>
<td>Difficulties of foreign investment attraction</td>
<td>Medium</td>
</tr>
<tr>
<td>Increase of unemployment among low-qualified people</td>
<td>Medium</td>
</tr>
<tr>
<td>Lack of competitively among labour force</td>
<td>Medium</td>
</tr>
<tr>
<td>Confluence of labour force from abroad</td>
<td>Medium</td>
</tr>
<tr>
<td>Latvian labour force leaving for abroad reduces</td>
<td>Medium</td>
</tr>
<tr>
<td>Formation of private closed pension funds (founded by en enterprise)</td>
<td>Medium</td>
</tr>
<tr>
<td>Decrease in learning technologies</td>
<td>Relatively low</td>
</tr>
<tr>
<td>Increase of unregistered employment</td>
<td>Relatively low</td>
</tr>
<tr>
<td>Diminishing of working efficiency</td>
<td>Relatively low</td>
</tr>
<tr>
<td>Growth of small entrepreneurship (self-employed)</td>
<td>Relatively low</td>
</tr>
</tbody>
</table>

Note: The results of the expert inquiry were grouped. There were five probability groups made: high (81% - 100%), relatively high (61% - 80%), medium (41% - 60%), relatively low (21% - 40%) and low probability (up to 20%). A similar classification was made for the amount of affected workers: high (81% - 100%), relatively high (61% - 80%), medium (41% - 60%), relatively low (21% - 40%) and low specific weight (up to 20%).

Taking into consideration the framework of three basic models of socially economical policy by G. Esping – Anderson, a high level on employed people protection is characteristic for the countries where in the social policy the approach of social democracy principals prevails. However, a state can afford to implement a policy like that only when a considerably high welfare rate is attained and the incomes and expenses of a state are balanced. A high level of social guaranties requires big expenses. It is indispensable that the national economy is stable and efficient enough in order to cover the expenses of wages and tax contributions. A high minimum wage in these states is one of the means to minimize the welfare difference among employed people (Esping-Anderson: 1990). The third of the scenarios developed is ideologically the most appropriate to the social and economical attitude, but it preserves the implementation impact on working motivation.
In the states there liberal policy dominates, minimum wages are not as high. Liberal and social policy provides for stimulation of the national economy with the less possible interference of the management. Protective measures for employed people are meant to reduce poverty, but not to ensure welfare, thus making the employed people to thing about the latter by themselves. Liberal policy is more appropriate for the Third World and states with rapidly growing national economies, because it allows a maximal usage of economic development (Esping-Anderson: 1990).

At the moment, Latvia performs liberal and social policy. Latvia has a rapidly developing national economy, which is to attain at least the average of the EU level concerning income and welfare. This is why a moderate policy is advisable in fixing the minimum wage – the minimum wage is to be increased along the development of the national economy, however the average growth of if in comparison with the gross earning should not be too rapid.

### 10.2. Differentiation of the minimum wage in construction, retail trade and forest exploitation

The second policy alternative chosen by Ministry of Welfare anticipates the differentiation of the minimum wage in three fields, which are placed under risk of non-declared employment (construction, retail trade, and forest exploitation/wood work industry), taking into account the amount of income gained in terms of non-declared employment. The aim of alternative is to decrease non-registered employment (“envelope salaries”) in mentioned fields. In this chapter, the team examines possible levels of differential minimum wage for given fields, basing on the productivity of employees in these fields and on the data of WIF employees’ survey about wages in corresponding fields. The team also analyses the adequacy of laws and regulations, which are in force and the capacity of state institutions to work in conditions of differential minimum wage.

#### 10.2.1. Case study

There are many types of differentiation for the statutory minimum wage in the EU member states (Funk, Lesch 2005), but only in Malta in addition to the national minimum wage, the government determines different minimum wage according to national economy sectors. But here the differential minimum wage is not that significant, because the salary level in the sectors to which differential minimum wage refers, go beyond differential minimum wage levels (Funk, Lesch 2005). In Lithuania decreased minimum wage refers to different groups of the public sector, but it’s not connected, because the wage level in these groups goes beyond the defined minimum.

There is the statutory minimum wage in the majority of the EU member states, especially in the youngest ones, but still approximately in one fourth of all countries the minimum wage is defined by collective agreement. The statutory minimum wage varies in areas of national economy in the countries where the statutory minimum wage is and where it is defined according to an agreement between labour unions and employers’ organizations. However, as
mentioned before, it is not correct to compare countries, in which there is a different procedure of minimum wage differentiation.

In countries where the statutory minimum wage exists, the differentiation of the minimum wage is more popular for new employees and employees with little experience in the position they take. In nine countries from nineteen that had been examined, the minimum wage was paid to the new employees. Another possible solution suggested by the World Bank, would be differentiation of the minimum wage in less developed state regions.

Focusing on the situation in Latvia, the question of practical mechanisms necessary for introduction of differential minimum wage are becoming more actual, because these mechanisms demand a well arranged normative basis and definition of the main supervising institutions.

The main problem connected with the introduction of differential minimum wage in Latvia, is the identification of enterprise activity field. The existing normative basis does not anticipate obligatory and legitimate declaration and registration of the field of enterprise activity; it does not anticipate consequences, which emerge from belonging to a registered activity area.

The necessity of registration of the field of the main enterprise activity is not defined in Latvia – enterprises can register their activity fields in the Enterprise Register, but it is not an obligatory demand. Although it is possible to define the field of the enterprise main activity, because the enterprise can point net turnover allocation according to types of its main activity in its annual summary appendix for profit and loss account, but it is prescribed in the second part of the Paragraph 48 of the law On annual report of an enterprise that “other enterprises may not fulfil these demands, if it seriously and negatively affects interests of the mentioned enterprise”. So, the valid editing of the law allows the enterprise to choose itself, whether to make the information about net turnover allocation according the types of basic activity open for the public.

The described situation proves that evaluating possibilities of introduction the differential minimum wage in Latvia, it is very essential to know how to identify enterprises that will be connected to the passed regulation.

10.2.2. Possible levels of minimum wage differentiation

It is possible to differentiate the minimum wage following different field characterizing rates. The idea about the necessity of the differentiated minimum wage means that even according the statistics the amount of employed gross earning and the amount of wage declared by enterprises are not precise – wages are paid illegally (in “envelopes”), and also in the bookkeeping there is only a part of salary. So, the level of differentiation can be defined according to differences of one employee’s productivity among fields or according to alternative surveys about real salary of employees (wages received after tax payment including “envelope” wages).

Added value for one employee can be used as an indicator for actual productivity of employed of a certain field, pointing at registered payment disparity in official statistics.
RS Group

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(taking on that information about field added value is true (employers include the “envelope” wages of their employees into their costs through other cost positions)).

The productivity of employed from each national economy fields was calculated basing on the CSB data. CSB information about the added value for average gross and net wages, as well as about the number of employed in the period from 2003 till the 1st quarter of 2006 according to fields of national economy (NACE 1.1. classifier), was arranged on order of the WIF team.

Table 12. Gross earnings and added value for one employee in construction, retail trade and forest exploitation for the year of 2005

<table>
<thead>
<tr>
<th>Field Description</th>
<th>Gross earning of employed, LVL</th>
<th>Gross earning of employed compared to the average in the state, %</th>
<th>Added value for one employed, LVL</th>
<th>Added value for one employed compared to the average in the state, %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Construction (F)</td>
<td>210,95</td>
<td>86%</td>
<td>8 398</td>
<td>98%</td>
</tr>
<tr>
<td>Retail trade, except cars and motorcycles; reparatory of subjects for individual needs and household equipment (G52)</td>
<td>150,31</td>
<td>61%</td>
<td>9 077</td>
<td>106%</td>
</tr>
<tr>
<td>Forestry, preparation of timber products and with that connected services (A02)</td>
<td>260,38</td>
<td>106%</td>
<td>12 786</td>
<td>149%</td>
</tr>
<tr>
<td><strong>Average in the state</strong></td>
<td><strong>245,75</strong></td>
<td><strong>100%</strong></td>
<td><strong>8 596</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

*Note: CSB information about the added value for average gross and net wages, as well as about the number of employed in the period from 2003 till the 1st quarter of 2006 according to fields of national economy (NACE 1.1. classifier), was arranged on order of the WIF team.*

In 2005, the official statistics of the gross earnings in the construction field (F) is on the level of 96%, in the retail trade (G52) field – 61%, but in the forest exploitation (A02) field – on the level of 106% of the average state wage (see table 12). The field added value for one employed compared to average added value in 2005 was 149% in the forest exploitation (A02) field, 98% - in the construction (F) field and 106% - in the retail trade field. Results show that in all inspected fields gross earnings ratio to the average national gross earnings is lower than the ratio of the productivity of corresponding field for one employed to average national productivity, but comparing the correlation of field productivity and average productivity in the state, it can be seen that in construction (F) and in retail trade (G52) it is very close to the average state level.

Basing on the employed productivity differences, shown in the table 12, differentiated minimum wage can be defined according to the field productivity compared to state average productivity, taking into account that non-differentiated minimum wage corresponds with average state productivity (minimum wage in the state, as it has been defined till now). Reading the table we can declare that the minimum wage would have to be in the amount of 149% from the state minimum basic wage, in the construction – 98%, which means that the minimum wage in this field would be lower than the minimum wage defined by the state. It has to be noted that CSB data were used in the calculation and it can be seen that the gained
result does not correspond to the one expected. It is unlikely that added value for one employed in the construction field is less than the added value in the retail trade field.

It has to be noted that there are two possible approaches for differentiation of wages. The first is shown in the table 12 and it anticipates differentiation compared to average productivity. The second approach anticipates differentiation compared to minimum productivity, but in this case differentiation of minimum wage compared to minimum productivity cannot be used, because minimum productivity corresponds with education (M) field. As far as teachers’ wages are attached to the minimum wage at least in the amount of two minimum wages, it cannot be accepted that the productivity in the education field corresponds with the minimum wage.

If the average productivity would be taken as a point of reference, we consider that the minimum wage in the state corresponds to it, and then fields, the productivity of which significantly overrun the average; the minimum wage can be defined proportionally to the correlation between the productivity in the field and the average productivity in the state. As far as in the construction field (F) the differences of added value from the state average added value for one employed, are little (see table 12), it can be accepted that it corresponds with the general (non-differentiated) minimum wage. The productivity differences in the retail trade field (G52) are also little, which means that differentiation does not have big significance if it is defined by the field’s productivity while in the forestry field (A02) it would be necessary to define the minimum wage, which would be 50% higher.

The other possibility of defining the differentiated minimum wage for national economy fields includes an attempt to evaluate the real average wages (including “envelope” wages), which are gained from the inspection of employed. In this analysis there will be results (including net wage and additional payment) evaluated, which have been used in terms of the WIF research dealing with the quantitative survey of full time employees.

The differences between average wages in the field of national economy were evaluated based on the WIF research data (quantitative survey of full time employees). In the fields like agriculture, forestry and fishery (A and B) (they are linked in the research, therefore there will be average wages in these fields used together for the evaluation) these are on the level of 94% - 95% from the average wage or 28% higher than in the mining industry (C) (according to the research data, there is the lowest wage). In construction (F) average wages are on the level of 139% from the average wage or 88% higher than in the mining industry, but in the wholesale trade and retail trade together (G) the payment is on the level of 90% from the average wage or 22% higher than in the mining industry.

These results are also based on the proportion of inspected employees, whose monthly wage is 100 LVL. In the mining industry these are 46% - approximately half of the employees receive a monthly payment in amount of 100 LVL, therefore the minimum wage in this field is very binding. In the fields like agriculture, forestry and fishery this proportion is 30%, in construction – 30%, in wholesale and retail trade – 32%. Thus it can be concluded that the most binding minimum wage is in the mining industry field, for other fields it is moderately binding.

Since the level of minimum wage is the most binding for mining industry field, it refers to the statutory minimum wage. For other fields which require differentiation of the minimum wage,
the appropriate minimum wage level could be stated according to the rate of average wage of the field to average wage of most binding field.

Taking into account these assumptions, it is advisable for such fields like forestry to increase the amount of the minimum wage for 35% to 45% (proportionally to average field wage compared to average mining industry wage) above the general minimum wage (evaluation is increased because the average salary evaluation mentioned above is lower, because of included agriculture field), in construction – for 50% to 60% above general minimum wage (results is decreased to avoid resistance of employers), in retail trade – for 20% to 30% above general minimum wage.

Table 13. Possible levels of minimum wage differentiation and their average evaluation in the expert inquiry

<table>
<thead>
<tr>
<th>Field</th>
<th>Advised level of differentiation</th>
<th>Version of a minimum monthly wage, LVL</th>
<th>Differentiated minimum wage for the field, LVL</th>
<th>Summary of expert evaluation in 100 point scale</th>
</tr>
</thead>
<tbody>
<tr>
<td>Forest exploitation/ wood industry</td>
<td>35 – 45%</td>
<td>90</td>
<td>120-130</td>
<td>55 – 60 points</td>
</tr>
<tr>
<td></td>
<td></td>
<td>100</td>
<td>140-150</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>120</td>
<td>160-170</td>
<td></td>
</tr>
<tr>
<td>Construction</td>
<td>50 – 60%</td>
<td>90</td>
<td>135-140</td>
<td>50 – 60 points</td>
</tr>
<tr>
<td></td>
<td></td>
<td>100</td>
<td>150-160</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>120</td>
<td>180-190</td>
<td></td>
</tr>
<tr>
<td>Retail trade</td>
<td>20 – 30%</td>
<td>90</td>
<td>110-120</td>
<td>50 – 60 points</td>
</tr>
<tr>
<td></td>
<td></td>
<td>100</td>
<td>120-130</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>120</td>
<td>140-160</td>
<td></td>
</tr>
</tbody>
</table>

WIF team included evaluation of experts in the survey, in which the specialists had given their evaluation about the level of minimum wage differentiation in each field in the scale of 100 points, shown in the table 13. Highest evaluation could have meant that offered minimum wage was absolutely convenient for the situation in Latvia. Table 13 shows information about suggested differentiation level, calculated examples of increased wage in the levels of different statutory minimum wage, and also expert evaluations. Experts considered that offered levels of differentiation of the minimum wage in the investigated fields corresponded to Latvia in moderate level. Various experts decreased their evaluation because conceptually they had not supported the idea of introduction of differentiated minimum wage into national economy fields.

The advantage of the calculation method, suggested by WIF team, is its theoretical base – as far as the minimum wage is mostly connected with the less earning field, then its differentiation allows, basing on the information about total income of employees (including “envelope” wages) according to national economy fields, to make relatively objective differentiation of the minimum wage. One of the disadvantages is the ethical aspect – anonymous information of employees about the total amount of wages is used instead of the state official statistics. If minimum wage increases significantly, employers will be forced to decrease wages for their employees in order to cover new expenses, and employees will be not deliberately “punished” for their openness.
10.2.3. Administration of minimum wage differentiation

Minimum wage differentiation does not contain only calculation of the level of potential differences. It is more important to understand administrative possibilities of introduction of the differentiation of minimum wage. These possibilities result from the state legislation and the work practice of state institutions. This chapter is devoted for a detailed analysis of questions mentioned above.

The main problem, which is connected with introduction of minimum wage differentiation, is Latvian legislation that does not anticipate obligatory identification of enterprise activity of a certain field. At present, the registration of the main enterprise activity of a certain field is not obligatory and it is rarely being implied into practice. However, some regulations of the Cabinet of Ministers anticipate its introduction, but if at least one of the economic activities of an enterprise corresponds to a certain field (and to its code according to the NACE classifier), the working group doubts that similar mechanism would be a better solution in case of the differentiated minimum wage.

When evaluating potential, initially the best solution for the situation in Latvia (assuming that it would be necessary to avoid essential changes in the Latvian legislation while introducing alternatives) was thought to be a definition of enterprise economic activity of a certain field according to documents, which are necessary for a certain type of economic activity. For instance, it is known that retail trade enterprises need permissions about products from alcohol and tobacco etc. So, the WIF team tried to check, if it is possible to identify the enterprise activity field, basing on its issued permissions, licences and other similar documents. Despite the fact that this approach received responsiveness among experts, who evaluated that as less repressive and more appropriate for entrepreneurship, the WIF team came to the conclusion that this possibility could not be completely fulfilled.

Among three inspected fields the only one, which can be controlled, is the construction, because The Ministry of Economics registers all construction merchants and construction companies, as well as construction practice and architect certificates. Although there are necessary licences for certain product trade (e.g. alcoholic drinks, medicine), they do not cover the whole field. There are many organizations in the trade field (such as Latvian Chamber of Commerce and Industry, Latvia Traders Association, Latvia Traders Chamber and other), which units certain retailer groups, and these are not all-in-depth organizations, which would include the majority of retail trade enterprises. The situation in the forestry field is similar - in order to work in forestry and wood industry it is not necessary to register in the Ministry of Agriculture, and in order to perform forest exploitation work, the contractor does not obligatory need any work permission documents.

If an enterprise is operating in various fields of national economy, it is not fair to imply the differentiated minimum wage for all enterprise workers. At the moment in the annual report it is necessary to show an average number of employees in an enterprise without a detailed accounting of the number of employees according to the main activity types. It is necessary to introduce some amendments of law here, which would define the part of enterprise employees working in kind of economic activity, and it would be necessary to implement the differentiated minimum wage only for them. Even if there is an amendment of the law On annual reports of an enterprise, the control of the number of employed (to whom the differentiated minimum wage is implemented) after annual reports of an enterprise could
foster avoiding these regulations, showing smaller number of employed in certain fields or concluding a contract with employees for a part-time job.

Summarising the above it can be concluded that one of the essential obstacles for introduction of the alternative is the lack of a corresponding regulation base. As far as the State Revenue Service is an institution that is responsible for tax revenues and registration of taxpayers, it might seem quite convenient at first to be able to entrust the function of enterprise control to the SRS. But it is necessary to mention that at present the legislation does not anticipate that the State Revenue Service should interfere into enterprise economic activities or handle the arrangement of entrepreneurship.

If the SRS were an institution that would receive a duty from the government to define the basic area of an enterprise activity, it would be able to use the net turnover shown in the annual report on profit and loss account, which is reflected in the appendix in division into basic activity types, which is anticipated in the paragraph 48 of the law On annual reports of an enterprise. But like it has been mentioned before, the law allows the enterprise to choose if it is willing to publish the information about the net turnover in the division into main activity types. If an enterprise chooses not to publish the information about the net turnover in the division into main activity types, the SRS does not have necessary information, on the basis of what it is possible to define to which national economy field the enterprise belongs.

In addition, it is necessary to point out that the lookup from annual reports is not operational. Enterprises have to hand in the report about the previous calendar year till May of the following year. It is possible to implement the differentiated minimum wage, which is based on the economic activity of the previous year, starting from the second part of the coming year or from the year after the coming one. This means that the system would not be flexible towards changes in economic activities of an enterprise.

Analysing the present legislation, the WIF team considers that implementation of this alternative would be followed by large expenses for the introduction of the system and its maintenance. Firstly, it would involve amendments of regulations and laws to make it possible to define the enterprise affiliation to a concrete economic activity field. Secondly, maintenance of the system of differentiated minimum wage needs enterprise control, which consists of two parts. The first part is control of received information that is done with the certain computer programme, the implementation of which would cost a new system higher expenses, which depend on provision of state institutions (mostly the State Revenue Service and the State Labour Inspectorate) with used programmes. The second part is physical control of enterprises in case there is a risk of violation of minimum wage regulations, identified in the information control. It is noted that the control capacity of both institutions is quite low at present. In order to ensure better control, there would be a need to involve more human resources. Thirdly, the introduction of differentiated minimum wage causes expenses for information about legislation changes. Fourthly, if the amendments of laws and regulations mentioned above come in force, enterprise accountants would have to present more complicated annual reports to the State Revenue Service. So, the administrative barriers will be increased. The adjustment to the new system of annual report preparation would involve accountant training and cause other expenses for all Latvian entrepreneurs.

Possible state administrative expenses of introduction and maintenance have not been identified till now. While defining those, the working group has faced certain difficulties, because, on the one hand, it was pointed that the state administrative expenses would
increase, but on the other hand, at least half of the expenses could be covered, implementing the alternative in a longer period of time. Implementation of amendments of laws and regulations, and provision with programmes is possible to do in terms of the working agenda of state institutions in one year and a half. Expenses have to be anticipated for control of the introduced system and assurance of activity, however, its amount will depend on amendments of laws and regulations and on the capacity of social partners (organizations of employers and labour unions) and state institutions.

10.2.4. Consequences of differentiation of the minimum wage

The list of risks and their probability identified in the expert inquiry gives an evidence that implementation of the alternative would not bring the expected result, which was not deliberately defined in the formulation of the alternative by the Ministry of Welfare. According to the work task, the introduction of differentiated minimum wage is anticipated in fields that are mostly brought under risk for non-declared employment. The expected result has to imply the decrease of non-declared employment, but experts think that the possibility of this result in comparison to other possible consequences is low.

There are five groups of results coming from the introduction of policy alternative identified by experts, except administrative difficulties, which have been analysed before.

First, experts point that the increase of minimum wage in such fields like retail trade, construction, forestry and wood industry, is not correct. Exactly these fields make a remarkable part of the national economy and they are included into the category of small and middle enterprises, which play an essential role in formation of GDP and employment. The WIF team has ordered the CSB statistical data about total number of employees in sub-sectors in division according to largeness of an enterprise, according to which there are 50% in construction and 63% legally employed employees in retail trade, who are working in companies up to 49 workers.

There is special attention paid to facilitation of development of small and middle entrepreneurship in the sphere of entrepreneurship policy and its implementation. Introduction of differentiated minimum wage in these national economy fields would create negative circumstances for the functioning of economics in different regions and in fields mentioned above, which would enforce socially economic disproportion between regions. According to experts the possibility for the regional inequality increase has been relatively high, but possibility has been even higher for the increase of bankrupted micro and small enterprises.

Second, minimum wage differentiation is conceptually not welcome, because it would increase intervention of the state into entrepreneurship, which is unadvisable from the point of view of state economic development.

Third, it is necessary to point, especially in relation to retail trade, that there are different level enterprises dealing in this field in all regions of Latvia, therefore it is impossible to implement the common minimum wage for trade companies in Riga and for a shop in the countryside. Experts suppose that the only field that could introduce higher minimum wage is construction. In this case from the point of view of the state administrative expenses, it would be more
convenient to facilitate general agreement between employers’ and employees’ organizations. It has to be noted that at the moment there is an agreement between these organizations in construction field, but it is difficult to implement its practical use.

Fourth, the three examined fields are those that employ a large part of low qualified labour force. Among registered free working places in the Employment State Agency, there is the highest demand for retail trade sales man, cargo workers and other professionals connected with construction. If the minimum wages is increased in these fields, the demand for low qualified labour force would decrease and there will be its excess on the labour market (unemployment). In the result the Employment State Agency would face problems in integration of unemployed into the labour market, because construction, retail trade and wood industry are the fields, where it is possible to involve people, who had been without work for a long term. The possibility of these effects after introduction of alternative is evaluated as relatively high.

Fifth, experts noted that minimum wage is considered to be the regulating instrument for achievement of two aims – facilitation of legal employment and increase of employees’ welfare, so now there are doubts if the defined aims are reached. Data that was received by experts together with questionnaires showed that in construction there was the largest difference between CSB and WIF data about the amount of average wage. Data shows that the average wage in construction overruns the minimum wage in the state, which make one believe that this is not the best tool for fighting illegal employment in this field. There is no evidence that a rapid increase of a minimum wage would facilitate the fight against non-registered employment in the field, and there is a question what happens with the real payment – if it increases or, increasing the minimum wage in the field, the situation of employees actually will not get worse.

Other consequences of the introduction of differentiated minimum wage in three mentioned fields would be increase of prices for services of corresponding fields, which would cause changes in employment types (change of the labour contract from full into part-time load) and decrease of the amount of employed in affected fields.

Experts think that positive effects might not be that significant to compensate the negative effects. In order to solve the situation it is necessary to facilitate organization of employers’ unions and support conclusion of agreements between field enterprise unions and labour unions.

Experts have anticipated possible results of introduction of possible policy and they tried to evaluate the part of employees that could be affected by the policy introduction. Results are summarized in table 14. Increase of the state administrative expenses is not mentioned in the result list. The state administrative expenses are not mentioned in the list of results, because the possibility of that result was evaluated with the maximum of probability. It was not worth to estimate the amount of employed who would be under the impact; there were too many interpretations about the possible impact (from the total employed till the workers of the responsible institution in particular).
### Table 14. Introduction of differentiated minimum wage into construction, retail trade, forest exploitation/wood industry fields. Prognosticated consequences of action policy

<table>
<thead>
<tr>
<th>Consequences/results</th>
<th>Evaluation of impact</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Probability</td>
</tr>
<tr>
<td>Increase of uncertainties about affiliation to a certain field of entrepreneurship</td>
<td>High</td>
</tr>
<tr>
<td>Increase of prices for services of corresponding three fields</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Bankruptcy of small enterprises</td>
<td>Relatively high</td>
</tr>
<tr>
<td>The Employment State Agency will have lower possibility involve unemployed (low qualified jobseekers) in these 3 fields</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Increase of prices for services of other (not connected) fields</td>
<td>Medium</td>
</tr>
<tr>
<td>Increase of regional inequality</td>
<td>Medium</td>
</tr>
<tr>
<td>Search of a new form of a work contract (for instance, passing to part-time job, hour payment, employees will register themselves as self-employed etc.)</td>
<td>Medium</td>
</tr>
<tr>
<td>Decrease of non-registered employment (including “envelope wage”)</td>
<td>Medium</td>
</tr>
<tr>
<td>Decrease of number of employees in 3 mentioned fields</td>
<td>Medium</td>
</tr>
<tr>
<td>Increase of labour force movement between national economy fields</td>
<td>Medium</td>
</tr>
<tr>
<td>Decrease of motivation to pay taxes</td>
<td>Medium</td>
</tr>
<tr>
<td>Break action of development of 3 corresponding fields</td>
<td>Medium</td>
</tr>
<tr>
<td>Improvement of working conditions</td>
<td>Medium</td>
</tr>
<tr>
<td>Decrease of additional benefits as the kind of salary</td>
<td>Medium</td>
</tr>
<tr>
<td>Decrease of cross-boarder migration</td>
<td>Medium</td>
</tr>
<tr>
<td>Increase of the non-registered employment</td>
<td>Medium</td>
</tr>
</tbody>
</table>

*Note: The results of the expert inquiry were grouped. There were five probability groups made: high (81% - 100%), relatively high (61% - 80%), medium (41% - 60%), relatively low (21% - 40%) and low probability (up to 20%). A similar classification was made for the amount of affected workers: high (81% - 100%), relatively high (61% - 80%), medium (41% - 60%), relatively low (21% - 40%) and low specific weight (up to 20%).*

Theoretically it is possible to introduce minimum wage in such fields like construction (F), retail trade (G52), forest exploitation/wood industry (A02), but it would cause additional implementation difficulties: identification of an enterprise, adequate calculation of differentiated wage, rise of various negative effects.

Experts suggest stimulating development of employers’ unions and labour union, therefore stimulating general agreement conclusion, which would include minimum wage of the field. If the minimum wage of a certain field is defined on the basis of a collective agreement, then
the gained result should be more effective than in case of a differentiate minimum wage defined by the state. Labour unions of the fields would try to achieve the maximum minimum wage, assuring that there would be no decrease of the employment level; meanwhile the employers’ organizations would try to prevent a strong increase of minimum wage level, which would negatively affect economic activity of an enterprise. Such mechanism of definition of differentiated minimum wage is considered to be optimal from the point of view of saving state administrative resources, so, keeping the minimum wage defined by the law, it would be necessary to support effects of social partners to achieve common agreement according to order define din the Labour Law.

10.3. Increase of efficiency of regulations of the Article 18 of the Labour Law

One of alternative solutions for definition of minimum wage, especially differentiated minimum wage, is to implement into practice regulations about general agreements, achieved in collective agreements between employers’ and employees’ organizations, about adjusting the minimum wage to all fields enterprises, basing on the part 4 of the Article 18 of the Labour Law “If members of employers’ and employees’ organizations employ more than 60% of people in any field …” (at present according to the suggestion of the Latvian Employers’ Confederation and Latvian Free Labour Union, in amendments of the Labour Law there is being a regulation developed that decreases 60% “rate” to 50%).

It is being discussed that this regulation could be added with one more criteria that would affect the force of general agreement in relation to the whole field and would assure the necessary flexibility. This anticipates that is it possible to conclude the general agreement even then, if members of employers’ organizations in some field do the amount of work of products and services 65% more from the common amount of work of products and services in the state (Ministry of Welfare 2006).

It is been observed that there are attempts to facilitate the skill of employers’ organization and employees’ labour union to affect the situation in a certain field, for instance, by defining higher minimum wage in comparison to the one defined by the state, or by defining flexible working hours. So, it would be possible to ensure higher flexibility in the regulation of a concrete field, and to affect the level of social security for employees of a certain field – which all would help to keep the labour force in Latvia, fight against unfair competition and shadow economics.

Laws and regulations that are in force now and which regulate labour relations totally support the possibility of general agreement between employers and employees in Latvia, except the condition about the 60% “rate” of the part 4 of Article 18 of the Labour Law. So, it can be pointed that there are no obstacles on the formally institutional level. It is known that most employers belong to the category of small and middle enterprises, therefore the difficulties to join such organizations that would unit 60% from working in the field, are basically practical and not institutional.

The analysis of image and impact of social partners conducted within framework of WIF research shows that Latvian labour unions exist in large enterprises and public sector. At
present, labour unions are not that strong yet to influence questions about the work and labour organizations on the level of fields and enterprises, introducing bilateral social cooperation. This fact is defined with a small member number, lack of leaders, low popularity of labour unions among youth, lack of solidarity and other negative factors.

Employers’ organizations have to facilitate participation of employers in organizations (paying special attention to increase of participation of small and middle enterprises), building common trust and cooperation. Experts consider that organization of employers’ unions has to be stimulated with corresponding legislation, i.e. it would be necessary to point that employers definitely have to unite in employers’ organizations. That would increase the interest of employers and in the result it would be defined what is necessary to conclude a general agreement with the representatives of employees.

**10.3.1. Actions for stimulating of implementation of the alternative**

Discussing the implementation of the part 4 of the Article 18 of the Labour Law, the experts advised following stimulating means:

- To decrease the initial condition of the part 4 of the Article 18 of the Labour Law about unification of 60% of employees to 50% or even 40%;
- Change legislation in order to stimulate employers unite in organizations;
- To announced the regulation of Article 18 as the only mechanism for definition of the minimum wage in those fields, where there are strong employers’ and employees organizations (education, medicine, construction, transport), and abolish the necessity for them to abide statutory minimum wage;
- Make fields, where there are strong employers’ and employees organizations, conclude and announce general agreement, anticipating state sanctions, if the agreement is not fulfilled (e.g. the state would define a minimum wage, which would be high enough to stimulate the field to unit);
- Abolish the minimum wage force in large enterprises (above 500 employees), making these companies conclude a collective agreement with a labour union of its own company or any other;
- Actively use conclusions and examples of “Labour Market Studies of Ministry of Welfare” in order to educate employees about the effect of the lack of the labour contract on the salary and social insurance; to consider those forms of social insurance that would be important for young and active workers.

The first suggested event (decrease of the condition of the part 4 of the Article 18) is being implemented now. Its effects will be felt after Saeima will have made amendments to the Labour Law. 50% of represented employees in case of Latvia are considered to be a high ratio; it would be stimulation to unit for those fields, which had not had a sufficiently high representation up to now.

The second event is not being implemented yet. Experts mention an example with Germany, where the legislation anticipates organization of employers. As it has been mentioned before, Germany is one of the countries where statutory minimum wage does not exist.
The third to fifth event are not being implemented yet, but it is being considered that in this way the government would help in creating a situation, when the general agreement is not only concluded, but it works on the labour market. Experts think that the collective and general agreements have to be stimulated gradually, starting with those fields of national economy, where there are the most positive conditions meant for achieving the agreement (here it would be enough with broad representation in organizations and experience in concluding a collective agreement).

In fields mentioned in the third suggestion there are strong labour unions with sufficient representation, therefore it could be expected that abolishing the statutory minimum wage in these fields, the agreement would be achieved. But it is necessary to point that there is a certain risk introducing traditions into general agreement through these fields. Employees’ organizations of educational and medical fields have frequently discussed with the government the possibility of increasing wages, but in the result of debates there have been only the most essential employees’ demands satisfied. The government considers that employer’s possibilities depend on budget income; therefore possibilities of development of a dialog in these fields are restricted. According to WIF data, Latvian private sector is the one that would need an experience in concluding of collective and general agreements.

The forth and the fifth suggestions are appropriate for realization in both, public and private sectors. But it has to be admitted that possibilities of implementation of these suggestions are also restricted. The WIF research data show that there are higher wages in larger enterprises than in smaller ones in terms of number of employees. This means that wage policy in larger enterprises is comparatively enabling and employees working there might not feel a real necessity of collective agreements. In this context a collective agreement could be a formal document that is concluded according to legislation demands (if such are defined). This outcome might not give the expected result, i.e. it would not facilitate conclusion of collective agreements in other enterprises.

Implementation of the sixth suggestion could be at least partially realized in terms of publicity of a project “Labour Market Studies of the Ministry of Welfare”. For instance, after analysis of the WIF research results there have been various regularities discovered anent to the effects of existence and non-existence of the Labour Law over wages. Representatives of labour unions and employers’ organizations are advised to get acquainted with research results and use them in their action planning and opinion argumentation. The Ministry of Welfare, being the institution that supervises the labour market, should actively engage in WIF research result publishing and evaluation of recommendations mentioned above.

Looking through the suggestions it can be seen that they anticipate at least primary active pressure from the government, the implementation of which demands a certain readiness to risk. It demands that the responsible institution (the Ministry of Welfare) is sure that the implementation of the Article 18 of the Labour Law into practice is necessary for Latvia. It is possible that a faster achievement of results could be stimulated by cooperation with employers of larger companies, because a part from smaller companies considers that the initiative of larger companies is needed in order to conclude the general agreement.

If the Ministry of Welfare chooses a more moderate approach for regulation of the labour market, then the minimum wage would continue increasing in the present sequence like other member states of EU do.
10.3.2. Social and economic consequences of the alternative introduction

Speaking about results of introduction of collective and general agreements, it is necessary to mention two situations. In one case, if the government keeps defining even the formal minimum wage in the state, some of the further described consequences will not be fulfilled, because the their possibility will increase, if the government decides to realize the second scenario. This anticipates that after a certain time, 5-6 years after implementation of the Article 18 of the Labour Law that social partners agree about work payment according to general agreement – this would be the only mechanism how the minimum wage would be defined in Latvia.

When examining consequences, those which corresponds to both situations is looked the first; afterwards, the second scenario will be analysed where statutory minimum wage does not exist anymore.

At present, the main part of Latvian business belongs to micro, small and medium enterprises, employers’ and employees’ unions are its smallest part – which means that it is difficult to conclude a general agreement that would be binding to the whole field. One of possible solutions how to decrease this risk, is to develop a legislation that would stimulate employers to join together in organizations, which is like it is in Germany. One of the drawbacks of general agreements is that large companies with the help of general agreements would set high minimum wages of a field, which would exclude small enterprises from the market. Experts evaluate the possibility of this risk as average.

The existing regional differences could cause decrease of competitive capacity of different entrepreneurs (especially small ones) or even bankruptcy in case the there was an increase of minimum wage in a concrete field of national economy, using regulations of the Article 18. If large companies of a certain field would agree upon an increase of the minimum wage, it would be binding for the whole field – it means that small companies in less developed regions would have to stop their commercial activities, because the costs would be too high.

Essential problems after introduction of the alternative would arise in terms of definition of company’s activity area, which was discussed in chapter two. At present, there is no legislation that would allow defining affiliation of an enterprise to a certain field, and there is no institution that would handle this account control. It would be necessary to answer the question about enterprise affiliation to a concrete field. Conclusion of a general agreement would make the possibility of actualizing this problem very high. In the case of general agreement involved social partners could control company’s field, and the state would not have to spend significant financial and administrative resources in order to introduce and control the differentiated minimum wage. But specialists are careful evaluating state benefits, because they think that even in case of the general agreement the state administrative expenses would increase. For instance, the government would have to control the content of concluded collective agreements, if they are in accordance with Labour legislation and if there are any discriminating regulation. But experts do not expect decrease of budget benefits, on the contrary – it is anticipated that state benefits would increase.

Evaluating this policy alternative, the experts point that in the short-term it would facilitate Latvian economic development, but in the long-term (after 20-30 years) it would be developing in the opposite direction – the experience of old EU member states gives the
evidence for this: sometimes too strong influence of labour unions on governmental decisions and protection of labour market. However, the present short-term positive results might seem quite attractive. Experts think that general agreement would facilitate development of labour force market in Latvia, and as the result the non-declared employment would decrease, which is considered to be a priority of the policy etc. But all mentioned benefits mostly depend on the level of organization of employers and employees.

In order to evaluate possible losses and benefits, experts were suggested a situation, which is not characteristic for Latvia – Latvian government decides that in 5-6 years the Article 18 of the Labour Law would be the only mechanism for definition of minimum wage and there is no statutory minimum wage any longer. Experts think that the suggested 5-6-year-long period is too short and that is why the situation in the next further years would get worse. That would be expressed in definition of lower minimum wages in fields, in which labour unions are weaker than employers’ organizations. The possibility of such situation is quite high, because involvement into labour unions is low, which is only characteristic for certain fields and large enterprises.

Thus, the rapid action, abolishing the minimum wage defined by the law, it would decrease social insurance of employees. Although it is considered that this situation would force employees create labour unions, it is possible to have an opposite effect – the number of labour force moving abroad from Latvia would increase. Wage regulation with general agreement would improve, if employees join together in labour units, which would make the general agreement not only formal but also factual and according to interests of both sides. Unfortunately, it is not possible to predict how fast employees would start joining together in labour unions because it depends on various circumstances (the possibility of their prognosis is quite low).

Evaluation of results that would appear if minimum wages were defined by the general agreement (and not by the law) are summarised in table 15.

At the moment, these results are considered to be contradictory, because they contain those results and consequences, which could be implemented in short term and those that could be implemented in the long-term. Long-term results are announced basing on experience of the EU member states. These are the following consequences: increase of minimum wage, increase of the number of highly qualified specialists, legitimate increase of wage, increase of tax revenues in the state budget, part of people working abroad will come back to Latvia, improvement of working conditions etc.

By introducing policy, it is necessary to pay attention that the government has to deal with essential short-term results, which mostly have a negative character. These are large wage differences among national economy fields, initially expected formal minimum wages in fields that would negatively influence low qualified labour force, decrease of tax revenues, increase of migration etc.
Table 15. Introduction of the part 4 of the Article 18 of the Labour Law as exclusive regulating mechanism of the minimum wage within the nearest 5-6 years. Prognosticated consequences of action plan

<table>
<thead>
<tr>
<th>Consequences/ results</th>
<th>Evaluation of impact</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Probability</td>
</tr>
<tr>
<td>Increase of minimum wage</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Problems in identification of enterprise activity fields, if they are working in various spheres</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Increase of the number of highly qualified workers</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Legitimate increase of wage</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Increase of tax revenues in the state budget</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Part of people working abroad will come back to Latvia</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Difficulties to realize general agreements in the public sector</td>
<td>Relatively high</td>
</tr>
<tr>
<td>Improvement of working conditions</td>
<td>Medium</td>
</tr>
<tr>
<td>Increase of the number of enterprises</td>
<td>Medium</td>
</tr>
<tr>
<td>Difficulties to control collective agreements</td>
<td>Medium</td>
</tr>
<tr>
<td>Decrease of non-registered employment</td>
<td>Medium</td>
</tr>
<tr>
<td>Large differences in wages among national economy fields</td>
<td>Medium</td>
</tr>
<tr>
<td>Large enterprises with general agreement press out small enterprises from the market</td>
<td>Medium</td>
</tr>
<tr>
<td>Increase of the number of employees</td>
<td>Medium</td>
</tr>
<tr>
<td>Facilitation of economic development in short-term</td>
<td>Medium</td>
</tr>
<tr>
<td>Increase of regional inequality</td>
<td>Medium</td>
</tr>
<tr>
<td>Minimum wages will be formal in various fields</td>
<td>Medium</td>
</tr>
<tr>
<td>Rate of wage increase</td>
<td>Medium</td>
</tr>
<tr>
<td>Decline of competitive capacity</td>
<td>Medium</td>
</tr>
<tr>
<td>Increase of the non-registered employment</td>
<td>Medium</td>
</tr>
<tr>
<td>Decrease of the number of employees</td>
<td>Relatively low</td>
</tr>
<tr>
<td>Decrease of tax/state budget revenues</td>
<td>Relatively low</td>
</tr>
<tr>
<td>Increase of cross-boarder migration</td>
<td>Relatively low</td>
</tr>
</tbody>
</table>

Note: The results of the expert inquiry were grouped. There were five probability groups made: high (81% - 100%), relatively high (61% - 80%), medium (41% - 60%), relatively low (21% - 40%) and low probability (up to 20%). A similar classification was made for the amount of affected workers: high (81% - 100%), relatively high (61% - 80%), medium (41% - 60%), relatively low (21% - 40%) and low specific weight (up to 20%).

Evaluating the possibility to announce the Article 18 of the Labour Law as the exclusive mechanism for defining the minimum wage, initially the evaluation of experts was divided into two equal parts. The first part considered that the Article 18 of the Labour Law should be implemented into the regulation praxis of Latvian labour environment as soon as possible, for
instance, starting from the year 2010. The second expert group had been more cautious and advised the introduction of the regulation for 2020.

In the result of the expert survey two thirds of specialists supported the conclusion that the point of reference for introduction of the Article 18 of the Labour Law as the exclusive mechanism for defining the minimum wage is 2015. But in order not to make such decision too radical, it is necessary to perform an active society preparation as well as to regularly evaluate the level of readiness of employees and employers to achieve mutual agreement. One of the essential indicators for society readiness is an increase of dissemination of collective agreements.

10.4. Conclusions and recommendations

WIF team would like to note that exercised alternatives are not the exclusive regulative mechanisms of the certain industry and that one of those mechanisms must be established in Latvia. In the paper, several solutions are analyzed which gives us the opportunity to handle the labour environment in Latvia from different point of view. They can encourage the new discussions or other retrievals for the suitable mechanism of the regulation of wages in Latvia.

Concerning the first policy alternative e.g. the increase of the minimal wage until 68% from the national average wage after 2010 we should note that to carry out completely the scenario established by Ministry of Welfare in the mentioned period of time (five or six years) WIF team did not find realistic.

In general, four scenarios to increase the minimal wage after 2010 were established, and each of them include the period of time until 2020. The first, the basis scenario analyses the possibility of the increase of the minimum wage in the way that in 2020 it would reach 50% from the average national wage. It forecasts that in 2010 the minimum wage in Latvia would be 140 LVL, untaxed minimum – 70 LVL and personal income tax rate will remain in the previous level – 25%. The second scenario of the reduced personal income tax rate describes similar situation: the difference is that personal income tax will go down to 22%. Although, the conceptual government regulation has been currently accepted to reduce personal income tax to 15%, the experts think that this scenario of the reduction is less possible than the previously mentioned.

The third, the optimistic scenario of the minimum wage is the most related to the work task of the Ministry of Welfare, i.e. it foresees that the minimum wage as to 2020 will reach 68% of the national average wage. Disregarding the scenario elaborated, it is unlikely to be fulfilled. At the present moment, there have not been any political alternative idea realized nor in the new or old EU member states, neither in the candidate states during the last decade. The highest specific weight of the minimum wage as to the average wage was practically observed in Ireland, in 2004 (51%) and in Belgium and Malta, in 1995 (52%). The specific weight of the minimum wage in Latvia was equal to that of the Check Republic, Hungary, Estonia and Great Britain (34 – 39%). In addition, experts of the survey indicated several remarkable risks, the occurrence probability of which will considerably increase if the specific weight of the minimum wage will remain high in comparison with the national average wage.
If the proportion of the minimum wage as to the national average wage will be high, then, first of all, the difference of wages between high-qualified and low-qualified employees will decrease. The calculations of the optimistic scenario show that the income of the majority of employed people (both high and low-qualified) should stay within the limits of one to two minimum wages in order that the minimum wage would reach 68% of the national average wage. This is approximation of incomes that is characteristic for a social democratic vision of the world and the correspondent strong social protection.

If the difference in wages among the employed people will be small, then the high-qualified labour force may lose motivation to work because return for education and personal skills would be considerably lower. In order to favour high-qualified labour force to work more efficiently, an employer will be forced to look for the mechanisms of motivation so that the difference in wages would be felt in another way than it was felt until then. Disregarding the efforts of the executives to reduce the difference of the reward among high and low-qualified employees, an enterprise will try to find ways of lowering these requirements. Wage difference for labour force having different levels of qualification is a requirement determined by the market, and it is reasonable for the government to define the fundamental requirements rather than to follow a strict regulation of the wage policy. It is to be noted that the EU member states prefer special programmes of tax reduction for definite social groups rather than strict wage regulation.

The fourth scenario, which is comparatively pessimistic, foresees the slowest scenario for minimum development, i.e. its percentage comparing the national average wage remains at the present level, i.e. at the amount of 37% of the national average wage. This scenario foresees an even increase tempo of the minimum wage and it is close to the EU indices.

In relation to the second described alternative, i.e. differentiation of the minimum wage in those fields of national economy that are the most subjected to the risk of undeclared employment (construction, retail trade, forestry and wood-processing), the majority of experts did not support this approach at all. The main arguments of experts against introduction of this policy were related to the enforcement of state administrative pressure and inapplicability of the present operating normative acts to introduce a differentiated minimum wage as well as to the targets of minimum wage fixation and labour particularities in the three mentioned industries.

In relation to the first counterargument, i.e. growth of state administrative pressure, it is necessary to consider that interference of the state in the control of one of the industries is not desirable from the point of view of economical development. This action requires additional investments. Additional functions and delegations to the existing responsible institutions will be regarded as a burden in a situation when the capacity of state control institutions is considered comparatively weak already. Although formally, it is possible to delegate the realization of the accepted norms in practice to State Revenue Service, but there will be no possibility of having a practical advantage without creation of an appropriate normative basis.

The inapplicability of the normative basis to the minimum wage in Latvia is another remarkable counterargument of the system implementation. The operative legislation does not prescribe an obligatory registration of the sphere of activity on an enterprise. In order to introduce a differentiated minimum wage, the identification mechanism for sphere of activities of an enterprise must be found or created, which requires definite state investments.
(expenses of introduction). Each more complicated administrative system would require an additional maintenance expenses.

The third requirement in defining the differentiated minimum wage is to determine the controlling institution that would check whether an enterprise fulfil the new requirements. Even if it seems that the State Revenue Service (SRS) is the institution for which to delegate the responsibility, the operative legislation does not prescribe a direct interference with the economical activities of enterprises.

Introduction of the differentiated minimum wage will require not only the state investments, but also investments of the employers. If the principle of the main sphere of activities of an enterprise is used in defining the differentiated minimum wage, there should be a precise identification mechanism. The present annual report form to submit to SRS is not appropriate for this. If annual report forms would be changed, bookkeepers of enterprises will have to be trained for the new accounting order.

Speaking about the next group of counterarguments, it is to be reminded that the minimum wage as a control mechanism is used to reach two targets – the favour of the legal employment and the welfare of the employees. The reaching of these targets may be evaluated as doubtful, now. When comparing the wage in the three fields, there was a great difference between the average wage in the official (the data of the Central Statistical Bureau) and the WIF research wage rate in the construction. Judging by these facts, the average rate in construction exceeds the minimum wage of the state at several times, and this creates doubt whether the minimum wage is the right means of struggle against illegal employment in the field. Experts indicate that first of all the identification of the exact reasons of illegal employment in the three above mentioned fields should be defined, which should help in elaboration of a programme of preventive measures.

One of the possible motives of illegal employment in the three fields of national economy is the particularity of the work. Fields of construction, forestry and retail trade require a low-qualified labour force. Persons out of work are also considered to constitute a part of this group of people, the working capacity of which has lowered due to the period of unemployment. The three considered fields give them chance to regain their place in the labour market. When the Labour Law provides for a relatively strict order of employing and dismissal, it is hard to meet these requirements. This may become one of the motives of illegal employment. In addition, increase of minimum wage in the three fields will reduce the ability of long-term unemployed to join the labour market if they look for work in the fields of construction, forestry or retail trade.

In the case the government decides to differentiate the minimum wage in the considered fields, it certainly should differ between the fields; however the introduction of the system could take place simultaneously. But experts say that the only field that could offer bigger minimum wage is the construction, although it would not be preferable to spend state administrative and finance resources for the introduction of the system. It would be better to favour a conclusion of the general agreement in the field of construction.

The third political alternative, i.e. stimulation of the effectiveness of Article 18 of the Labour Law, is the most difficult to implement. It is related to the favouring of employers’ and employees’ activities. At present, the degree of self-organizing of the both parties is relatively
low. Collective agreements are generally concluded on the number of the employees in the enterprise.

Yet, this political alternative could seem attractive for several reasons. First of all, the general agreement or the collective agreement is a form of wage determination in the states that are geographically close to Latvia – Scandinavian countries and Germany. Secondly, the alternative offers a greater flexibility that is relevant for employers – a general agreement is defined for each field considered separately. As the result of this, wages in one field may differ from that in other fields, and this is why it should correspond to the efficiency of the correspondent field as labour requirements in it.

In order to favour application of the Article 18 of the Labour Law, it is advisable first of all to improve the basis of normative acts and thus to stimulate employers and employees to unite in organizations that would stand for their interests. Secondly, it is advisable to terminate the power of the minimum wage in large enterprises (having more than 500 employees) and to delegate them the responsibility to conclude collective agreements with the labour union of the enterprise of sphere of activity. Thirdly, it is proposed to amend the Article 18 part 4 of the Labour Law and to reduce the amount of 60% to 50% or even 40% of employees to unite and then, when organizations of employers and employees will be founded, to restore gradually the proportion of included employees back to the present level.

Considering the proposal, one can understand that it requires at least an initial pressure of the government, fulfilment of which needs a definite daring and the willingness to take the risk. It also requires certainty of Ministry of Welfare that implementation of the Article 18 of the Labour Law is a vital necessity for Latvia or that this is the recommendable controlling model of differentiated minimum wage for Latvia.

In case the Ministry of Welfare chooses moderate field regulating policy, it can prolong defining the statutory minimum wage in previous order or involve social partners into more active discussions.
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