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**THE EU-UKRAINE CIVIL SOCIETY PLATFORM**

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**The role of remuneration in reducing poverty and its impact on labour migration (practices of governmental and collective bargaining regulation in Ukraine and the EU)**

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**The role of remuneration in reducing poverty and its impact on labour migration (practices of governmental and collective bargaining regulation in Ukraine and the EU)**

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# Overview of the issue

As it progresses towards European integration, Ukraine is undergoing large-scale reforms. However, there is a lack of due attention to social and economic issues and particularly to the labour market, where the remuneration arrangement plays an essential part.

In recent years, **negative trends concerning the low level of earnings, which do not allow for any improvement in the current welfare of Ukrainian workers,** **have become more entrenched** due to:

* the economic crisis and threats to the territorial integrity of the country;
* infringements of current legislation and lack of efficient legal and economic instruments in the area of wage protection;
* poor corporate social responsibility;
* lack of effective and meaningful social dialogue.

Wages that fail to meet workers' basic needs and at the same time are the lowest among European countries, as well as increasing wage arrears of over UAH 2.5 billion (as of January 2018), have resulted in:

- deepening poverty in the population, including among employed workers (20.1% in the first half of 2017);

- **migration abroad as a consequence of growing poverty in the working population;**

- chronic deficits in the Pension Fund of Ukraine and state social insurance funds, leading to a low level of pensions and other social benefits;

- low purchasing power of the population, resulting in declining production and in economic recession;

- a build-up of utility payment arrears in the population (UAH 36.9 billion by the end of January 2018;

- growing social unrest.

Further delays in tackling the problem of the low level of earnings – in view of Ukraine's future accession to the EU – is causing a further decline in living standards among the working population, a shrinking middle-class, a shortage of adequately paid jobs, growing employment in the shadow economy and outward migration of highly-skilled workers.

# Poverty and labour migration

Earning more while working abroad is not the key push-factor for Ukrainian labour migration. Alongside this there is another issue, namely overcoming poverty. Working population poverty leads to a typical psychological problem: how to make one's living today without thinking about the future. It is the lack of prospects for the future, lack of opportunities for professional success as well as the desire to improve one's social status, caused by the insufficient material means for normal living, that is prompting Ukrainians to become migrant workers – referred to as "zarobitchanstvo".

According to the conclusions of the *Human Development Report 2016, Human Development for Everyone,* by the United Nations Development Programme (UNDP), over 60% of Ukraine's population lives below the poverty line. Ukraine also comes 84th in the 2016 Human Development Index ranking list, which is substantially worse than in 2015, when it was in 55th place[[1]](#footnote-1).

# Ukraine's international commitments on combating poverty

At present, the State's commitments to tackling the afore-mentioned problems are outlined in a number of strategic documents at both national and international level, including:

* *The* *Association Agreement between the European Union and the European Atomic Energy Community and their Member States, of the one part, and Ukraine, of the other part[[2]](#footnote-2)* – to ensure adequate employment, improvement of the quality of human life, reduction of poverty (Chapter 21, Articles 419 and 420);
* provisions of the *European Social Charter (Revised)*[[3]](#footnote-3) ratified by Ukraine as regards employees' right to fair remuneration ensuring adequate standard of living for themselves and for their families;
* Conventions of the International Labour Organization ratified by Ukraine, including:
* *Protection of Wages Convention[[4]](#footnote-4) (No. 95)* setting out the privilege of remuneration in the event of bankruptcy or judicial liquidation of an undertaking (Article 11);
* *Social Policy (Basic Aims and Standards) Convention (No. 117)[[5]](#footnote-5)*, which positions raising living standards as a key goal for economic development policy, sets the overall policy direction for achieving welfare and development and determines the minimum subsistence level (Articles 1, 2 and 5);
* *Minimum Wage Fixing Convention (No. 131)[[6]](#footnote-6),* requiring account to be taken of the needs of workers and their families, the overall level of wages in a country and the need to hold large-scale negotiations with both employers' and employees' representative organisations when setting a minimum level of wages (Articles 3 and 4);
* *Protection of Workers' Claims (Employer's Insolvency) Convention (No. 173)*[[7]](#footnote-7) making remuneration a privileged payment in the event of the employer's insolvency (Part II);
* *ILO Decent Work Country Programme for Ukraine 2016-2019*[[8]](#footnote-8) revising the minimum wage in accordance with the criteria set by the ILO *Minimum Wage Fixing Convention* and aiming at reducing wage arrears (Priority 3, Outcome 3.2);
* *The* *Strategy for Sustainable Development* "*Ukraine* *– 2020"*[[9]](#footnote-9) aiming at introducing European standards of living in Ukraine;
* *The Strategy for Overcoming Poverty*[[10]](#footnote-10) aiming at improving remuneration in order to overcome the high poverty rate among the working population, set a minimum subsistence level in line with EU practices, raise minimum wages in accordance with international practices and ILO *Convention No. 131 guidelines*, developing sectoral remuneration standards and improving conditions for public sector workers' remuneration;
* *Mid-Term Government Priority Action Plan until 2020*[[11]](#footnote-11) aiming at raising the minimum wage level, reducing the poverty rate, further reforming the remuneration system and establishing an insurance institution for compensation for workers' claims in the event of the employer's insolvency (Part 12);
* *The General Agreement on Regulation of Basic Principles and Norms for Implementation of Social and Economic Policy and Labour Relations in Ukraine for 2016-2017*[[12]](#footnote-12), sectoral agreements on State and contractual insurance of remuneration, etc.

# Evaluation of living standards in Ukraine

In terms of living standards, Ukraine has become one of the poorest countries in the world:

* Ukraine scored seventh in Bloomberg's annual ranking of the poorest countries[[13]](#footnote-13);
* nearly 60% of Ukrainians live below the poverty line[[14]](#footnote-14);
* the poverty rate among working citizens is as high as 19-23%[[15]](#footnote-15);
* the share of remuneration for employed workers decreased from 49.9% (2013) to 44.1% in the GDP structure by categories of income (2nd quarter 2017);
* the share of wages and salaries in the income structure of the population remains low: 40.9% (2013) – 43.3% (3rd quarter 2017).

According to the *Economic Activity of the Population* survey carried out by the State Statistics Service of Ukraine based on ILO methodology in the 3rd quarter of 2017, the working age population (15-70 years) stood at 28.4 million including 16.2 million employed, 1.17 million unemployed and 11.1 million economically inactive people. The unemployment rate reached 9.4% of the economically active population and persistently remains close to the highest level recorded over the last 15 years.

Devaluation of actual income has changed the structure of household expenditure – purchases of goods and services increased from 84% (2013) to 89.2% (3rd quarter 2017) with a simultaneous reduction in savings from 7.7% (2013) to 0.5% (3rd quarter 2017)[[16]](#footnote-16). At the same time, the number of households receiving utility subsidies increased from 4.6 million in December 2015 to 6.27 million as of January 2018[[17]](#footnote-17).

# Effects of the current remuneration policy

The significant gap between the growing cost of living and the unduly low level of minimum fixed wages results in a low level of earnings.

In 2017, **the monthly average nominal salary** grew, compared to 2013, by 116.5% to UAH 7 104, but this did not reduce the number of workers who, having worked out 50% and more of their work lives, were paid within the limits of the minimum salary (5% or UAH 476.2 thousand in December 2013 and 6.6% or UAH 487.2 thousand in December 2017). Among other things, this can be due to changes in the legislation as regards the structure and content of the minimum salary, which, from 1 January 2017, was doubled to meet the current minimum subsistence level for the working population (UAH 3 200). At the same time, the number of workers who received salaries of over UAH 10 000 has increased from 3.8% or 361 900 in December 2013 to 23.5% or 1 734 600 in December 2017[[18]](#footnote-18). However, despite this positive trend, the devaluation of the national currency caused a significant drop in salary size in foreign currency equivalents. For instance, in 2013, the average monthly salary amounted to EUR 309.3 whereas in 2017 it dropped to EUR 236.8[[19]](#footnote-19) and was lower than the minimum salary size in most of the EU Member States (the lowest being in Bulgaria – EUR 235) and the average monthly salary in Moldova (EUR 273.5).

At the same time, rapid growth in the consumer price index and worsening overall economic conditions in the country caused a noticeable decrease in the actual value of wages to 93.5% in 2014 and to 79.8% in 2015 (compared to the previous year respectively). Even in 2017 the increase in earnings in 2016-2017 has not restored real wages to the pre-crisis level (the consumer price index in 2017 stood at 217.2% as compared to 2013, while the increase in the average monthly nominal salary over the same period amounted to 216.5%)[[20]](#footnote-20).

Thus, non-compliance with the current legislation on the part of both government authorities and employers, lack of efficient government control and effective legal instruments, insufficient corporate social responsibility and the weak position of the trade unions resulted in the negative trends that undermined improvement to Ukrainian workers' welfare, namely:

* cheap labour and low level of wages as compared to the equivalent indicators in developed European countries;
* unduly low minimum social standards and guarantees with artificial restraints for their growth, at least, considering the level of inflation;
* inequalities in remuneration at all levels resulting in a distorted differentiation based on position, qualification, gender, economic sector, territorial location, etc.;
* growing wage arrears and lack of efficient legal and economic instruments for worker protection.

# Remuneration regulation in the EU Member States

Wage regulation in the EU member states is based on various economic, political and other conditions specific to a particular country, as well as on interrelated components such as:

1) minimum wage, increases in the ceiling during inflationary periods, taxation policy **(State regulation);**

2) general procedure of income indexation, system of pay rates, additional payments and bonuses, other forms and systems of remuneration, etc. **(collective agreement regulation);**

3) average wage (salary) **(labour market)**.

The international instruments regulating the key remuneration issues are listed in the table below:

# International instruments for regulating the key issues of remuneration

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| **Instrument** | **Issues** |
| **ILO Minimum Wage Fixing Convention (No 131)** with Special Reference to Developing Countries | When fixing a minimum wage, one should not only consider workers' and their families' needs, but also take into account economic aspects including requirements for economic development, labour productivity as well as sustaining a high level of employment in the country. |
| **ILO Minimum Wage Fixing Recommendation (No. 135)** with Special Reference to Developing Countries | Minimum wage fixing should constitute one element in a policy designed to overcome poverty and to ensure the satisfaction of the needs of workers and their families. The fundamental purpose of minimum wage fixing should be to give wage earners the necessary social protection as regards minimum permissible levels of wages. |
| **European Social Charter (Revised)** | Defines the right of all workers to fair remuneration ensuring a sufficient living standard for themselves and for their families. |
| ****Resolution** on promoting social inclusion and combating poverty, including child poverty, in the EU (2008/2034(INI)) of 9 October 2008**[[21]](#footnote-21) | The European Parliament recommends fixing minimum wages (in legislation and collective agreements at national, regional or sectoral level) to provide for remuneration of at least 60 % of the relevant average wage. |
| **ILO Protection of Wages Convention (No. 95)** | Employers shall be prohibited from limiting in any manner the freedom of the worker to dispose of his wages  In the event of the bankruptcy or judicial liquidation of an enterprise, the workers employed therein shall be treated as privileged creditors as regards wages due to them. |
| **ILO Protection of Workers' Claims (Employer's Insolvency) Convention (No. 173)** | In the event of an employer's insolvency, workers' claims arising out of their employment shall be protected as the first priority.  The payment of workers' claims against their employer arising out of their employment shall be guaranteed through a guarantee institution when payment cannot be made by the employer because of insolvency. |

Fixing the minimum level of income is one of the major means and t**he primary function of State regulation of wages**. The State defines enterprises' obligations in terms of wage management. Even under market regulation of wages, one cannot completely refuse State regulation in this area. This is especially relevant in the period of the transition to a market economy, where State intervention can be in the form of the State guaranteeing remuneration, benefits and compensations. The experience of the EU Member States with mature economies shows that the system of minimum state guarantees of remuneration includes:

* minimum wage;
* minimum subsistence level;
* procedure for their correction in relation to rising prices;
* procedure for wage regulation depending on place of residence (regional coefficient) and hazardous working conditions;
* 90% of all countries in the world have fixed minimum wage systems[[22]](#footnote-22).

When fixing minimum wages, the EU Member States consider the following key factors:

* living standards differentiation for various social groups;
* size of social benefits;
* employment rate;
* labour productivity[[23]](#footnote-23).

There are two internationally practised approaches for setting minimum wages. The first approach uses a ***consumer goods basket*** – a monetary equivalent of essential goods and services. The second one is based on the assumption that social needs stemming from socio-cultural conditions should be also satisfied at a minimum level along with the essential physical need for food and accommodation. The second approach therefore correlates fixed minimum wages with the current level of wages[[24]](#footnote-24).

In most countries, the lowest level of remuneration for all workers is fixed by law. The fixed minimum wage is most important for low-skilled labour, youth, women and immigrants. Procedures for setting and mechanisms for correcting minimum wages are defined differently in various countries, namely by:

* national legislation;
* general agreements at national level;
* sectoral pay rate agreements;
* local government;
* specialised governmental authorities, etc.

One can identify two groups of countries among the EU Member States by type of minimum wage regulation.

The **first group** comprises France, the Netherlands, Portugal, Spain and Luxembourg, where minimum wages are set by the law, as well as Belgium and Greece, where minimum wages are set by agreements. The **second** includes countries where minimum wages are approved by sectoral agreements (Italy and Denmark) or by specialised bodies (wage committees, as is the case in the UK).

# Comparison of wages in Ukraine and the EU Member States

In order to increase the efficiency of human capital, the State has to promote remuneration growth as a major source of recreation and accumulation of human resources, since low and delayed remuneration negatively affects the quality of workers' recreation.

As indicated above, the significant gap between levels of remuneration in Ukraine and abroad is the key factor for labour migration on the part of Ukrainian citizens.

The only goal of Ukrainian labour migrants is that of maximising their income and minimising expenses.

The increase of the minimum salary to UAH 3 200 (EUR 106.7) from 1 January 2017 provided an impetus for wage growth in Ukraine. For instance, the average salary of a full-time worker, in November 2017, amounted to UAH 7 479 or EUR 238.8 (the National Bank of Ukraine (NBU) official exchange rate for that period)[[25]](#footnote-25).

As usual, the lowest average salaries were in the following sectors: temporary accommodation and meals services (UAH 5 062 or EUR 161.6), healthcare and social services (UAH 5 101 or EUR 162.9); education (UAH 5 859 or EUR 187.1); agriculture (UAH 6 142 or EUR 196.1).

Compared to 2008, minimum wages grew in all countries except Greece, where it decreased by 14%. Over the period 2008-2017 the greatest minimum wage growth occurred in Bulgaria (109%), Romania (99%), Slovakia (80%), as well as in Estonia (69%), Latvia (65%) and Lithuania (64%).

Despite almost annual growth in the minimum wage in Ukraine, the purchasing power of the basic social guarantees cannot keep up with the overall wage and inflation dynamics. Besides, their excessively low level means that Ukrainian workers' earnings fall significantly behind those in the European countries: the average salary in Europe, as of early 2017, amounted to nearly EUR 2 100 per month.[[26]](#footnote-26)

The minimum salary in Ukraine, from 1 January 2018, has been fixed at UAH 3 723 (EUR 107.6 under the NBU exchange rate in January 2018), which has almost no effect on most people's living standards because of constantly the rising prices of basic consumer goods and utilities as well as fluctuations in the UAH (hryvna) exchange rate.

The minimum salary in Ukraine lags significantly behind those in the EU Member States. For instance, as of January 2018, the minimum salary amounted to EUR 260.8 in Bulgaria, EUR 407.3 in Romania, EUR 430 in Latvia, EUR 444.1 in Hungary, EUR 462.5 in Croatia, EUR 477.3 in the Czech Republic, EUR 480 in Slovakia, EUR 500 in Estonia, EUR 502.6 in Poland, EUR 676.7 in Portugal, EUR 683.8 in Greece, EUR 747.5 in Malta, EUR 842.8 in Slovenia, EUR 858.6 in Spain, EUR 1 497.8 in Germany, EUR 1 498.5 in France and EUR 1 998.6 in Luxembourg[[27]](#footnote-27).

# Labour migration as a consequence of labour market deterioration in Ukraine

Solving the problem of migration and illegal migration, illegal migrant employment, as well as promoting labour market conditions that combine flexibility and employment protection, work safety and social security, are essential components of the European integration process. This is also mentioned in the Ukraine-EU Association Agreement, Title III *Justice, Freedom and Security*, Article 16 Cooperation on migration*, asylum and border management* and in Title V *Economic and Sector Cooperation*, Chapter 21 *Cooperation on Employment, Social Policy and Equal Opportunities*, Articles 419 and 420.

Lack of opportunities for finding appropriate jobs with decent remuneration on the domestic market pushes Ukrainians to seek jobs abroad. An exact estimate of migrant workers from Ukraine is problematic. According to the latest number of work visas issued to Ukrainian citizens (*Example*: Poland issued 1.2 million declarations of intention to employ a foreigner to Ukrainian citizens in 2016 and 905 thousand such declarations in the first six months of 2017; the Czech Republic (as of September 2017) received 300 000 employment applications from Ukrainian citizens and offered them about 200 000 job vacancies) as well as to various estimates, there are currently at least 3.5-4 million Ukrainians living and working abroad (*unofficial sources*). However, there are no agreed verified estimates on the exact number of migrant workers.

Ukraine has become a donor (exporter) of labour to the EU Member States.

The International Organization for Migration (IOM) Mission in Ukraine estimates Ukrainian migrant workers abroad at nearly 700 000. This number apparently does not take into account the phenomenon (which is very difficult to estimate appropriately) of circular labour migration, where a person leaves the country to work for several weeks or months abroad and then returns to Ukraine – sometimes several times a year. Such migrants may be completely overlooked or, conversely, counted several times, which may lead to both under- and over-reporting of the real number. At times, there appears a figure of 5 million Ukrainian migrant workers that is not confirmed by any research. A reasonable estimate of the more or less constant labour migration is somewhere within the 1.5-3 million range, but since there is no universally accepted methodology (including on circular migration), there are currently no agreed, verified estimates.

Moreover, this figure unfortunately does not cover **illegal** migrant workers.

Ukrainian migrant workers face the issues of illegal employment, labour rights violations, non-compliance with standards adopted in the host country (unregulated working day, safety violations, hazardous work, delayed and incomplete remuneration, labour market dumping in the EU Member States). Ukrainian construction workers agree to these precarious working conditions.

The figure of 3.5-4 million people indicates that almost 10% of the total population of Ukraine (*estimated at 42 403 000, not including the temporarily occupied territories of the Autonomous Republic of Crimea and the city of Sevastopol - as of 1 December 2017*) is missing[[28]](#footnote-28).

One should also note that according to *The Labour Market Assessment* published by the State Employment Service, the employed part of Ukraine's population stood at 16 224 000, while unemployed people amounted to (according to ILO) 1 677 000 for the first nine months of 2017[[29]](#footnote-29). The figure of 3.5-4 million migrant workers thus makes up almost 25% of the country's entire working population.

Migrant workers compensate for their absence by transferring foreign earnings back home. According to the National Bank of Ukraine (*Private Monetary Transfers to Ukraine in 2016 Survey*[[30]](#footnote-30)), the amount of private money transfers from abroad in 2016 amounted to USD 5.4 billion (or 5.8% of GDP), an increase of 5.3% on the previous year.

Most Ukrainian workers abroad are employed in the construction industry (men) and household occupations (women), as well as in the service sector and agriculture (seasonal work).

*Our data on long-term migrants is as follows:* Construction – 45%; Manufacturing – 12%; Agriculture – 11%; Hotels, restaurants, and tourism – 8%. (*Migration in Ukraine: Facts and Figures 2016.* IOM Mission in Ukraine)

We note that not all migrant workers abroad can find jobs appropriate to their skills and qualifications. The majority of them – regardless of their education – work in low-skilled jobs. Men, aged 30-44 years old, prevail among migrant workers. 41% of migrant workers have secondary or specialised education, 36% have higher education[[31]](#footnote-31).

It is sad to note that Ukraine is on the same list as other countries (Albania, Serbia, Vietnam, Bosnia and Herzegovina, Turkey, Kosovo, Moldova and Ghana) whose citizens reside and are employed illegally in the EU Member States. The proportion of those who work abroad unofficially grew to almost 41% in 2015 compared to 28% in 2011.

The worse conditions in the country get, the more Ukrainians are prepared to seek employment abroad without official permission, risking falling victim to human traffickers. (CSP Report *The Labour Market in Ukraine on the part of UP CSP*[[32]](#footnote-32))

# Protection of Ukrainian migrant workers' social welfare rights

Ukrainians who have made the choice to work and live abroad face the problem of social protection, which appears to be the most pressing issue related to labour migration.

**The key problems of failing to ensure appropriate labour and social guarantees in the EU Member States are as follows**:

1. Ukrainian migrant workers may not be in possession of the A1 Certificate confirming payment of social contributions (this document confirms that a person is covered by the social protection legislation).

2. "Re-exporting" (displacement) of migrant workers, where an employee with permission to work in Poland actually works in other EU Member States (we know of instances in Finland, Estonia, Lithuania), while the employer – a hiring company – persuades Ukrainian migrants that this employment system is legal. Example: in contractual terms, Ukrainian construction workers are employees of a Polish company and, once they have a Polish visa, can work in Poland legally. However, they do not physically work there: they are leased, i.e. sent to a partner-company in another country. Note that the goal of their visit is not professional training or exchange of best practices, but real work abroad that requires permission from the government of Finland, Estonia, Lithuania or another country. Workers have to be registered and must obtain work visas or residence permits giving them the right to work (registration is also required for short-term work). Unfortunately, this procedure is often omitted. As a result, the requirement on worker registration by the employer is not met, there are no social and economic guarantees and no legal working conditions, and the problem of illegal presence in the country arises (which may lead to the deportation of a migrant worker).

3. Exploitation of labour (of a migrant worker) based on a contract with no mention of social protection, or even without any employment contract at all (this form of employment is practised in agriculture and the construction industry). Example: a worker represents a sub-contractor (in construction work) and performs the work based on the contract for rendering services or a sub-contract (for a 1-2 month term) (Estonia and Poland).

4. The lack of legal awareness regarding payment of contributions to the social security fund in a host country. Example: only 300 000 Ukrainians out of 900 000 pay contributions to the social security fund in Poland.

**Ukraine has signed bilateral international treaties regulating social protection relations with the EU member states including Bulgaria, Estonia, Spain, Latvia, Lithuania, Portugal, Poland, Slovakia, Hungary and the Czech Republic.**

Treaties with the EU Member States on social and pension protection aim to make employment legal and cover the issues of mandatory social protection as well as workplace accidents, occupational disease, emergency and temporary disability insurance.

**As regards workers' employment, Ukraine has signed the treaties with Poland, Spain, Lithuania, and Portugal.**

These treaties cover employment procedures including the issues of seasonal work, candidate requirements and selection, conditions of employment agreements, etc.

Unfortunately, the employment treaties are not widely implemented since they have not accounted for labour market dynamics in the countries in question, although they are extremely important for Ukrainian migrant workers as regards their protection.

We note that Ukraine has not signed treaties with all countries where Ukrainian citizens work. Besides, loopholes in Ukraine's own legislation narrow the scope of their coverage. Moreover, since illegal employment is widespread among Ukrainian migrant workers, social protection does not apply to many of them even in those countries which have signed treaties.

In order to solve these problems, one should focus on the issue of trans-border cooperation with the EU Member States, especially as regards raising the awareness of migrant workers and citizens who plan to work abroad.

In order to improve the economic and social conditions of Ukrainian migrant workers, including construction workers, one should establish and deepen cooperation between various types of public institutions, including NGOs alongside governmental bodies, in both local and trans-border contexts.

# Impact of labour market conditions and the level of wages on labour migration: employers' perspective

A shrinking and aging population means that Ukraine's labour potential is rapidly deteriorating. Compared to 1991, Ukraine's population (including inhabitants of temporarily occupied territories and the annexed region of Crimea) decreased from 51.9 to 42.4 million. In 2017, there were 100 deaths per 63 births and the population decreased by 198 100. At the same time, employers are deeply worried[[33]](#footnote-33) by the labour outflow. Currently, over 80% of Ukrainian migrant workers aged 30-44 years old working in the EU Member States are employed in Poland (over 1.5 million), while other countries have doubled their quotas for Ukrainian guest-workers, as is the case with the Czech Republic.

Employers argue that the State's policy needs urgent changes. The Federation of Employers of Ukraine notes that at present there are no adequate steps being taken to preserve the labour potential. This refers to creating attractive conditions for investments in Ukraine's economy and, correspondingly, creation of new jobs, development of professional education, etc. The Joint Representative Body (JRB) of employers is planning to raise this issue at the special meeting of the National Tripartite Social and Economic Council in April 2018. It is anticipated that normative legal acts will be drafted, which will have to be considered at the Cabinet of Ministers' special meeting on the preservation and enhancing of labour potential initiated by domestic employers.

While the JRB of employers does not directly equate the labour migration problem with low wages in Ukraine, the construction industry sector association (Confederation of Builders of Ukraine - CBU) explicitly links these two problems.

Today, labour migration is considered a major new problem in Ukraine. Many Ukrainian construction companies face a shortage of high-skilled professionals. CBU member companies openly recognise that there are more vacancies open than job seekers as well as the growing labour turnover, which they "have not seen before"[[34]](#footnote-34).

Apparently, Ukrainians improve the labour market situation in European countries. Entire crews of construction workers move abroad to work. Most then return home but, as a rule, at least one of then remains permanently in the host country.

Foreign companies are actively expanding and cannot fully satisfy their demand for personnel in the sectors such as construction or agriculture. They used to seek highly experienced and qualified workers, but now they take everyone and, if necessary, arrange their training, provide accommodation, assist with registration, etc. The deputy head of the executive board of the Confederation of Builders of Ukraine and chairman of the Altis-Holding Corporation supervisory board, Oleksandr Glimbovskyi, notes that "according to various estimates, there are over a million registered Ukrainians in Poland and another half a million (and perhaps more) stay there unofficially. The Czech Republic is going to double its annual quotas for Ukrainian workers. This can pose a serious risk for economic growth in Ukraine and for stability of the construction industry in the coming years".

Poland is attractive for Ukrainian workers because of the wage difference. On average they are paid PLN 3 500 (roughly USD 1 046). Understanding the risk of losing human resources, the Ministry of Regional Development and Municipal Economies has raised the recommended pay rate for 2018 compared to that of 2017[[35]](#footnote-35).

At the same time, leaders of the sector's business association note that raising wages by several percent cannot solve the problem. A dramatic, multiple wage increase is needed. "Perhaps this would be an attractive condition for some of Ukrainian construction workers" – Yurii Serbin, vice-president of the CBU comments – "but it would hardly solve the critical situation with labour migration since we have neither a comprehensive strategy nor a cohesive migration policy, nor ideas on how to reduce the outflow of labour from Ukraine. Raising salaries by UAH 1 000 – 2 000 will not keep skilled workers from migrating. Some companies had to raise wages up to 70 percent in order to keep people working here and discourage them from moving abroad".

Labour migration is a problem for all countries that start working with developed economies. For instance, Polish construction workers who look for higher wages move to Germany, Lithuanian ones to Germany and Norway, while Ukrainian workers head for Poland and Lithuania.

"In order to keep labour in the country, one needs the average salary for a construction worker to be at the level of UAH 15-16 000", according to Yurii Serbin.

# Predicted outcome of a "no active wage reform in Ukraine" scenario

In the event of there being no change to remuneration policy, all the negative social and economic trends in the country will continue to get worse.

1. The State policy on fixing the subsistence minimum and the minimum wage (based only on budget considerations, without taking into account workers' needs and the actual cost of the consumer goods basket and, at the same time, violating the principles of social dialogue and ignoring the trade unions' position during collective negotiations on the minimum wage and changes to the legislation) defers increases to the guaranteed minimum wage and, therefore, does not lead to real earnings growth that is tangible to workers.

Artificially low subsistence minimum and wages in the non-public sector results in low minimum guarantees and a low basis for payroll accounting and reduced additional payments, bonuses and other forms of compensation, while in the public sector it leads to the lower quality services (state administration, education, healthcare etc.). Inefficient collective agreement regulation results in imbalances and a deterioration in sectoral and collective agreements and a decline in productivity and market competitiveness.

2. Growing wage disparities between the highest and lowest paid workers makes for **persistence of large-scale poverty** and its substantial (three to five-fold) subjective exaggeration. This poses a major risk to social stability and causes total mistrust in the government. Income inequality causes massive macroeconomic instability, narrows the potential for economic growth, fuels more widespread corruption, lowers guarantees for high-skilled workers and makes the poorer groups in the population even more vulnerable[[36]](#footnote-36)..

3. **Wage arrears** – considering the trends in 2017 – may get close to UAH 3 billion by the end of 2018 and almost 150 000 workers of economically active companies will remain unpaid.

4. **Growing forced outward labour migration**: the outflow of high-skilled and educated workers abroad will increase the risk of losing human capital and a qualified labour pool for employers. According to the *Economist Intelligence* forecasts, Ukraine is among the top five countries of the world to lose the most labour force in the long term, up to 2050[[37]](#footnote-37).

5. Deepening problems with state revenues and local budgets as well as of state social funds, together with the growing deficit of the Pension Fund of Ukraine, will lead to a funding shortfall for public sector employees wages, a deterioration in social security for the most vulnerable population, including pensioners and people with disabilities, as well as for a lack of funds for settling arrears on domestic and international liabilities.

6. **Growing corruption and shadow economy**, problems that are typical of cheap labour economies, significantly reduce the effectiveness of macroeconomic regulation, worsen the investment climate, lower the competitiveness of the economy and result in an even larger part of the population sliding below the poverty line[[38]](#footnote-38),[[39]](#footnote-39).

To sum up, a level of wages that is insufficient for workers' survival, chronic wage arrears and the gradual deepening of unreasonable wage disparities contrasted by rising goods and utility prices and the cancellation of state regulation of food prices[[40]](#footnote-40) make for spreading poverty in the working population, a decline in its purchasing power and a growing shortage of skilled labour, thus threatening the country's potential for social and economic development and security[[41]](#footnote-41).

# Proposals for a comprehensive remuneration reform

Comprehensive remuneration reform makes provision for changes to be made in the current legislation and regulations.

We propose to solve the problems of remuneration by making amendments to legislation and regulations on the following issues:

1. Changing the methodology for fixing the subsistence minimum, namely its calculation based on updated sets of food, non-food goods and services[[42]](#footnote-42) in accordance with the *ILO Social Policy (Basic Aims and Standards) Convention No.117*, which recommends taking into account expenses for purchase or rent of accommodation, healthcare services and education. This will contribute to reducing poverty.

2. Changing the mechanism of defining the minimum wage structure, namely making the provision that the minimum wage is a payment for simple, non-qualified work that does not include additional payments and compensations to account for family conditions in accordance with Article 4 of the *European Social Charter (Revised)*, *ILO* *Minimum Wage Fixing Convention No. 131* *with Special Reference to Developing Countries* and *ILO Minimum Wage Fixing Recommendation No. 135**with Special Reference to Developing Countries*[[43]](#footnote-43). This will help to ensure sufficient living standards for workers and their families.

3. Changing the Unified Wage Tariff System for the public sector by optimising the number of wage tariff categories and simultaneously raising the coefficient range taking into account sectoral specifics. This will help to ensure fair wage differentiation with regard to position and qualifications.

4. Reducing the large wage gap between enterprise leadership and workers by fixing reasonable inter-position coefficients that will help to reduce disparities.

5. Strengthening workers' protection with regard to timely wage payment and settlement of arrears by making these priority payments and establishing a guarantee institution for guaranteeing employees' claims in the event of employer insolvency.

6. Ensuring sufficient level of wages for low-paid workers by introducing a non-taxable income equal to the subsistence minimum for the working population calculated by the new methodology in line with the *ILO Social Policy (Basic Aims and Standards) Convention No. 117,* as well as by introducing a progressive tax scale (lowering the tax rate for low-paid workers and increasing it for high-paid ones).

7. A separate proposal from the trade unions – a proposal which does not enjoy support on the part of employers – aiming to protect workers' income, in the event of inflation, by raising the level of income that is subject to indexation up to the size of two subsistence minimums (calculated by the new methodology in line with the *ILO Social Policy (Basic Aims and Standards) Convention No. 117*)for the working-age population, along with a simultaneous limitation on the maximum income that can be indexed (for instance, up to 25 subsistence minimums for the working-age population).

8. Strengthening collective agreement regulation.

9. Ensuring workers' right to strike in accordance with international standards (Article 6 of the European Social Charter (Revised)) for meaningful collective agreement regulation of wages, and as a means to promote their employment rights.

# Impact of remuneration reform on major stakeholders

The proposed strands of remuneration reform will have different effects depending on the different stakeholder groups.

Considering the current low level of remuneration and significant wage arrears, the major stakeholders of the reform are 10 million employees, one fifth of whom (20.1%) are living below the poverty line[[44]](#footnote-44), while hundreds of thousands have not received their due payments.

Raising wages will:

- boost consumer demand and improve of consumer sentiments. According to the NBU, the twofold increase in the minimum wage from 1 January 2017 increased the nominal income of the population (up to 20.2% in the 3rd quarter of 2017 compared to the same period of the previous year), which, among other things, raised consumer demand and increased real GDP over the first nine months of 2017 by 2.3 % compared to the same period of the previous year[[45]](#footnote-45);

- ensure growth of tax and deduction revenues at all levels, as well as the Pension Fund and social insurance funds. According to expert evaluations, almost half of each hryvna from increased wages returns to the State Budget through income tax, VAT, excise levies, etc.[[46]](#footnote-46). According to the State Fiscal Service of Ukraine, budget revenues from income tax and deductions in 2017 increased by 25.5% (+ UAH 15.2 billion) compared to 2016; revenues from the unified social tax grew by UAH 49.0 billion[[47]](#footnote-47);

- contribute to unshadowing of the economy. According to the Ukrainian Minister of Social Policy, A. Reva, nearly UAH 200 billion of wages remain in the shadow economy. Reducing the shadow economy's size from 40% to 30% will increase the economic growth rate by 13%[[48]](#footnote-48). According to expert evaluations, if in 2014 the nominal monthly salary had grown to UAH 5 150, the shadow part of the economy would have accounted for only 15.4% (close to that of the economically developed EU Member States). If the nominal salary were increased to UAH 6 050 and the proportion of remuneration as a part of total production costs were to come close to its optimal value of 0.382, then the shadow economy would, in theory, not exist [[49]](#footnote-49);

- contribute to reducing the deficit of the Pension Fund of Ukraine and generating extra funds for increasing pensions to 12 million pensioners, reducing the number of utility subsidy recipients (6.3 million households or 41% of all households in the country[[50]](#footnote-50)) as well as recipients of targeted social assistance (nearly 3 million people receive one or several kinds of social assistance[[51]](#footnote-51)), and contribute to reducing utility payment arrears (UAH 36.9 billion at the end of January 2018[[52]](#footnote-52)).

Increased population income will also have a positive effect on the banking sector: growing monetary deposits will help banks to recover a fully-fledged consumer loan market, especially in the area of mortgages, and to accumulate the lending funds needed by the economy.

Socially responsible businesses also are stakeholders in any increase in remuneration. Employers are ready to raise wages in order to curb migration of highly-skilled professionals and support domestic demand. At present, the necessary conditions for wage increases, according to businesses, include economic recovery and a lower tax burden[[53]](#footnote-53). Businesses possess certain financial resources allowing for wage increases for their employees.

Cutting the unified social tax twofold in 2016 allowed employers to save, since instead of the expected "unshadowing" of the labour market, the unified social tax revenues (budget income) decreased[[54]](#footnote-54). A mandatory increase in the labour cost will prompt employers to rationalise and modernise production, implement the latest technologies, optimise non-production expenditures and upgrade their personnel, all of which will enhance the competitiveness of national producers.

However, not all employers support increasing wages for employees, since this will result in a parallel increase in tax and deduction expenses, prices rises and a reduction in current assets and investment opportunities, thereby lowering competitiveness.

Problems may arise for entrepreneurs paying the single tax, since the size of this tax and the unified social tax are directly linked to the minimum wage. Thus raising the latter may force them to either close their businesses or move them into the shadow economy. Therefore, one will need to negotiate the single tax and the unified social tax rates for this category of entrepreneurs.

The true risks of wage increases may include growing inflation and unemployment, encouraging the spread of part-time or unofficial employment.

Experts predicted that extra inflation caused by the twofold increase in the minimum wage to UAH 3 200 from 1 January 2017 would stand at 2 percent points. They expected small businesses to be the hardest hit.

According to the NBU survey on business expectations in the 2nd quarter of 2017, businesses have gradually adapted to the increased labour costs. For instance, compared to the 1st quarter, businesses lowered their expectations for price growth in their products/services over the following 12 months. Among other things, it was also due to the lower impact of the increase in labour costs. Only 2% of survey participants said they were likely to close their businesses over the year. Among the latter, there was a larger share of small businesses (3.6% of responses)[[55]](#footnote-55).

According to the NBU, by the end of 2017, consumer prices in Ukraine had grown by 13.7%, exceeding the inflation forecast by 4.6 percentage points. The greatest contributor to the deviation from the forecast were fresh foods (due to the unfavourable weather conditions, there was an increase in meat and dairy exports supported by growing global prices and lower domestic market supply) as well as growing production costs including labour expenses, rapid recovery of consumer demand and growing prices for services[[56]](#footnote-56).

# Implementation mechanism for the comprehensive remuneration reform

Implementation of the comprehensive remuneration reform requires the following steps to be taken:

1. Central executive bodies (CEBs), with the participation of the social partners and academic experts, develop draft legislation and ordinances of the CMU on the issues which, when solved, will ensure the increase of workers' earnings and purchasing power. The draft legislative acts, their contents and the key participants are listed in Table 1.2.

2. Ministries and other CEBs, the key authors of the draft legislative acts and the CMU ordinances, arrange legislative and regulatory acts approval procedures involving trade union and employers representatives, in accordance with the General Agreement, the Law of Ukraine *On the Social Dialogue in Ukraine*, the working procedures of the CMU approved by the Ordinance of the CMU of 18 July 2007 No. 950 (with changes), as well as the Regulation on state registration of the legislative and regulatory acts of the ministries and other executive bodies approved by the Ordinance of the CMU of 28 December 1992 No. 731 (with amendments).

3. Ministries and other CEBs, the key authors of the draft legislative acts and CMU ordinances, forward them to the CMU.

4. The CMU:

* approves draft legislative acts and submits those to the Verkhovna Rada (parliament) of Ukraine (VRU);
* passes the ordinances of the CMU.

5. The President of Ukraine submits the Draft Laws of Ukraine *On Ratification of Paragraph 1 of Article 4 and Article 25 of the European Social Charter (revised)* as well as *On Ratification of Part III of the International Labour Organization Protection of Workers' Claims (Employer's Insolvency)**Convention No. 173 of 1992.*

6. The VRU passes the afore-mentioned draft legislative acts and submits these to be signed by the President of Ukraine.

7. The CMU ensures full compliance with the requirements and guarantees of the current legislation and normative and regulatory acts on remuneration.

8. The parties to the Social Dialogue in Ukraine ensure at all levels:

* implementation of the norms of the General Agreement, sectoral, cross-sectoral and territorial agreements, as well as collective agreements;
* completion of negotiations on setting the minimum pay rate for employees of Category I of the non-public sector;
* negotiation of the General Agreement for the new term, taking into account the need to raise wages at a faster rate (according to the employers' position – at the rate of GDP growth) in order to meet international obligations to reach European standards of living in Ukraine.

9. The Ministry of Social Policy of Ukraine arranges negotiations on:

* fixing the minimum wage;
* fixing the official salary for employees of Category I in the unified tariff system;
* fixing the minimum pay rate for employees of the Category I in the non-public sectors in the General Agreement.

10. Local government bodies budget for sufficient funds for the remuneration of public sector and public utility companies' employees.

11. The State Employment Service of Ukraine monitors implementation of the legislation and normative and regulatory acts' requirements by employers as regards remuneration.

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