

Aleksander Surdej Ph.D.
Krakow University of Economics

Managing Labor Market Reforms: Case Study of Poland

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Abstract

When state socialism collapsed in Poland in 1989, the Polish society nurtured great hopes to rapidly establish well functioning democracy and efficient markets. This paper describes the labor market reforms in Poland since 1989 and labor market changes throughout the country's economic transformation. The gravity of the situation on the Polish labor market, with high unemployment rate, has been recognized by both the EU and the OECD. The paper concludes that labor law reforms have been eased by the fact that the public opinion in Poland was favorable to deregulation; partially due to the perception that such changes would be advantageous to the society, and partially because no credible alternative existed. Polish mass media did overwhelmingly support labor law reforms and there were no voices calling for an alternative (for instance an interventionist approach) approach to try to reduce unemployment. The upcoming membership in the EU created favorable conditions for deregulatory changes.

The views expressed are those of the author and do not necessarily reflect official views of the World Bank.

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I. Introduction

When state socialism collapsed in Poland in 1989, the Polish society nurtured great hopes to rapidly establish a well-functioning democracy and efficient markets. The first democratically legitimized Polish government formed in September 1989. It needed to act rapidly and with resolution in order to confront an economic crisis, and simultaneously implement market economic reforms.

Basic ideas about how to transform a socialist economy into a market economy were derived from mainstream textbook economics and known as the so-called *Washington consensus*.¹ The main components of such transformation policies included price liberalization, macroeconomic stabilization —through tight monetary policy—, and the privatization of state owned firms.² Polish reformers decided to implement these economic reforms at a great pace. This approach is known as a shock therapy as opposed to the policies of gradual economic transformations.

Initially the policies of economic transformation led to a dramatic fall in GDP (1990-92) and rising unemployment.³ Macroeconomic stabilization was difficult to achieve due to the fall in public revenues, strong pressure of state owned companies to continue their subsidization, and rising social expenditures on pensions, unemployment benefits and social assistance. Furthermore, privatization in Poland has been slow as the mass privatization scheme was only implemented to a limited extend.

The changes in Poland and in other East European states have been called dual transition, since political and economic systems changed simultaneously.⁴ This fact meant that the scope and degree of change was

¹ Williamson, J. (1990). What Washington Means by Policy Reform. In John Williamson (Ed.), *Latin American Adjustment: How Much Has Happened*. Washington D.C.: Institute for International Economics.

² Blanchard, O., Dornbusch, R., Krugman, P., Layard, R. and Summers, L.(1991) *Reform in Eastern Europe*, Cambridge: MIT Press.

³ Kornai, J. (1993) Transformational Recession: A General Phenomenon Examined through the Example of Hungary's Development, in *Economie Appliquée* 46 (2): 181-227.

⁴ Przeworski, A.(1991),*Democracy and the Market*, Cambridge: Cambridge UP.

much wider than in all previous democratic transitions such as those that took place in Latin America.⁵

Economic transformations in Poland consisted of two elements: economic restructuring, typically the social economy was characterized by large and inefficient state owned enterprises, misallocation of labor and distorted prices), and institutional changes, the first of such changes was re-establishment of private property and of the system of its legal protection. Policy makers seemed initially (1990-95) preoccupied with privatization and economic restructuring and only later (in the late 1990s) they perceived the importance of institutional and regulatory changes.

Political transformations in Poland proved equally difficult. Although it took a few weeks to run free elections, to overhaul the functioning of public institutions (including the state administration) has taken years and this process is still far from being completed.

Economic policies in Poland were designed and implemented amidst great uncertainty about the underlying causes of economic problems they were supposed to solve. This uncertainty stemmed from the necessity to manage many shocks that have affected the post-communist economy: from endogenous shocks induced by domestic policy choices to external shocks due to growing economic openness.

II. Selected Dimensions of Economic Restructuring

It needs to be stressed that post-communist economic reforms have set in motion deep structural changes in the economy. Some aspects of these changes will be briefly presented.

II.A Privatization: Growth of Small Firms and Large Scale Privatization with Foreign Participation

During the 14 years of post-communist transformations the private sector has become the dominant sector of the Polish economy. The share

⁵ Balcerowicz, L. (1994), Understanding Post Communist Transitions, in *Journal of Democracy* 5(4): 75-89.

of the private sector in the economy as measured in relation to Poland's GDP increased from 30% in 1989 to more than 76.9% in 2002.⁶

At the end of 2000, the share of the private sector in industrial output was 46.9%; in construction 95.8%, in transportation 59.3%, and in domestic trade 95.1%. The share of the private sector in exports rose from less than 10% at the end of the 1980s, to 83.6% in 2001. Altogether, the private sector employed 73.7% of the workforce at the end of 2000.⁷

This impressive shift in the proportion between public and private property has happened chiefly thanks to the explosion of newly founded private firms, mostly of small and medium size. In contrast, the privatization of existing state owned companies, especially of the large ones, proved to be difficult from the social and political point of view.

Despite these difficulties one can say that the privatization process of the state owned sector has trespassed the critical point, and the share of the public sector in the economy has been dramatically reduced.⁸

IIB. Size Distribution of Polish Enterprises

The Polish economy is dominated by small and medium sized enterprises: in the end of 2001 there were 3.375m enterprises registered, of which 3.206m employed less than 10 workers (that is 95%), 0.131m between 10 and 49 workers (3.9%), 0.031 between 50 and 249 workers (0.1%) and 6589 more than 250 workers (0.02%).⁹ There is a strong correlation between the size of enterprise and its private/public status. The share of remaining state owned enterprises grows rapidly with the size of the enterprise.

⁶ Statistical Yearbook, GUS, 2003, p: 581.

⁷ Statistical Yearbook, GUS, 2001.

⁸ In the end of 2002 there were 1951 state owned enterprises, which privatization has proved to be difficult chiefly because these are technologically obsolete units or enterprises operating in declining sectors of the economy - see Statistical Yearbook, GUS, 2003, p: 612]

⁹ The Polish Agency for Enterprise Development (<http://www.parp.gov.pl/statlatami2001.php> - accessed 8 February 2004).

IIC. Sectoral Changes of Employment

The economic restructuring has generated significant displacement on the labor market. The sectoral changes in the employment structure (see the table below) can be treated as a good measure of these displacements.

Table 1

Changes in employment structure

	1992	1999	2005 (forecasted)
Mining	3.1	1.6	1.0
Agriculture and forestry	33.8	27.5	26.4
Manufacturing	22.3	18.6	19.0
Construction	6.2	5.8	5.4
Services	34.6	46.5	48.2
Total employment	100	100	100

Source: Czyzewski, A.B., Orłowski, W. M., Zienkowski, L., *Economic development of Poland in the period of 1992-2005: verification of the forecast* (mimeo) 2002.

The data show that employment changes were relatively slowest in agriculture, where they have been most needed, and fastest in services (due to the fast expansion of this sector of the Polish economy).

Large structural changes have led to the massive dislocation of the labor force. As a rule, the labor force shed in contracting sectors goes into economic inactivity (unemployment, pre-retirement, retirement or withdrawal from the labor market) or moves to expanding sectors. When economic restructuring generates labor displacement, the flexibility of the labor market is of crucial importance for the speed of the adjustments. This is illustrated by the size and average duration of unemployment.

III. The Development of the Polish Labor Market Since 1990

The labor market changes in Poland throughout the 1990s can be divided into four sub-periods. The first period comprises the years 1990-

1991 and is characterized by a dramatic rise of unemployment. The second period (the years 1992-1993) was characterized by a slower rise of unemployment, followed in the third period, covering the year 1994-1997, by a gradual reduction of unemployment). Again, in the years 1998-2003, the Polish economy witnessed an increase in unemployment.¹⁰

The gravity of the situation on the Polish labor market has been recognized by both the EU and the OECD. Thus, the European Union's "*Comprehensive monitoring report on Poland's preparations for membership*" of October 2003 indicates unemployment as a key economic policy issue for Poland pointing to both high unemployment (almost 20% in 2002) and a low employment rate (51.5% in 2002).¹¹ Besides the general evaluation of the situation on the Polish labor market the European Commission has noticed that "Poland's Labor Code is only partially aligned with the *acquis* on labor law, and completion of transposition must be prioritized. Legislative alignment still needs to be completed in the fields of working time (including sectoral working time), part-time work, transfer of undertakings and posting of workers." [op. cit. p. 39]. The transposition of the *acquis communautaire* in the Polish labor law had to be completed before Poland formally joins the European Union (foreseen for May 1, 2004) and such changes were introduced in the November 2003 law.

The 2002 OECD Report "*Poland: From Transition to New Regulatory Challenges*" notices high unemployment in Poland and goes further pointing to the "structural factors" behind high unemployment. This includes labor market rigidities such as "high labor taxes, a regionally non-differentiated minimum wage, regulatory obstacles to the renewal of fixed-term contracts, and mismatches between skills offered and required"

¹⁰ E. Kwiatkowski, L. Kucharski(2003)Analiza strumieniowa bezrobocia w Polsce w okresie transformacji, in *Rynki pracy*, nr 3-4.

¹¹ The European Union influences the labour market policies of candidate countries by doing in 2001 a *Joint Assessment of the Employment Policy Priorities* whose implementation has been controlled by subsequent various progress reports.

[p.25]. The Report has called the Polish government to pursue labor market reforms that would tackle these problems.¹²

It is important to notice that high unemployment in Poland ceased to be explained as so-called “transformatory unemployment”.¹³ This is unemployment stemming from the transition from the command economy to the market economy. It is now analyzed as par excellence structural unemployment. The notion of the structural causes of unemployment encompasses a variety of factors starting from the level and duration of unemployment benefits, and ending with labor law regulation regarding employees’ hiring and firing.

Table 2

Unemployment rate in Poland, 1996-2002 (as a percentage of the total labor force)

Country	1996	1997	1998	1999	2000	2001	2002
Poland	12.3	10.9	10.2	13.4	16.4	18.5	19.9
Hungary	9.6	9.0	8.4	6.9	6.3	5.6	5.6
Czech R.	3.9	4.8	6.4	8.6	8.7	8.0	7.3
Slovakia	11.3	11.9	12.6	16.8	18.7	19.4	18.6
EU	10.2	10.0	9.4	8.7	7.8	7.4	7.6
OECD	7.2	7.0	6.9	6.7	6.3	6.5	6.9

Source: *OECD Employment Outlook 2003*, p. 299

Accordingly, one could observe the change of labor market policies which served to address labor market problems. In the early 1990s the government policy used to encourage pre-retirement as a solution to the

¹² OECD(2002)*Poland: From Transition to New Regulatory Challenges*, Paris.

¹³ The transformatory unemployment does result from the systemic transformation of the Polish economy and consists chiefly of labour shedding in previously overmanned state enterprises [see: Mieczyslaw Socha, Urszula Sztanderska, *Strukturalne podstawy bezrobocia w Polsce* [Structural Basis of Unemployment in Poland], PWN, Warszawa, 2002, p: 69] Transformatory unemployment can be treated as a kind of frictional unemployment, that is a temporary unemployment due to employment rationalization in former state owned enterprises now undergoing privatization and restructuring.

growing unemployment. Older employees from closed factories were sent on pre-retirement to avoid rising the number of unemployed. As a result, the average retirement age in Poland is 57 years for men and 55 for women, instead of the statutory retirement age of 60 and 65 years respectively.¹⁴ Polish retirees are thus relatively young and in principle able to work or to get involved in social activities. However, the subsequent governments propagated the economic fallacy that there exists a lump sum of jobs in the economy, so by sending the elderly on retirement, jobs are freed for the young.

Table 3

Older workers follow multiple pathways out of the labor market

(Labor force status of persons aged 50 to 64 years and reasons for being inactive, 2000, percentages)

Country	Active			Inactive					
	Employed	Unemployed	Total	No work available	Retired	Illness, disability	Family duties	Other	Total
Poland	43.3	4.6	48.0	2.5	15.7	22.3	4.8	6.7	52.0
Hungary	39.1	1.6	40.6	1.8	47.2	6.5	0.8	3.2	59.4
Czech R.	54.8	3.6	58.4	0.3	31.5	8.7	0.6	0.6	41.6
Slovakia	40.5	6.1	46.6	0.3	50.4	1.5	0.8	0.3	53.4
Norway	72.8	0.9	73.7	-	-	-	-	-	26.3
Finland	58.4	5.0	63.4	2.0	12.3	15.9	1.3	5.1	36.6
Germany	48.6	6.0	54.6	0.4	28.7	4.1	5.0	7.1	45.4
OECD	50.6	3.4	54.1	1.3	16.9	6.6	8.5	6.2	45.9

Source: *OECD Employment Outlook 2003*, p. 85

One of perverse of policies encouraging pre-retirement and early retirement was the increase of social contributions. Contributions to social insurance and unemployment insurance amount to approx. 39% of

¹⁴ See: M. J. G. Cain; A. Surdej, *Facing the Pension Crisis: Current Problems and Future Perils in the Polish Pension System*, in *Emergo*, nr 2/1996.

salaries –the percentage is calculated in relation to the remuneration after contribution deduction– (see table 4).

The rate of pension (both retirement and disability) contributions was growing over time in Poland: from 15.5% between 1951 and 1980, to 25% in 1981, 43% in 1986 and 45% in 1992. The 1999 reform of the pension system altered the organisational structure of the system by introducing the second (mandatory) and the third (optional) pillars, which function according to the financial principle of capitalisation via specialised investment funds.

The 1999 change did not however reduce the rate of pension contributions, but it has established a visible relationship between the contribution paid and the benefits received. An employee receives an information about the amount of contributions paid by him and by employer to the pension fund. It has also introduced the principle of contribution sharing between an employee and an employer.

What was the impact of these changes on the incentive to work in the shadow economy? It is obvious that in a difficult labor market situation an employee faces a trade off between being employed legally and accumulating contributions for her future pension and not being employed at all.

Table 4

Contributions to social insurance, unemployment insurance and health insurance as of end 2002

Type of insurance	Contribution rate	Of which percentage rate paid by	
		Employer	Employee
Old age	19.52	9.76	9.76
Of which: first pillar	11.22		
Second pillar	7.30		
Demographic reserve	1.0		
Pensions (disability, survival and funeral grants)	13.0	6.5	6.5

Sickness	2.45	--	2.45
Work injury	1.62	1.62	--
Total	36.59	17.88	18.71
Unemployment	2.45		2.45
Health insurance	7.75		7.75

Source: ZUS (Social Security Office), 2003.

In parallel to the move to the market economy, the Polish government introduced an unemployment insurance, which throughout the 1990 amounted to approx. 2% of gross salary. The contributions were managed by the Labor Fund, which has paid out unemployment benefits and financed various forms of labor market programmes. The rise of unemployment made the Labor Fund to spend as much as 65-75% of its resources on unemployment benefits.

But, despite such a large share of spending on unemployment benefits, a significant share of the unemployed is not entitled to the unemployment benefits, as they stay unemployed for long time periods (over 12 months). In the end of 2001 the share of long-term unemployed—those searching jobs for longer than 12 months— amounted to 48.3% of the total number of unemployed.¹⁵

In late 2002, there were more than 1.6 million long-term unemployed people, an increase of almost 140,000 since late 2001. Long-term unemployment was thus increasing at a rate three times greater than unemployment as a whole. People without paid employment for more than 12 months accounted for 51% of registered unemployment, a proportion that had increased by almost 3% points since the end of 2001. Furthermore, the number of unemployed people without jobs for more than 24 month rose in 2002 by almost 146,000 (up 17%).

The combination of pre-retirement policy and the growth of long-term unemployment has shown that discouraging people from labor market participation does not solve the problem of unemployment and results chiefly in the growth of social expenditures.

¹⁵ GUS, *Statistical Yearbook*, 2003, p: 153.

During the 1990s the share of social spending in GDP amounted to approx. 33-35%, and was thus similar to the level of social expenditures in West European countries such as Belgium, Denmark, or the Netherlands. The bulk of social spending (approx. 50% of all social expenditures) goes for pensions and retirement schemes (social security system).¹⁶ As the table below shows throughout the 1990s expenditures on pensions were crowding out other social expenditures.

Table 5

Share of total social expenditures (and selected issue spending) in GDP (as %)

	1990	1991	1992	1993	1994	1995	1996	1997	1998
Social welfare expenditures	25.2	32.1	32.3	31.2	33.3	32.0	33.5	33.2	31.2
Pension expenditures	8.6	12.6	14.6	14.2	15.8	15.6	15.2	14.6	14.1
Family policy	1.8	2.5	2.4	1.7	1.7	1.3	1.3	1.4	1.3
Social assistance	1.5	0.7	0.9	0.9	1.3	1.3	1.4	1.4	1.4

Source: Golinowska, S., *Państwo opiekuńcze w Polsce*, Polityka społeczna, vol.1, Warszawa, Styczeń 1998, p. 4. and Golinowska, S., J. Hausner, *Ekonomia polityczna reformy emerytalnej*, CASE Reports no. 15, 1998, p. 34, and Golinowska, S., *Polityka społeczna: koncepcje-instytucje-koszty*, Warszawa, 2000, p.23.

There is a threat that pension expenditures cannot but further increase with the ageing of the Polish society.¹⁷

A high level of social expenditures (relative to the level of GDP per capita) has led to a high level of taxes and social contributions that all employees have to pay. High taxes and social contributions have increased a gap between the wages employees receive and the labor costs

¹⁶ Golinowska, S., *Państwo opiekuńcze w Polsce*, in Polityka społeczna, vol.1, Warszawa, Styczeń 1998, pp.1-4.

¹⁷ - The anticipation of the collapse of the social security system was the principal reason behind the pension reform introduced in 1999.

for employers. Prominent Polish economists, like Marek Gora, point to the fact high labor costs and not high wages are the main cause of high unemployment—i.e. low demand for labor—in Poland and the government’s policy should aim at reducing them.¹⁸

One of peculiarities of postcommunist economies, including the Polish economy, is a large informal economy propelled by high taxes, and in turn causing high taxes needed to finance public spending. Kaufmann and Kaliberda estimate that:

„Till the mid 1990s, 1/3 of the former Soviet countries economic activity originated from the informal economy. By comparison in Central and Eastern Europe the average amounted to ¼. Intra-regional variance is large, with some countries having 10–15% of their economy engaged in informal (unofficial) activity while others exceed 50%.“¹⁹

Other authors, for instance Lacko, estimate that the share of the hidden economy in Poland oscillates between one third and one quarter of GDP.

Table 6

The share of the hidden economy (in % of total GDP) in selected transition countries in 1990-1995²⁰

Country	1990	1991	1992	1993	1994	1995
Poland	32.0	33.0	32.0	31.0	28.0	24.0
Czech	Nd	Nd	Nd	27.0	25.0	22.0

¹⁸ M. Gora, Innego wyjścia nie ma (No other solution exists), in Rzeczpospolita, 13 January 2004.

¹⁹ Kaufmann D., and A. Kaliberda, *Integrating the unofficial economy into dynamics of post-socialist economies*, in B.Kamiński (ed.), *Economic Transition in Russia and the Newly Independent States*, Armonk, NY: M.E. Sharpe, 1996a & Kaufmann, D. and A.Kaliberda, *Integrating the unofficial economy into dynamics of post-socialist economies: A framework for analysis and research*, Harvard Institute for International Development, *Development Discussion Paper*, (1996b), no. 558.

²⁰ Lackó, M., *Hidden Economy – An Unknown Quantity? Comparative Analysis of Hidden Economies in Transition Countries in 1989-1995 in University of Linz Working Papers*, 1998a, no. 10.

Republic						
Hungary	26.0	31.0	33.0	34.0	31.0	33.0
Russia	Nd	Nd	38.0	36.0	39.0	39.0
Ukraine	Nd	Nd	Nd	37.0	47.0	55.0

Source: Lackó (1998a), pp. 51-54

A high share of shadow economy is positively correlated with a high share of informal employment in the Polish economy (see the table below).

Table 7

The share (in %) of the shadow economy in the sectors of the Polish economy in 2002

Sector	The share of hidden turnover	The share of illegally employed
Manufacturing	17.1	14.0
Construction	26.0	27.3
Retail and wholesale trade	21.3	18.7
Hotels and restaurants	13.8	15.8
Telecommunication, transport, and storage	20.9	22.2
Property market	16.0	15.8
Education	12.1	12.5
Health care	12.7	5.5
Total	20.2	18.6

Source: ASM The Centre for Market Research and Analyses for the Polish Confederation of Private Entrepreneurs, data taken from Szawałek, K., *Ostrożnie z wybielaniem. Raport specjalny: szara strefa*, in *Business Week - Edycja Polska*, 2003, no. 8 , p. 13

Note: „Hidden turnover” denotes the share of undeclared sales to total company’ sales.

High structural unemployment and large shadow economy are to certain extent interrelated, and it is plausible that both are propelled by too stringent labor law regulations.²¹

In the section below we look at certain indicators of labor law flexibility and related labor market phenomena.

The availability of part-time workers and the easiness to hire labor for fixed-term employment contracts are widely used indicators of the opportunities for business to hire flexible labor.

In Poland, part-time employment is regulated by the general rules regarding employment contracts, that is, the part-time employment contract can be for a definite or indefinite period and the right to holidays and severance pay are calculated in proportion to the rights granted to those in full employment.

The data in the table 8 show that the share of part-time employment in Poland was relatively stable throughout the 1990s oscillating around 10-11 percent.

Table 8

Share of people employed part-time by gender based on the BAEL data

In %	1992	1995	2000	2001
Total	10.7	10.5	11.2	10.8
Men	8.9	8.2	8.7	8.8
Women	12.9	13.3	14.2	13.2

Source: Poliwczak, I., *Zatrudnienie w niepełnym wymiarze czasu pracy (Part-time Employment)*, in *Polityka Społeczna*, vol. 7, July 2003.

The share of part-time employment in Poland is significantly lower than in those EU member states, which are characterized by most flexible labor regulations (like the Netherlands), but it does not differ much from

²¹ There are of course other factors that also favor the growth of the shadow economy like income taxes or social security contributions.

the share of part-time employment in countries with most rigid labor law regulations (see the table 9).

Table 9

Share of part-time employment in selected OECD countries in 1983-1996

	Men			Women		
	1990	1996	2002	1990	1996	2002
Netherlands	14.8	16.1	14.7	36.4	38.0	58.8
Belgium	2.0	3.0	6.0	25.9	30.5	32.4
Germany (*)	2.6	3.6	5.5	33.8	33.8	35.3
France	3.3	5.3	5.2	23.6	29.5	24.1
Italy	2.4	3.1	4.9	9.6	12.6	23.5
Denmark	10.4	10.8	10.3	38.4	34.5	23.0
Finland	4.8	--	7.5	10.6	--	14.8
Great Britain	5.3	--	8.9	39.5	--	40.1
USA	8.3	--	8.3	20.0	--	18.8
Czech R.(a)	--	1.7	1.4	--	5.6	4.9
Hungary (a)	--	2.1	1.7	--	5.1	4.3
Slovakia (a)	--	0.9	1.0	--	2.9	2.3
Poland (a)	--	9.8	7.5	--	19.2	16.7

Source: OECD, Employment Outlook, Paris July 1997 and 2003, table E.

* Till 1993 exclusively Federal Republic of Germany (a) first OECD data on the Czech R., Hungary, Slovakia and Poland refer to 1999.

The research shows that Polish employers would like to expand the use of part-time workers, when there is no continuous work at the company, and in regard to some particular job positions like lawyers, health and safety specialists etc. (see the table below).²²

²² Poliwczak, I., *Zatrudnienie w niepełnym wymiarze czasu pracy*, in *Polityka Społeczna*, vol. 7, lipiec 2003, pp.16-18.

Table 10

Share of companies willing to employ part-time (based on labor market surveys)

Part-time employment	In %		
	1997	2001	2003
Yes	57.6	66.3	63.6
No	42.4	33.7	36.4
Total	100	100	100

Source: Poliwczak, I., *Zatrudnienie w niepełnym wymiarze czasu pracy* (Part-time Employment), in *Polityka Społeczna*, vol. 7, July 2003.

It is likely that the share of part-time employment will grow in Poland, if remaining regulatory constraints are eliminated.

Until 1996 the Polish labor law did not limit the use of fixed-term contracts. During the works of the parliamentary commission for the labor law reform in the years 1994-1996 (see subsequent parts of this paper), the representatives of trade unions complained about the spread of fixed-term contracts that crowded out indefinite-term contracts. In 1996, the parliament introduced the rule that the third fixed-term employment contract concluded within a month after the termination of the second fixed-term contract becomes by law an indefinite-term contract. This rule was suspended in July 2002 for the period until Poland's entry into the European Union, which requires some restrictions on the use of fixed-term employment contracts.

Part-time work and fixed term contracts are not the only legal forms increasing the flexibility of employment. In 2003, approx. 0.5m people worked as temporary workers via private employment agencies, which take advantage of rules for job intermediation in the employment law. The temporary jobs were explicitly recognized by the Law dated July 9, 2003,

which sets rules for employing people via the temporary work agencies.²³ The Law requires the employees of temporary workers to them not worse than their stable employees and grants them the right to two days of paid vacation for each month worked. On the other hand, the Law lifts the restrictions regarding the rule of the third fixed-term employment contracts and it shortens the period of dismissal notice.

Besides these forms of employment in Poland there is a growing substitution of civil contracts for employment contracts. In such cases a person does the same job as a self-employed person. The main reason of such a substitution is the high cost of social security contributions, but labor law regulations also contribute to the spread of this phenomenon.

Another dimension of labor regulations refers to the employment conditions. Until 2003, working time was broadly regulated by setting the norm of weekly working time and the maximum of yearly overtime hours.

These rules were made more specific by the labor law modification from 14 November 2003, which implemented the European Union directive nr 93/104 from 23 November 1993 (later amended by the Directive 2000/34 from 22 June 2000).²⁴

In tune with the November 2003 amendment since January 2003 an employee will be guaranteed 11 non-interrupted hours of rest during the working day and 35 hours of non-interrupted weekly rest. Furthermore, the 2003 Labor Law introduced a limit of 48 hours of work per week, which means that the weekly overtime hours cannot exceed 8 hours. It might seem that this law change is very restrictive, but the law comprehensively lists types of enterprises (works and services) in which the working day and working week might be organized more flexibly.²⁵

In Poland the labor law requires that overtime is paid more than work within limits of the working week. Until November 2003 legal regulations required that every extra hour of work during festivities and

²³ See the Official Journal nr 166/2003, item 1608.

²⁴ The Official Journal, nr 213/2003, item 2081.

²⁵ Working Time in Poland according to the EU Standards, in *Rzeczpospolita*, 10 February 2004.

on Sundays was paid with 100 percent premium and the same premium was imposed on third and any further extra hour of work during ordinary days. In November 2003, these stringent rules were slightly relaxed as the premium for overtime during ordinary days was set to a flat rate of 50 percent.²⁶

To the restricting rules one can add the mandatory payments for work stoppages due to reasons not related with employees and the minimum wage requirement (the minimum wage is relatively generous if compared to other countries).²⁷

Table 11

Minimum wage in Poland

Year	Minimum wage (in PLN)	Average wage in the economy (in PLN)	Minimum wage as a percentage of average wage in the economy
1999	653,33	1697,12	38.5
2000	695,00	1923,81	36.1
2001	760,00	2061,85	36.9
2002	760,00	2154,00	35.3

Source: Ministry of Economy, Labor and Social Policy.

Labor law regulates several aspects of the termination of employment contracts. In the case of an indefinite-term employment contract the law requires a three-month dismissal period and a one-month

²⁶ These limitations were justified by hopes that the increase of costs of overtime will directly reduce the demand for them and indirectly increase demand for additional employees.

²⁷ In Poland the requirement of minimum wage is set in the art. 65 par. 4 of the Constitution from 1997. The minimum wage initially was set uniformly. In October 2002 minimum wage was temporarily (till the end of 2005) differentiated to facilitate the hiring of high school graduate. Thus, the minimum wage for a high school graduate is set at the level of 80% during the first year of employment and 90% during the second year of employment. Contrary to the government's plans the minimum wage has not been differentiated regionally.

severance pay. Separate regulation exists for collective dismissals, which gives employees a special three-month severance pay.

Furthermore, when an employer dismisses an employee (unless it is a group dismissal for economic reasons) it has to state in writing the reason for the dismissal and these reasons can be challenged by the dismissed employee in the labor court. If the court recognizes the employee's objections, the court can mandate rehiring the employee or to pay her dismissal compensation. These rules do not apply to fixed-term employment or to the use of temporary workers, which makes this kind of employment contract particularly attractive.

The World Bank Employment Law Index gives a useful synthetic picture of employment regulations in Poland and in other countries undergoing post-communist economic transformations (see the table below).²⁸

Table 12

Stringency of Labor Regulations (2003 Indices)

Labor Regulation Indices (2003)	Poland	The Czech R.	Hungary	Slovakia
Flexibility of Hiring Index	33	17	46	34
Conditions of Employment Index	92	63	92	89
Flexibility of Firing Index	39	27	23	60
Employment Laws Index	55	36	54	61

Source: <http://rru.worldbank.org/DoingBusiness/TopicReports/HiringAndFiringWorkers/>

Note: Index components are scored between 0 and 100, with 100 representing the highest level of regulation. The Employment Laws Index is the average of the first three indices, and varies from 0 to 100.

²⁸ For comprehensive description of methodology and results see: <http://rru.worldbank.org/DoingBusiness/TopicReports/HiringAndFiringWorkers/Default.aspx>

The employment regulations are less flexible in Poland than in the Czech Republic, but similar to Hungary and Slovakia. Among the four: the Czech Republic and Hungary have low (below 10 percent) unemployment rates, whereas Slovakia and Poland have unemployment rates around 18-19 percent.

The gravity of the labor market situation has not only been recognized by international organizations (like the OECD or the EU). Increasingly, the main political forces in Poland have been pointing to the importance of the labor market changes for the sustainable growth of the Polish economy. For instance, a 2000 document of the Council of Ministers, at that point composed of right wing parties, expressed concern about the underutilization of labor resources (page 57 and further). Among actions that the government planned to undertake to stimulate the utilization of labor force, the report named measures "to increase the dynamics and flexibility of the labor market" (p. 58), including "the rationalization of the labor law" [p. 59] and "the introduction of such legislative measures, which would stimulate job search activities of the unemployed and shorten the duration of unemployment including the diversification of unemployment benefits depending on the duration of being unemployed and the region."²⁹

The changes in the employment law were also announced in the economic program of the left-wing coalition, which won the elections in September 2001.³⁰ At the beginning of the 21st century, no political party aspiring to govern Poland could have neglected the problem of employment laws and their impact on the labor market situation.

IV. The Main Features of the Polish Political System

²⁹ "Polska 2025: Długotrwała strategia trwałego i zrównowzonego rozwoju", Warsaw, June 2000. Earlier the same government adopted "A National Strategy for the Growth of Employment and Human Resources in the years 2000-2006" approved by the Council of Ministers in January 2000.

³⁰ See: Council of Ministers (2002) *Przedsiębiorczość-rozwoj-praca* (Entrepreneurship-Development-Work), January, p: 24.

Post-communist economic transformations initially generated political instability measured by the time a given government stayed in power. In the years 1990-1993, there were three prime ministers and three governments. Between 1993-1997 three prime ministers led the same party coalition. Between 1997-2001 one person led the coalition government, which ended its term as a government backed by a parliamentary minority. After September 2001 parliamentary elections until today the same person, Leszek Miller, runs the government.

The 1990s were characterized by the alternation of political alignments in power.³¹ Thus, the governments running Poland between 1990-93 can be described as liberal, between 1993 and 1997 as social-democratic, between 1997 and 2001 as central-right and from fall 2001 on as social-democratic.

The political dynamics of the Polish 1990s economic transformations cannot be properly understood without paying due attention to the role of trade unions. It should be reminded that the decay of the communist regime, and the 1989 changes were initiated by the union-based social movement Solidarnosc (Solidarity).

From 1989 until 2001 all Polish governments, be they social-democratic or center right, were created with the involvement of trade unions or directly backed by them. During the 1990s the Polish system of employees' interest representation was composed of two large union confederations. The first was the All-Polish Alliance of Trade Unions (OPZZ), which was the reformed continuation of the communist trade unions. The second was NSZZ Solidarnosc, which was the trade union wing of the social movement Solidarnosc.

NSZZ Solidarnosc was part of governments from 1990 until 1993. The OPZZ was part of the left party coalition in power from 1993 until 1997. In 1997, NSZZ Solidarnosc organized the electoral committee AWS

³¹ The consequences of the democratic alternation for public policies (especially for privatization) are well explored in the book by Mitchell A. Orenstein, *Out of the Red, Building Capitalism and Democracy in Postcommunist Europe*, University of Michigan Press, 2001.

(the Electoral Action Solidarnosc) which won the elections in 1997 and formed the governing coalition between 1997 and 2001.

The position of trade unions vis a vis the government changed in the 2001 parliamentary elections. The OPZZ decided to not run for the parliamentary seats neither alone nor in coalition with the SLD (the Alliance of Democratic Left), which won the elections. The NSZZ Solidarnosc, running alone, did not manage to pass the electoral threshold of 5%, remaining outside the parliament.

Thus, from 2001 on no trade union is directly involved in the government, although the OPZZ has a privileged access to the governing SLD as many of its leaders were and are the members of the SLD. The OPZZ's current president, Maciej Manicki, was a deputy minister of labor and social policy, and the minister of labor and social policy for a short period (between November 1996 and January 1997) .

After the break out of the former center right coalition in 2001, NSZZ Solidarnosc remained without direct reference to any political party. The leaders of the two leading right wing parties (PO, and PiS) have taken a distance vis a vis the NSZZ Solidarnosc trade union.

Although the two dominant trade union confederations are increasingly challenged by a newly organized Forum Zwiaskowe (Trade Unions Forum), this increased rivalry is taking place in a moment when trade union membership is declining. All the three unions have at present less members among active employees (not counting pensioners) than NSZZ Solidarnosc and the OPZZ alone had ten years ago.³²

All these changes (an increased distance from politics and the decline in membership)³³ have made trade unions more inclined to participate in the Tripartite Commission (created by the law of 15 July

³² The OPZZ has approx. 800,000 members, NSZZ Solidarnosc approx. 600,000 members and the Forum Zwiaskowe claims to have more than 300,000 members.

³³ Furthermore trade unions used to lose public support as more and more people are inclined to think that the major goal trade unions are fulfilling is to pursue the interests of its militants (83%), than their own members (75%), next all employees (38%), then the whole economy (27%) and finally the whole society (15%) - see the representative survey published in Rzeczpospolita, 12.01.2002, "W interesie raczej wlasnym". Trade unions are thus perceived as serving the interests of "insiders".

1994), which in the late 1990s years was paralyzed by the conflicts between major trade unions. The NSZZ Solidarnosc did not assent to agreements about a change in the indicator of salary growth in 1997 and 1998, and the OPZZ suspended its participation in the Tripartite Commission in 1999. On July 6, 2001 the new Law on the Tripartite Commission for Social and Economic Affairs was passed with the explicit rationale to meet the EU requirements regarding social dialogue. Jerzy Hausner, the new Minister of Labor and Social Policy, who took office after the September 2001 parliamentary elections, decided to involve social partners in his reform plans using as a platform the Tripartite Commission. The Commission henceforth met frequently to discuss the general economic situation of the country, the economic program of the government, and specific reform plans like changes in the labor code. The works of Tripartite Commission were supported by the government. However, the Ministry of Labor and Social Policy stressed the importance of the so-called autonomous dialogue, that is, encouraging autonomous agreements between trade unions and the representatives of employers and ex-post embracing their outcomes.³⁴

It should be stressed that Jerzy Hausner encouraged the involvement of "social partners" in his reform program out of conviction that this way of making reforms is both more effective and leading to more socially just outcomes.³⁵

Union rivalry has not entirely disappeared. For instance, on December 3, 2003 the President of NSZZ Solidarnosc signed an agreement about the need to further modify the labor code, but only a week later his union withdrew from the agreement and sent letters to OPZZ enterprise commissions denouncing its leaders' betrayal. But trade

³⁴ An interview with Deputy Minister of Labor and Social Policy Dagmir Dlugosz, on 15 January 2004.

³⁵ Already in the early 1990s Jerzy Hausner as then academic researcher criticized the technocratic method of introducing economic reforms and put forward an idea of an interactive method of reforming, which exploited the potential of social dialogue - see his book: J. Hausner, Ash Amin(ed.) *Beyond market and hierarchy: interactive governance and social complexity*, Elgar 1997.

unions, weakened and deprived of a direct influence on government, became more inclined to listen to the government and make compromises.

The Tripartite Commission is composed of the representative of the government, employees and employers. For some time in Poland the members of the Tripartite Commission suffered confusion of identities and roles. The representatives of one of the major trade unions used to represent also a part of the government's coalition and the main representation of employers, known as the Confederation of the Polish Employers (KPP-Konfederacja Pracodawcow Polskich - founded in 1989), was composed of the managers of large state owned enterprises. This situation changed in the late 1990s with the creation of the Polish Confederation of Private Employers (Polska Konfederacja Pracodawcow Prywatnych - PKPP), which has excluded firms with dominant position of the state treasury from its ranks .

Since its inception the PKPP and its leader Dr. Henryka Bochniarz have stressed the importance of the improvement of the business environment for the country's economic development. High taxes and bureaucratic red tape have been the most important targets of this fight, but over time the PKPP has turned its attention to the employment regulations. The simplification of the labor law and the reduction of legal protection of employment have been presented to the public as the necessary condition to relaunch economic growth and, as a result, the growth of employment. The PKPP could press on the government and could try to convince the public without entering the talks with trade unions. Yet, its President has decided that the talks with trade unions would be more effective since, if successful, they would not lead to social conflict. Her conviction has been based upon the idea that the coming membership in the EU would enhance trade unions' beliefs that Polish employers and employees have common interests to remain competitive

in the international economic environment.³⁶ The threat of the loss of jobs when Polish companies start directly facing competition from other EU countries is a powerful argument in the eyes of trade unions.

The coming membership in the EU created favorable conditions for deregulatory changes.

V. Changes in Labor Market Regulations in Poland from 1989 until 2003

Poland is a Roman law country, that is, the Polish legal system is evolving by the changes in written statutes and not by the reliance on judicial cases. The first modern statutory regulation of employment dates from March 16, 1928. The 1928 Labor Code was written to shape employment relationships in a market economy of the interwar period. Yet, it survived almost 30 years of the communist command economy and was replaced only on June 26, 1974 by the Labor Code .

The 1974 Labor Code kept the basic elements of the early codification. Thus, it stated (art. 11) that the employment relationship is based upon the principle of freedom of contract. It distinguished between an employment contracts of indefinite and definite duration (the indefinite contract being the norm), and it stipulated the rules for employee dismissal (with notice and without notice).³⁷ But, first and foremost the 1974 Labor Code served to frame an employment relationship in which the state was the dominant employer and an enterprise was not only a business unit, but also an instrument of social policy and a means for the realization of ideological goals of the socialist state. For these and other reasons, the 1974 Labor Code was ill-suited to serve the economy undergoing market reforms.

³⁶ The opinion expressed by Dr. Henryka Bochniarz in the presence of the author at the conference „Social dialogue” in Ustron, 9-11 January 2004.

³⁷ The 1974 Labour Code comprises both an article stipulating the right to work (a formal guarantee of full employment in the communist economy) and „the duty to work”, which allowed the public authorities to fine a male of 18-45 age who did not work for the work avoidance. The latter was crossed out from the Labour Code in the beginning of the 1990s.

VA) Labor Law Reforms in the Years 1989-1990

Under the planned socialist economy an employee enjoyed an extensive system of entitlements written into the labor code. The scope of these entitlements had to demonstrate the superiority of the planned socialist economy over market capitalist economy. These entitlements were *de facto* directed towards the state since the government was the dominant employer and the private sector was limited to agriculture and craft.

Understandably, in the fall of 1989 at the outset of economic transformations, the changes in the labor law were not among the top priorities of the Polish economic reformers. They were preoccupied with the goals of macroeconomic stabilization, liberalization and privatization. The most important legal changes related to the labor market were introduced by special laws introducing the procedure of group dismissals and unemployment benefits.

The changes introduced to the Labor Code in 1989 were limited to such "minor" things like the addition of a "business necessity" clause to the legitimate reasons for a dismissal or the change of the article 36 [1]§1, which allowed an employer to shorten a three-month notice period to one month, if business necessity justifies the termination of the employment contract.³⁸

At the start of the post-communist economic transformation the most important thing seemed to be the creation of conditions for economic restructuring. This was done by the Law on Collective Dismissals passed on December 28, 1989.³⁹ According to it, a dismissal of more than ten percent of the workforce of a given plant should follow a special procedure. The enterprise should notify about its plans both the trade union organization and the local employment office. Only then the normal dismissal restricting measures could be bypassed—like an obligatory period of notice. By requiring the consultation of layoffs with

³⁸ A. Swiatkowski(1990)Current Developments in Labour Law and Labour Relations in Poland, in *Comparative Labour Law Journal*, vol. 12, nr 1, p: 52 ff.

³⁹ The Official Journal nr 4/1990, item 19.

trade unions, the legislator wanted to grant the trade unions leverage over who is selected for dismissal.⁴⁰

A second labor market change took place on December 29, 1989. One day after the Law on Collective Dismissals and just two days before the launch of the program of macroeconomic stabilization, the Polish parliament passed the Law on Employment and Unemployment.⁴¹ This Law set the system of unemployment benefits in preparation of an expected emergence of unemployment. Initially the eligibility criteria for unemployment benefits were soft and generous. The amount of unemployment benefit was made dependent upon the previous earnings of an employee, but the duration of the period for receiving these benefits was limited to 12 months. The eligibility criteria were tightened by the July 27, 1990 Law⁴² and by several subsequent changes— the latest one on December 20, 2002.⁴³ The most important recent changes include: setting unemployment benefits as a percentage of the statutory minimum wage, and excluding high school graduates from the list of persons eligible to unemployment benefits.

All legal changes introduced at the end of 1989 in preparation for the program of macroeconomic stabilization were passed rapidly with little involvement of the parliament.

To sum up, in the first period of post-communist economic transformations, between 1990 and 1994-95, labor law regulations were not perceived as important for the functioning of the labor market. They were overshadowed by the scale of economic changes.⁴⁴ Policy-makers focused on such urgent policy issues as high inflation, budget deficit,

⁴⁰ From 1 July 2003 the Law on Collective Dismissals is not applied to enterprises employing less than 20 employees, which, in the intent of the legislator, should facilitate the adjustments of SMEs to changing market circumstances - see the Official Journal nr 112/2002, item 980.

⁴¹ The Official Journal nr 75/1989, item 446.

⁴² The Official Journal nr 56/1990, item 323.

⁴³ The Official Journal nr 6/2003, item 65.

⁴⁴ In his book "800 dni" (800 Days) which reconstructs his thinking when in the office of deputy prime minister, Leszek Balcerowicz - the author of the Polish shock therapy, does not even mention employment regulations all focused on questions of macroeconomic stability and privatization, - L. Balcerowicz, 800 dni, BGW, Warszawa, 1992.

indexation of wages, unemployment or social turmoil (like strikes) caused by economic hardship.⁴⁵

VB) Labor Law Reforms in the Years 1995- 1996

Public attention to the issue of labor code reform revived in 1995 as it became clear that the existing labor law was not entirely suitable for the market economy.

The 1996 labor law changes were initiated by the government, which was then backed by the centre-left coalition composed of the Alliance of the Democratic Left (SLD), Labor Union (UP) and the Peasant Party (PSL). The government created an Extraordinary Parliamentary Commission for the Modification of the Labor Law, which worked from July 1994 until February 1996 under the guidance of Wit Majewski - a SLD representative. The parliamentary commission was composed of 26 members, of which 14 were union militants. Before passing the draft law for the open floor parliamentary debate in fall 1995, the parliamentary commission met to discuss article by article the proposed modifications to the 1974 Labor Code. The proposed modifications were elaborated by the expert body—the Committee for the Reform of the Labor Law, established in 1990 as a standing advisory body to the Ministry of Labor and Social Policy.⁴⁶

The parliamentary commission held its meetings with the participation of the representatives of the major trade unions (both the OPZZ and Solidarnosc), the representatives of employers (KPP -

⁴⁵ The Law on Trade Unions was passed on 23 May 1991 and it gave trade unions the right to strike - see The Official Journal nr 44/1991, item 234.

⁴⁶ In 1990 Tadeusz Mazowiecki, then the prime minister created a commission for the reform of labor law with an implicit goal to create labor law suitable for the "social market economy" modeled after the German social economy. Its first chairman Prof. Tadeusz Zielinski, became later the Ombudsman for Human Rights and, in 1995, the candidate for the presidency of the Republic of Poland. The continuity of the work on labor law reform was assured by the constant presence of Andrzej Baczkowski who was a deputy minister of labor and social policy in five subsequent governments to become the Minister of Labor and Social Policy from February 1996 till his sudden death in November 1996.

Konfederacja Pracodawcow Polskich, the Polish Business Roundtable (PRB) and Business Centre Club - BCC), specialized state agencies like ZUS (the National Insurance Office) or PIP (the National Labor Inspectorate). The representatives of the Ministry of Labor and Social Policy received assistance from the members of the Ministry's Committee for the Reform of the Labor Law, mostly university labor law professors.

The outcomes of the Parliamentary Commission's work were submitted for vote in the Sejm—the lower chamber of the parliament—and passed in late November 1995. In December, the Senate—the upper chamber of the parliament— reviewed the Labor Code, introducing some minor changes and passed it. The Sejm then re-examined the draft law and passed it on February 2, 1996.⁴⁷ The new Labor Law entered into force three months after being signed by the President (that is since June 2, 1996).⁴⁸

The most contentious issue of in the preparation of the 1996 labor law changes was the definition of employment contract. The members of the Parliamentary Commission put forward a proposal to change the legal definition of employment to prevent the substitution of civil contracts for employment contacts.

It should be remembered that as a rule the Labor Code is not applied to civil contracts concluded for a single task (so-called agency contract) or for the performance of a specific professional assignment. Hence work based on a civic contract bypasses the Labor Code regulations. The controls of the National Labor Inspectorate (PIP) showed that in 1994, 15 percent of the enterprises concluded agency contracts for assignments that should have been employment contracts.⁴⁹ Trade union members, supported by the representatives of state agencies (the PIP and the National Social Insurance - ZUS) called for the introduction of a legal

⁴⁷ The Official Journal nr 24/1996, item 10.

⁴⁸ The only exception was the rule extending the period of annual leave, which became law starting from January, 1997.

⁴⁹ The protocols of the a Extraordinary Parliamentary Commission for the Modification of the Labour Law - www.sejm.gov.pl.

assumption that every job implies employment contracts unless an employer proves that the job qualifies for an agency contract. This proposal was opposed by the Ministry of Labor and Social Policy and eventually rejected since it would have created legal uncertainty and high implementation costs. A compromise solution was worked out which defined employment contract as “a work under principal’s supervision”.

Table 13

Main Labor Law Changes Introduced in 1996

The number of the Labor Code article	Subject	Direction of change
Art. 23 par. 6	An employee is automatically <i>ex lege</i> transferred to a new employer after the merger or take over	Preventing employees firing when a merger takes place
Art. 25	Mandatory transformation of a third definite employment contract into an indefinite one	Before no limit existed as to the number of employment contracts for definite time
Art. 25 par. 2	Lengthening of the maximum probation period from 2 weeks to 3 months	Facilitating the selection of employees.
Art. 98	Removing the obligation to issue an opinion about an employee’s work	Such a mandatory opinion was not credible and in practice was replaced by a letter of reference issued to support an employee
Art. 101	Ban on conducting competing activities to the activities of an employer during and, conditionally, after the	Before the 1996 Labor Law nothing similar existed

	termination of employment contract	
Art. 104	Obligation to create a working code in companies employing more than 5 persons	The law reduced the threshold for writing a working code from 50 to 5 employees
Art. 129	Shortening weekly working time from 42 to 40 hours	Increased labor costs
Art. 154	According to the Labor Code an employee has the right to: a) 18 days after having worked for at least 1 year; b) 20 days after 6 years; c) 26 days after 10 years	The length of annual leave was increased from 14 to 18 days only for the first group

The 1996 Labor Code introduced over 200 modifications to the 1974 Labor Code. It did clarify many employment rules, which were inherited from the old 1974 Labor Code, and adjusted them to the needs of the changing economy. But the changes were not sufficient to meet the requirements of the market economy, as it became evident later.

The 1996 Labor Code was criticized by the employers' representatives (the Polish Business Roundtable (PRB) and the BCC) as too friendly to employees and too inflexible for small businesses. However, the two main trade unions were satisfied with the changes. The representatives of NSZZ Solidarnosc, then in the opposition as a political force, were satisfied with the reduction of weekly working time. This represented the implementation of the 1980 union's request.

In the public perception, however, the 1996 Labor Code modifications distributed gains and losses between employers and employees quite evenly.

VIC) Labor Law Reforms in the Years 2002-2003

The comprehensive statutory regulation of the employment relationship seems to fit better an economy characterized by a stable economic structure with large industrial enterprises and skilled workers than an economy undergoing rapid economic transformations, with diminishing average size of an enterprise, with decreasing employment in the manufacturing, and expanding employment in the service sector.

The coexistence of comprehensive employment regulations with the transition from an economy dominated by large production enterprises to an economy dominated by services has resulted in a dual labor market. It consists of a declining number of protected jobs versus a growing area of the economy where existing labor regulations do not apply for two reasons. First, micro-enterprises are not covered by some legal regulations. Second, existing laws are under-enforced. Adding to this picture the existence of an extensive grey zone that accounts for approx. 20% of GDP,⁵⁰ the discrepancy between the legalistic picture of the employment relationship and the real functioning of the labor market becomes evident. This could strike analysts and decision makers and, even more importantly, would make a large segment of the workforce indifferent towards protective employment regulations as they do not benefit from them.

The new government taking office in fall 2001 was aware of the inadequacy of normative views and it decided to boost economic development by flexibilizing labor market and supporting small and medium sized enterprises.

The reduction of financial costs and administrative burden for enterprises was the priority of Minister of Labor and Social Policy Jerzy Hausner since he took office in fall 2001. The program document of the new government "Entrepreneurship above all" (Przede wszystkim

⁵⁰ M. Kabaj(2003)Zatrudnienie w szarej strefie (*Employment in the grey zone*), in MGPIPS, e-gazeta.

przedsiębiorczość) approved in the beginning of 2002 attests it.⁵¹ In fact, the words in the title of this document are not randomly chosen: they reflect the belief that by easing the burden for entrepreneurs the government hopes to speed up economic growth and by this to increase the number of available jobs.⁵²

The package of labor law changes was presented and discussed with Social Partners in a Tripartite Commission in its meeting on 28 January 2002.

The labor law changes were prepared by the Ministry of Labor and Social Policy, and coordinated within the government and in the parliament by Deputy Minister of Labor and Social Policy, Ms. Krystyna Tokarska-Biernacik. Then the proposal for labor law changes was consulted with trade unions and employers representatives, agreed with them as two draft agreements and signed on 19 April 2002 and on 8 May 2002. NSZZ Solidarnosc did not sign these agreements, but its opposition was inconsequential as this union has lost the power to mobilize social protests and it did not get support in the Polish parliament.⁵³

The parliament passed the law modifying labor code on July 26, 2002 with the votes of the governing social-democratic coalition supported on this occasion by the Citizen's Platform (PO) - a party representing the Polish middle class and entrepreneurs.

The table below lists the main changes in the labor law passed on July 26, 2002 and agreed earlier in the Tripartite Commission.⁵⁴

Table 14

Main Labor Law Changes in 2002

⁵¹ The economic program of the new government was composed of three packages: Entrepreneurship above all (Przede wszystkim przedsiębiorczość), First job (Pierwsza praca) and "Infrastructure - the key to development" (Infrastruktura - klucz do rozwoju).

⁵² See „Kodeks będzie bardziej elastyczny” (Labour Code will be more flexible) in Rzeczpospolita, 27 July 2002.

⁵³ The Forum of Trade Unions (Forum Związków Zawodowych) became the member of the Tripartite Commission on 7 March 2003.

⁵⁴ The trade union NSZZ Solidarnosc did not sign the agreement in the Tripartite Commission, but it did not mobilize its members to oppose the changes and claimed its success in softening the impact of some changes (see the text).

The number of the Labor Code article	Subject	Direction of change
Art. 22	The definition of employment contract	Limiting the substitution of self-employment for dependent work
Art. 25	Definite and substitution employment contract	Suspending the third contract rule and introducing flexible substitution employment contract
Art. 37	Limiting the right for a paid leave for the search of a new job	The right is limited to employees who are dismissed by an employer (3 days when a dismissal period is 3 months and 2 days if the dismissal period is shorter)
Art. 38	Limiting the scope of union consultation in case of an employee's dismissal	The change requires from an employer to consult an enterprise unions and not their local (or regional) offices
Art. 77 par. 2	Remuneration code	The obligation of preparing a remuneration code limited to enterprises with more than 20 employees
Art. 77	Travel on duty	Employers outside the public sector can set the travel reimbursement about the official minimum level
Art. 86	Payment of salaries	No longer an employer is required to ask an employee for a permission to transfer his salary to his bank account
Art. 92	Sickness pay	The law shortened the employer's payment period

		from 35 to 33 days and introduced a rule than an employee does not receive a salary for the first day of his sick leave, if the sick leave if for a period of less than 6 days
Art. 93	Death bonus	Employer can discount the insurance premium the family of dead employee gets from a mandatory death bonus, in case he insures his work force (the regulation boosts interest in insuring employees)
Art. 97	Work certificate	Employer does not have to issue a work certificate if an employee renews the contract with him
Art. 104	Working code	The obligation of preparing a working code limited to enterprises with more than 20 employees
Art. 108	Financial fines	Financial fines imposed on employees counted as spending to improve working conditions
Art. 129	Extension of work duration calculation period	A weekly working time should be calculated and should stay within maximum limits in the period of 4 (instead of 3) months
Art. 129 (par. 5a)	Extension of the possibility of having an	Interrupted working time is not limited any longer to the

	interrupted working time	transportation sector, but can be used in all sectors of the economy
Art. 129 (par. 8)	Employment arrangements for task oriented work	Task oriented working time will allow to work at home (for instance telecommuting)
Art. 129 (par. 10)	Break in working time	An employer can introduce one (up to 60 minutes) working break which does not count to the working time
Art. 133	Annual working time	In an employment contract both sides can expand the limit of yearly overtime, but weekly working time cannot exceed 48 hours
Art. 134	Supplement for overtime	The supplement for overtime was lowered to 50% for normal days, but kept 100% for overtime for work on Sundays and holidays
Art. 143	Free time for overtime	Employer can grant free time in exchange for work overtime
Art. 154, 155, 162	Principle for granting annual holidays	Free days falling in the period of annual holidays are counted in the duration of annual holidays
Art. 163	Plan of annual holidays	Regulation lifts the obligation to compile the enterprise's plan of annual holidays
Art. 209	Reporting to inspection agencies	Regulation extends the periods in which an employer starting his activities has to report this fact to the local

		work inspection office and hygiene inspection office
Art. 229	Medical check up	Employees re-hired by the same employer are freed from the obligation to repeat medical check ups
Art. 237	Sanitary education	Employees re-hired by the same employer are freed from the obligation to repeat sanitary education

The 2002 labor changes were presented by the government, employers and the mass media as one of the indispensable reforms for the reduction of unemployment. The reformers stressed labor law modifications, which would make labor market arrangements, and the employment relationship in particular, more flexible. In fact, these labor law changes seem to have increased the flexibility of the employment relationship. The increased flexibility is best illustrated by examples: the *direct* reduction of labor costs through the reduction of the sickness period paid by an employer, the limitation of paid leave for the search of a new job, the reduction of a premium for overtime, and the elimination of the costs of medical check-up if an employee is rehired, or indirectly via the elimination of bureaucratic fatigue—the plan of annual holidays.

The changes were especially favorable to smallest businesses (employing up to 20) as they reduced administrative costs of creating remuneration and working codes.⁵⁵

A year later, in fall 2003, labor law modifications⁵⁶ were passed with the explicit goal to harmonize certain Polish labor law regulations to the

⁵⁵ In addition small businesses do not have to create the services for the monitoring of occupational health and safety.

⁵⁶ The Official Journal nr 213/2003, item 2081.

requirements of membership in the European Union (the selected labor law changes are presented in the table below).⁵⁷

Table 15

Main Labor Law Changes in 2003

The number of the Labor Code article	Subject	Direction of change
Art. 18	Broadening the list of factors of discrimination	Ban of discrimination has been extended on ethnic, faith, sexual and form of employment reasons
Art. 37	Leave for search a new job	During a dismissal period an employee can take two days of leave to search for a new job, only if he is covered by a shortened (one month or a two week notice)
Art. 92	Payment for sickness leave	Employer pay 80 percent of remuneration yearly for first 33 days of sickness leave
Art. 132 and 133	Daily and weekly statutory rest	Employees get the right for an uninterrupted 11 hour daily and 35 weekly rest
Art. 154	Length of annual holidays	Since 1 January 2004 each employee has the right to 20 days of annual leave before his cumulative work period reaches 10 years, and 26 days afterwards.

In fact, the harmonization law was prepared by the previous government and passed by the parliament on 18 September 2001, but the

⁵⁷ The changes were presented as “the Europeanization of the Polish labor law”.

President of Poland vetoed it . The reason was that the 2001 labor law modifications comprised art. 151 par. 2 and 3, which introduced the ban on working on Sundays and on festivities in service and commercial enterprises employing more than 5 persons.⁵⁸

Among the November 2003 modifications of the labor law, the most important is the return to the principle of sickness payment for all days of sickness leave. From 1995 an employer had to pay to her employees a salary equal to 80% of her basic remuneration during the sickness period, up to 35 days per year. The sickness pay for the period exceeding this threshold is paid by the National Social Insurance (ZUS). In the 2002 Labor Code reforms the parliament shortened the this period to 33 sickness days per year, and introduced the rule that an employee did not get a sickness pay for the first day, if the sickness leave lasts up to 6 days. The intention of the legislator was to reduce the number of short sicknesses without punishing those who get seriously ill. The regulation was mandatory since 1 January 2003, but by mid-2003 it became clear that it was costly for both employers and the National Social Insurance (ZUS). An average sickness leave had expanded over 6 days, apparently due to the corrupt practices of medical doctors.⁵⁹ The plausible failure of this regulation was foreseen by the representatives of employers, who in 2002 argued for not paying the first day of any sickness leave. Not being able to put it through, they agreed for the rule of not paying for the first day out of sickness leave up to 6 days.⁶⁰ When the failure of the regulation was identified, the representatives of the employers decided to restore the former rule as a "second best," not being able to introduce their preferred choice of not paying for the first day in the case of any sickness leave.

⁵⁸ Niedziela dniem pracy (Sunday remains the working day) in Rzeczpospolita, 13 October 2001.

⁵⁹ The short term (up to 6 days) sickness leave decreased by 25% and the long term leave increased by 50% - see "Od państwa socjalnego do państwa pracy" (From Welfare State to Workfare State), in Rzeczpospolita, 6 November 2003.

⁶⁰ An interview with Dr. Jacek Mecina, Responsible for Social Dialogue at the Polish Confederation of Private Employers (PKPP) on 16 January 2004.

The 2003 labor law changes harmonizing the Polish labor law to *the EU acquis communautaire* included, among others, the broadening of the list of causes of discrimination to ethnicity, religion, sexual orientation or employment for a definite or indefinite period;⁶¹ requiring parents' permit in the case of employing adolescents or restoring the rule of the third contract for a definite period. Furthermore, the 2003 modification of the labor code introduced a ban on mobbing, and allowed a mobbed employee to resign and ask for damages. The amount of damages is not limited and depends on the court's decision. This last change is perceived by Polish employers as being too early, as it is recommended, but not required by the EU.⁶²

It is important to stress that until the 2002-2003 labor law reforms most of entitlements granted to employees by the Labor Code depended on total working years of a given person. This was the case of the length of holidays or the amount of dismissal compensation. Thus, an employer was obliged to pay a premium for the years an employee worked for another employer. From the 2002-2003 labor reform the duration of work is calculated as *the duration of employment with the current employer*. This is a significant change, as it took the government and trade unions more than a decade to recognize that the consequences of an employment relationship should be a function of current employment and not the accumulation of work history.

VII. Conclusions: Labor Law Reforms in the Context of Post-Communist Transformations

Sejm - the lower chamber of the Polish parliament, passed the July 2002 and November 2003 labor law changes with the votes of the governing social-democratic coalition and the oppositional liberal Citizens'

⁶¹ See: Interview with Waldemar Gujski entitled "Warning for employers" in Rzeczpospolita 31 December 2003.

⁶² Mobbing is defined as those acts of managers or employers that increase stress at work or generate emotional violence.

Platform (PO). This ideologically particular coalition was not an outcome of political horse-trading but rather a program-oriented alliance, due to the widely diffusion of the opinion that low flexibility of labor law is one of main reasons of high unemployment. However, it seems that social-democratic governments can implement the reform of labor market regulations more easily. In addition, if these reforms contribute to the reduction of regulatory costs falling on enterprises, they might enjoy the support of liberal parties.

Labor law reforms have been eased by the fact that the public opinion in Poland was favorable to deregulation partially due to the opinion that such changes would be advantageous to the society, and partially because no credible alternative existed. The Polish mass media overwhelmingly supported labor law reforms and there were no voices calling for an alternative (for instance an interventionist approach) approach to try to reduce unemployment.

Furthermore, labor law reforms were facilitated by the fact that Polish trade unions were "in the defensive" in the public perception. They did not take a uniform position vis a vis changes and that some changes served to strengthen their position among employees and vis a vis potential competitors. Let us elaborate on these points.

As noted earlier, NSZZ Solidarnosc - one of the two leading trade unions, has lost a large part of its political clout due to the failure of its parliamentary campaign in 2001. Its new leaders have started to act cautiously not being certain of their social support. The experience of co-governing the country in the years 1997-2001 has shown that grand ideas and values are not easily transformed into practical policy measures. Still NSZZ Solidarnosc tends to perceive labor market regulations in terms of social rights, and has kept contesting recent labor law changes portraying them as the erosion of some of these rights.

The leadership of the OPZZ - the second large trade union, is much more pragmatic and does not speak about employment laws in terms of

social rights, but rather in terms of job opportunities and the impact of such changes on the position of trade unions.

The difference might be partially explained by pointing to the social characteristics of their members. The most important component of the OPZZ is the union of teachers, whose job security is regulated by a special statute - "the Teachers' Charter."

In general, the OPZZ tends to represent a better-educated part of workers (including middle-rank managers), whereas NSZZ and Solidarnosc includes both unskilled and skilled workers.

The new unionist force - The Forum of Trade Unions (Forum Zwiaskow Zawodowych) is a new and very heterogeneous organization comprising groups of employees of enterprises in need of state aid (the National Railway - PKP, or Steelwork - Huta Katowice). Thus, they tend to be more involved in pressing the government for subsidies and a special treatment for the branches they represent.

Furthermore, trade unions have been more inclined to support reforms when they could make "a deal". Thus, for instance, until 2002 the law gave protection against the dismissal of a potentially numerous category of union militants.⁶³ By the 2002 labor law changes, the protection has been limited to the three members of the unions' founding committee, and no more than one member of a trade union, which does not have the status of a trade union representative of the employees. The change restricting the number of protected unionist was agreed with largest trade unions, which as a rule have the status of representative unions. The large unions used this limitation to restrict the attractiveness of the so-called "wild trade unions," small trade union organizations created with the goal of granting its members legal protection against dismissal. This change was promoted and defended by large union leaders amidst miscomprehension among union rank-and-file, but it did effectively limit the spread of new union initiatives.

⁶³ Even to the members of union's internal auditing committee, which is in charge of controlling the action of the union's board.

Increasingly, the changes in the labor law have been influenced by the decisions of the Supreme Court and the Constitutional Court. As noted earlier from 1996 the Polish labor law stated that every third fixed-term employment contract concluded within a month after the end of the second fixed-term employment contract would become, by law, an indefinite employment contract. In the practice, this troublesome rule was avoided by signing annexes to existing fixed-term employment contracts.

In the sentence from November 17, 1997 the Supreme Court decided that annexes to a contract should not be treated as separate contracts, unless they serve to bypass the law.⁶⁴ This sentence meant in the practice that annexing was legitimate if both sides had done it voluntarily. Counteracting the Supreme Court decision, trade unions pressed the government to include annexes as an integral part of an employment contract and such a change was introduced in the labor law (art. 25 par. 2) dated November 14, 2003. In exchange for this restriction, the 2003 labor law has allowed the unlimited use of employment contract for definite period, if it serves to substitute an absent employee or to perform seasonal and cyclical works.

The Constitutional Court by decision from 18 November 2002 invalidated the art. 214 par. 7 of the Labor Code, which stated that if a collective agreement expires, it remains obligatory until a new collective agreement is signed.⁶⁵ If a new collective agreement is not signed, in the case of enterprises employing more than 20 persons, an employer is obliged to state the principles of remuneration in the enterprise's remuneration code.

The works on labor law reform in Poland have drawn chiefly on legal experts, with the expected outcomes of the law changes defined only in general terms.

⁶⁴ The Sentence of the Supreme Court from 17 November 1997 (I PKN 370/97).

⁶⁵ In Poland collective agreements refer to and wage bargaining takes place predominantly at the enterprise level.

The impact of labor law deregulation on the economy and on employment has not been quantified in any research accompanying the work on the labor law. As a rule, in Poland the government makes quantifiable estimates only when a law might cause spending out of the budget. Thus, the change of the rules of the sickness pay was justified by pointing to the increase of spending out of the National Social Insurance (ZUS) budget. Thus, at present the government identifies *the budgetary costs of a regulation* and not *regulatory costs* in the broad meaning of the term.

Economic theory considers labor market regulations as one of the main sources of unemployment. According to the current state of the economic knowledge, at least in the short run, other economic factors are more important for the level of employment. Thus, the Polish government has moved with reforms on other fronts. Thus, the corporate income tax was reduced from 32 percent in 2003 to 19 percent starting in January 2004. The government has also intensified efforts to develop the transport infrastructure and to restructure loss-making industries, chiefly hard coal mining.

The effects of the 2002-2003 labor law reforms are difficult to estimate, not least because their effects will show up with a time lag. Fortunately for Polish reformers, the economic growth, spurred by rapidly growing exports, resumed in 2003. The estimated rate of GDP growth in 2003 was 3.4%, much higher than the 2.5% written in the budget law for 2003.⁶⁶ But, the results of faster economic growth were hardly reflected in the rate of unemployment, which fell slightly in 2003.⁶⁷ Yet, the combination of faster growth and of more flexible labor market regulations made the government more optimistic about the future level of unemployment. The government started to give an unemployment rate of

⁶⁶ See: Raport makroekonomiczny i walutowy, in Gazeta Wyborcza, 22 December 2003.

⁶⁷ According to National Statistical Office (GUS) in 2003 the number of registered unemployed fell by 41,300 persons reaching in the end of 2003 3.175m persons, whereas in 2002 this number rose by 100,900 persons. [PAP, 22 January 2004]

13.6% as a probable rate of unemployment in 2006 in its macroeconomic forecasts .

Recent labor law reforms, and especially the 2002 labor law reform, had clearly a deregulatory edge. They were initiated by the government, which saw in the increased labor market flexibility one of the crucial components in its strategy to relaunch economic growth and to reduce unemployment. Leszek Miller, the prime minister in office from Fall 2001, decided to modernize the Polish post-communist left pointing to the priority of entrepreneurship over redistribution. From the late-1990s the leaders of the Polish Social-democratic Party (SLD) tried to learn from the reform strategies of new left leaders such as Tony Blair or Gerhard Shroeder. The basic principle of social reforms implemented by the SLD can be summarized as follows: to modernize social policies in order to save their usefulness instead of conserving current policies and see the welfare state crumbling incapable of fulfilling its high promises.

Labor market reforms were supported by the representatives of entrepreneurs. For the first time since the beginning of economic transformations, they started to represent the interests of small businesses, hence the interest in the quality of the business environment, instead of lobbying the government on behalf of large companies. Henryka Bochniarz - the dynamic leader of the Polish Confederation of Private Employers exemplifies this change, as in the mid-1990s, she was the president of the Polish Business Roundtable—a club of wealthy business leaders.

Building a broad consensus, almost across the political spectrum, except for the two populist parties—the League of Polish Families (LPR) and Self-Defence (Samoobrona)—was eased by the fact that the three ministers dealing with economic issues and nominated by Prime Minister Leszek Miller in Fall 2001, that is Jerzy Hausner, Minister of Labor and Social Policy, Jacek Piechota, Minister of Economy and Wieslaw Kaczmarek, Minister of State Treasury were representing the so called technocratic wing of the social-democratic party. Jerzy Hausner clearly

relied more on the soundness of his policy arguments than on the calculations of the party's interests.

The reform strategy of the Minister of Labor and Social Policy Jerzy Hausner, which consisted of getting a pre-approval of social partners before submitting the law for vote in parliament, proved successful since all parties trumpeted their victory. Henryka Bochniarz, the president of the Confederation of Private Employers (PKPP) evaluated the 2002 Labor Code modification as reasonable compromise, which "showed that the interested parties can work together and agree on such hard issues".⁶⁸ Maciej Manicki, the President of OPZZ, was satisfied from the fact that the Law would allow to reduce various forms of self-employment by making a regular employment a more attractive option.⁶⁹ Even Marian Krzaklewski - a former president of NSZZ Solidarnosc claimed a success for his union saying that thanks to its involvement the employment rules became more protective for employees than otherwise would have been.

For the success of the 2002 labor reform it was important that the costs of reforms were not concentrated on any distinct labor group and that the representatives of employers convinced the public that short-term benefits for them would be translated into better job chances for all.

The timing of the 2002 labor law reforms seems also important for their success. The reform law was written, consulted and agreed with social partners and passed by the parliament within the first ten months after the 2001 parliamentary elections and the start of a functioning of new social-democratic government. Reforms, which could be perceived to harm a party's social base in the short term, could only be introduced at the outset of a government's term in office. In addition, the opposition parties see less immediate benefits of attacking the government at the beginning of its term.

According to all sides participating in the reform of the Polish labor regulation, the need to make regulations more flexible had been identified

⁶⁸ See „Kodeks będzie bardziej elastyczny” (Labour Code will be more flexible) in Rzeczpospolita, 27 July 2002.

⁶⁹ Author's interview with Maciej Manicki on 16 January 2004.

by looking at how the existing regulation fit the new economic system and its structural characteristics. These were thus domestic considerations. According to high officials of the Polish government, foreign investors participating in the process of privatization were not complaining about the employment regulations in Poland. Indeed, these employment regulations are quite close to the rules existing in the countries of continental Europe.

But these policy statements hide the fact that the international competitiveness of the Polish economy is a major concern of the subsequent governments. In such a perspective, employment regulations are a part and parcel of the national economic system and should be adjusted to the requirements indispensable for its international competitiveness. This point was neglected by people who compare the level of employees' protection to the most expensive models without due attention paid to the problem of international competitiveness.⁷⁰ The public discourse regarding labor law reform has been divided between the rhetoric of social rights (employees rights), and the economic discourse on costs and flexibility. The rhetoric of social rights was pointing to the generous employee protection offered in some European countries (like Germany or Italy), the economic arguments pointed to the examples of jobs boosting flexible arrangements introduced in some countries like for instance the Netherlands.

Labor law reforms are not a one time act, but rather a process of change. The initiatives to modify some current arrangements come from trade unions and employers. Thus, for instance, in an agreement dated December 23, 2003, social partners—trade unions and employers representatives—agreed to introduce a new rule, according to which a third fixed-term employment contract is not automatically transformed into an employment contract for indefinite period, if the fixed-term employment contract is signed for a period longer than 12 months.

⁷⁰ Like for instance Ewa Tomaszewska, Vice-president of NSZZ Solidarnosc - see author's interview with Ewa Tomaszewska on 15 January 2004.

The current government also prepares new labor law reform initiatives. Among the most urgent questions to be addressed, the government mentions the cancellation of a rule stating that the period of high and higher education is counted to define the length of annual holidays, and the simplification of registration of household workers in order to extract this area of work from the shadow economy.⁷¹ The reforms of the labor law in Poland will continue in the future.

⁷¹ See "Flexibility of employment" - an interview with Krzysztof Pater, Deputy Minister of Labor and Social Policy in Rzeczpospolita, from 11 February 2004.

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