The cost of dismissals in Spain before and after the labor reforms

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Abstract: Several reports and papers about Spanish labour market have focused on the allegedly high dismissal costs and the persistently high rate of temporary work. In fact, the last major reforms on labour regulation have tried to reduce them. In this paper, I will discuss the most relevant expenditure items that any employer is Spain has to face to lay off workers. Implicit, indirect and procedure costs appear to be the main problem, and not severance payments for unfair dismissal. Despite of the efforts on improving the regulations being put forward by this article, there are several dysfunctions caused directly by the law, as it provides incentives to hire temporary workers and to avoid redundancy legal procedures.

Keywords: dismissal, severance payments, temporary workers, labour market reforms.

Introduction[1]

We shall begin this analysis with a truism. Employers (be they individuals or legal entities) seek to earn money and the more, the better. This however, does not mean imply that this is their only goal or that they are without ethics. Workers too are unlikely to offer their services free of charge. Both of these parties adapt their behavior to the specific labor market in which they operate, be it in terms of regulation, judicial interpretation or social habits.

The decision to begin or end a working relationship is, therefore, the result of a cost-benefit analysis. However, the effects of the Employment Protection Legislation (EPL) affect the entire labor relations system. An at will dismissal system grants employers a strong negotiation power to alter the working relationship. Clearly, if workers can be dismissed with no incurring costs, they will have little resistance ability against employer pressure. On the other hand, very restrictive dismissal regulation may make it difficult for employees to voluntarily adapt their working conditions to the needs of the market.

The cost of dismissals, therefore, is a key element in understanding the dynamics of working relations. The effects of the EPL have been widely studied by economics researchers[2], although there are still many aspects left to examine. Thus, the majority of studies are partial, referring only to the impact of some specific issue, failing to offer an overall view of the situation.

The desire to synthesize the EPL into one unique indicator has led diverse institutions to create indices that, though of limited value, offer an objective vision of the issue at hand. The most frequently used and probably the most complete of these indices was created, in several versions, by the OECD. In the most recent version 3 of the Employment protection for regular contracts index, nine elements are

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[2] In a review of the current research available on this issue, we find John T. Addison and Paulino Teixeira's «The economics of employment protection», *Journal of Labor Research* 24, no. 1 (March of 2003): 85-128, doi:10.1007/s12122-003-1031-0.

included to determine how restrictive legislation is in regards to the costs of individual dismissals and four others for collective redundancies.

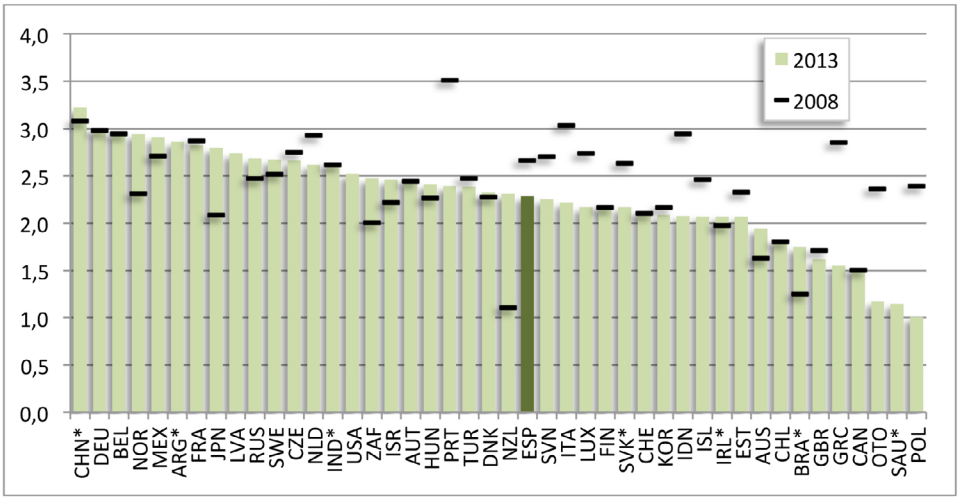
Table 1: OECD Employment protection for regular contracts (v3). Items and weights.

Name		Version 3 weights
Individual dismissals	Notification procedures	1/2
	Delay involved before notice can start	1/2
	Length of the notice period at 9 months tenure	1/7
	Length of the notice period at 4 years tenure	1/7
	Length of the notice period at 20 years tenure	1/7
	Severance pay at 9 months tenure	4/21
	Severance pay at 4 years tenure	4/21
	Severance pay at 20 years tenure	4/21
	Definition of justified or unfair dismissal	1/5
	Length of trial period	1/5
	Compensation following unfair dismissal	1/5
	Possibility of reinstatement following unfair dismissal	1/5
	Maximum time to make a claim of unfair dismissal	1/5
Collective dismissals	Definition of collective dismissal	1/4
	Additional notification requirements in case of collective dismissals	1/4
	Additional delays involved in case of collective dismissals	1/4
	Other special costs to employers in case of collective dismissals	1/4

Source: OECD.

As we shall see later, in a direct or indirect manner, all of the signaled aspects have been the object of modification in Spanish legislation between 2010 and 2014. However, the impact on the aggregate index has been limited, even though certain aspects are not included such as the role of case law. In fact, the set of regulatory modifications has reduced the index for Spain by 14.1% between 2008 and 2013. This reduction is not linear, but rather, it concentrates on two moments: the labor reform of 2010 reduced it by 3.8% and the reform of 2012, by more than ten points.

Figure 1: EPRC.v3 Index for 2013and 2008.



Source: OECD.

However, it is certain that despite the fact that the quantitative change is not as great as it was anticipated a priori, it is certainly not insignificant. The move from 2.660 to 2.284 out of a maximum of six, in relative terms, has had a notable impact. Thus, of the forty four nations for which the OECD created its index, it has moved from the fourteenth to the twenty fourth position.

Aside from the actual impact of cost of the dismissals on the economy or on employment, or even the questionable weighing of the different items that is carried out in this index, clearly these are good starting points to structure the analysis. To correctly contextualize the exhibition, it is necessary to briefly present the starting point of dismissal regulation and its costs, and the management and sense of the latest labor reforms, which are the focus points of the first two sections of this work. The third and fourth sections, respectively, examine individual and collective dismissals, evaluating the elements that generate costs. Finally, and to conclude, the fifth section analyzes the implications of the costs of dismissals in the Spanish system of dismissal on business contracting strategies and indirectly, on the labor market.

1. Basic elements of the historic configuration of costs of work contract termination in Spain

The compensation system for contract termination, as it is currently known in Spain, has its origins in the Statute of Workers approved in 1980. This law, with numerous modifications[3], is the one that still governs labor relations in Spain. In it, for the first time, a fixed system of compensation was established, without a margin of appraisal for the judicial bodies.

It is not necessary to perform an exhibition of the history of the regulation, but it should be understood that this is the moment in which the distinction between the fair dismissal *(despido procedente)*, i.e. which is according to the legal causes and proceedings, and the non-legal one became consolidated, with the latter being qualified as unfair or invalid.

Furthermore, in a discussion of this norm in the Spanish Parliament, the terms of the political and social debate regarding this issue were also established; while some anticipated the failure of this regulation because of its lack of sufficient social support[4] or suggested the risk of the destruction of employment due to the lower dismissal costs[5], others denounced that a rigid termination process impedes hiring[6]. These are very similar arguments to those used today to defend certain positions.

Although we shall not go into the precise content of the legislation established, we shall note the basic elements, which to some extent are also those that are the basis of the current model. First, a distinction should be made between dismissals based on economic or technological causes– typically affecting various workers– and individual dismissals having objective causes. In the first, there was a requirement for a consultation period of 30 calendar days, carried out with worker representatives and, if agreement was not reached here, for an authorization of the Labor Authority. The so-called "termination due to objective causes" is applicable, among other cases, to the "objectively accredited need

[3] The applicable text was redrafted in 1995 (Royal Legislative Decree 1/1995, of 24 March), although it should be noted that a new draft has been authorized. Law 20/2014, of 29 October has provided the government with a period expiring on the 31st of October of 2015.

[4] The Deputy of Euskadiko Ezquerra Bandrés Molet, in the first session of the Labor Commission, declared that the new regulation would be «an absolute failure» as it was approved without the support of workers, as reflected by Gallego-Díaz, S. «*Socialistas y Comunistas, enfrentados respecto al estatuto del trabajador*». *El País*, 7th of September 1979.

[5] Communist leader Carrillo, in the session, referring to the majority and in regards to the text presented, affirmed that «they open the doors to dismissals in this Statute, to objective dismissals, disciplinary dismissals, under multiple forms, without control, that will result in business owners laying off a large number of workers» (Diario de Sesiones del Congreso de los Diputados no. 51, 11 December 1979, p. 3398).

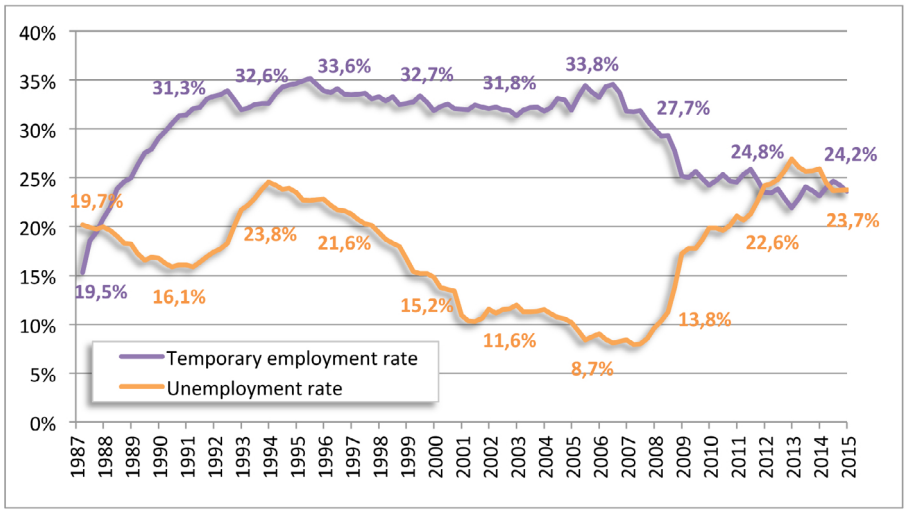
[6] Then deputy and later Labor Minister, Pérez Miyares declared the following: «All of this is no more than a philosophy: Are we here to defend the work positions, position by position? It is about making the worker situation in the company so rigid that it is almost impossible for a worker to be fired, closing the employment market off in a manner that in this country, no one can be hired? Don't we realize that this legislation that we wish to declare the best, among other things, is making the country incapable of exiting the employment crisis that we are in, created by whatever the causes may be, these and others? But this mechanism does not operate in support of the solution to the problem and when we wish to offer solutions to the same, in the end, the qualifications and the sentiments that I clearly respect but do not share, do not seem to be the logical, coherent and valid responses to the problem that we are facing»; an argument that was immediately responded to by the union leader (and Communist deputy) Camacho, negating the idea that «employment is not created by laying off workers more easily». *Ibid.* p. 3747.

to abolish an individual work position", although this was only applicable to companies having less than 50 workers. In this case, the procedure is limited to a written communication of the dismissal, the availability of compensation and the granting of a notice period of up to three months, according to the worker's tenure. Depending on the case, the results of not carrying out the formal requirements was the invalidation of the dismissal, with the obligation to readmit the worker and pay all wages that were not received during this period. In the case in which the content and form of the dismissal was correct, the legal compensation was -and this remains the same, thirty five years later– 20 times the daily salary for every year of worker service, with a one year limit.

Along with this general system, which is quite strict, for the case of temporary contracts, the termination had not further procedures than the prior notice of 15 days for workers with over one year of tenure with the company. In subsequent years, especially after 1984, there was the clear intent to use temporary contracts as an employment mechanism. With the unemployment rate nearing 20% and having increased by two and a half points since the previous year, the so-called temporary employment contract was extended and consolidated. This contract type allows for temporary contracting without cause, with a maximum of three years and a compensation equaling the salary of one day for every month that the contract lasted. Temporary contracting data did not begin to be published until 1987, but the effects of this policy were devastating. Since this time and until 1992 when the problem of temporary work began to be addressed, some two million temporary work contracts were created, while simultaneously eliminating 610,000 permanent jobs.

This situation has become one of the most characteristic features of the Spanish labor market over the past decades. The high degree of temporary contracts, over 30% for the past 28 years, has been reproached by international institutions and has focused on legislative efforts. Over the following decades, numerous reforms were introduced, affecting the cost of dismissals, almost always with the aim of reducing the cost differences between temporary and indefinite contracts.

Figure 2: Unemployment rate vs temporary employment rate.



Source: Spanish National Statistics Institute.

At this point, we shall now take a leap across time and consider the year 2008, prior to the onset of the harshest effects of the economic crisis. At this time, the dismissal system was established in the following manner:

- Collective redundancies are distinguished from individual ones in regards to the total number of workers affected in the company. Thus, collective dismissals affect more than 10 workers in a company of under one hundred employees, ten percent of the staff in companies of between

one hundred and three hundred employees, and over thirty employees in larger companies. It should be noted that, although a scheme is followed that is similar to Council Directive 98/59/EC of 20 July 1998 on the approximation of the laws of the Member States relating to collective redundancies, it is more protective. This is because the reference to dismissals is not taken in the work center but in the entire enterprise, which generally speaking, offers a greater degree of protection to the workers[7].

- In the case of collective redundancy, there was a mandatory worker consultation lasting for a period of no less than 15 days (companies of less than 50 workers) or 30 days (larger companies). Regardless, the labor authority intervened in the final phase of the proceedings. If agreement was reached between the worker representatives, only in exceptional cases was the dismissal prohibited. If agreement was not reached, the labor authority was entitled to evaluate the proposed measures in regards to the alleged causes and, when relevant, did not allow the contract termination. This labor authority is an administrative body which, according to the scope of the dismissal, may be either state-based or a regional administration (*autonomous communities*). Regardless, although it was a motivated decision based on the law, it always had a certain political nature.
- As for the causes of collective redundancy, it was indicated that the economic causes are given if the measures proposed by the company contributed to its overcoming the company's negative situation. If the alleged causes were technical, organizational or production based, the measures should contribute to ensuring the company's future viability and employment in the same via a more appropriate resource organization.
- In the case of individual dismissal, in addition to these causes, the business owner may terminate the worker for inadequacy, lack of adaptation to the work position, and justified but repeated lack of attendance, always when this absenteeism had certain repercussions in the company. In all cases, as we shall see, legislation has introduced modifications over the past years.
- Regarding the individual dismissal, advance notice of thirty days is required, as of the written communication and the availability of the corresponding compensation.
- In both cases, compensation is calculated at twenty times the worker's daily salary per year of company service. In the case of a failure to respect the procedure, the legal consequences include the invalidation of the termination decision. Therefore, the business owner is obligated to readmit the workers.
- In individual dismissals, the general rule is that if the judicial body does not find the cause of the dismissal to be proven, the termination is declared unfair. In this case, the compensation to be paid by the employer was of 45 days of salary per year of service, with a duration limit of 42 months. Only in specific cases may invalidation be declared (protection of fundamental rights or some other causes related to maternity and family). As a special regulation, since 1997 and as result of an agreement of the social agents, there is the so-called "Contract for Encouraging Indefinite Hiring", initially directed at workers having job placement difficulties. The main characteristic –apart from public bonuses– was the reduction of the improper dismissal compensation of 33 days of salary per year, with a limit of twenty four months. This decreased compensation was only applicable in the case in which the dismissal was based on objective termination causes, but not in the case in which the unfair dismissal was initiated due to disciplinary causes. In some cases, another amount must be added to this quantity, corresponding to the salaries that were not received since the date of the dismissal until the notification of the court judgment.
- In practice however, the most frequently used channel for dismissals was the so-called "express dismissal" (*despido exprés*). In 2002, the possibility of avoiding the second part of the

[7] In this regard, we should consider the recent Judgment of the Court of Justice of the European Union (Fifth Chamber) of 13 May 2015 (Case C-392/13), that concludes "Article 1(1)(a) of Council Directive 98/59/EC of 20 July 1998 on the approximation of the laws of the Member States relating to collective redundancies must be interpreted as precluding national legislation that introduces the undertaking and not the establishment as the sole reference unit, where the effect of the application of that criterion is to preclude the information and consultation procedure provided for in Articles 2 to 4 of that directive, when the dismissals in question would have been considered 'collective redundancies', under the definition in Article 1(1)(a) of that directive, had the establishment been used as the reference unit".

compensation (the so-called "salarios de tramitación", procedural salary) was introduced. Specifically, this may not be accrued based on a deposit (or worker payment) of the corresponding compensation. If this deposit was made over the first 48 hours, there was no generated entitlement to any quantity. Given the normal delays occurring in the process, and although the State returned these quantities to the company after sixty working days, this amount often exceeded the amount corresponding to the compensation for loss of employment. Therefore, in 2010, approximately sixty five percent of all indefinite contract holders who were eligible for unemployment benefits[8] lost their employment in this manner. Thus, the most typical manner of dismissing workers was by recognizing the unfair nature of the dismissal, with the payment of compensation of 33 or 45 days of salary per year of service. The employer thereby tended to opt for a certain cost, preventing the risk of indefinite legal processes; furthermore, by assuming the unfair nature of the dismissal from the beginning, often it was considered to be a disciplinary dismissal, as in this case there was no legal obligation to advise the worker, making the decision immediate, with the resulting cost savings.

This set of regulations, applicable to all types of contracts, follows the same rules as those established for temporary hiring. These are formally causal, and may be caused by structural causes related to company production (for a specific work or service or in response to a special work quantity need–the so-called temporary contract), for the need to substitute interim employees. Although there are more instruments in legislation (such as training contracts), the three mentioned instruments make up approximately 98% of the temporary contracts that are registered in Spain, which may be omitted for the purposes of this work.

In 2010, before the start of the crisis reforms, no maximum period was established for contracts for a specific project or service, and in the case of the temporary contract for production circumstances, art. 15 of the Worker's Statute established it at six months, although it could be carried out over the 12 months following the initiation of the alleged cause of the temporary hiring. In various cases, collective negotiation had a specific action period; in the first, to determine what activities could be covered by the same, and in the second, to extend the periods of duration (up to twelve months) as well as reference. The formal requirements for terminating a temporary contract are certainly reduced; it is only necessary to offer advance notice of 15 days when the working relation has extended for over one year.

These types of temporary contracts represent some 80% of all recorded contracts– with no major changes having occurred in different moments of the economic cycle– leading us to believe that, in large part, they might be being used improperly. Thus, in response to these situations, in 2001 compensation was established for the termination of these contracts, equaling eight days of wages per year worked. In the case of the provisional contract, as well as training contracts, the law does not consider it necessary to introduce this penalization.

Despite the suspicion of the existence of a high level of fraud or at least, of improper use of these temporary contracts, neither the administrative nor the judicial channels have reported increased rates of litigation. As for the former, the extension of problem may hinder its control. Regarding the scarce judicial sentences regarding the indefinite nature of temporary relations, the explanation for this may be found in the relationship between worker risks and benefits. Given that the employer is not obligated to readmit the worker who was incorrectly contracted as a temporary employee; it is most likely that they shall simply receive the corresponding compensation, which will be little given their short tenure.

In practice, the greatest limitation of recurrent temporary hiring is probably the automatic conversion of indefinite contracts of employees hired two or more times by a company once the total reaches twenty four months out of a thirty month period. This rule, introduced in 2006, does not prevent increased temporary contracting, but it does prevent employees from remaining in situations of permanent precariousness.

[8] They are almost the entirety. The only others are those workers that do not request the benefits (due to finding other employment or for other reasons) and those who have not accrued this right due to not having been employed for sufficient time.

2. The great reforms of the crisis and their context

According to the previous section, it can be deduced that, in regards to dismissal and redundancies costs, the labor relations system continues to follow the same logic regardless of the contract type. Thus, we can easily compare the elements described by the OECD in its index. On the one hand, business owners should offer compensation that is always calculated in compliance with the same scheme; employee service time with the company is multiplied by the value of the daily salary of the same. This amount is multiplied by a different module, depending on whether the employee contract is temporary or indefinite, and within these, in accordance with the appropriateness or inappropriateness of the dismissal.

A series of costs must be added to this amount. In some cases, they are quite simple to quantify (such as advance notice or the following of a specific procedure), but, in other cases, they are not so clear (such as process risk, based on its duration and due to the scope of the judgment). Furthermore, over recent years, there has been an increase in some of the payments to be made by companies in the case of collective redundancy, although, according to legislative technique, this increase is not necessarily appropriate.

To put the reforms into context (and also, therefore, their assessment), it is useful to look at some relevant data from the Spanish labor market. In 2007, Spain reached its lowest unemployment rate since 1979, at 7.93%, having historically high maximum employment levels, with over 20 million job positions. At this time, three out of every ten salaried employees were temporary and fourteen percent of these were in the construction sector. On a broader scale, in the European Union, unemployment rates were similar (7.1%) but temporary contracts (14.6%) and the construction sector weight (8.4%) were substantially lower. Only three years later, at the start of 2010, some 2.1 million jobs had been lost, the unemployment rate neared 19% and the construction sector only made up 8.4% of all employment. The temporary contract rate had fallen to 24.2%, unheard levels in Spain since the late 1980s.

In 2010 the government of Rodríguez Zapatero, supported by the social democratic party (PSOE), initiated a labor reform process, consisting of several laws that were approved over this year and the following year. Regarding the costs of dismissals, it should be noted that the first of the objectives declared by the government[9] were to reduce duality. The hypothesis suggested that excessive temporary contracting is caused by the difference in termination costs between the permanent and temporary contracts. Thus, it acted directly on the compensation costs, progressively increasing the factor that determines compensation in the temporary contracts and immediately reducing–with certain nuances– those corresponding to the indefinite contracts. For this, it opted to notably increase the collective of workers receiving a Contract to Promote Indefinite Hiring, and at the same time, some of the compensation for the dismissal of indefinite employees hired following the reform was subsidized by the Wage Guarantee Fund[10].

The reform also attempted to reduce the less clear costs incurred through different channels. On the one hand, formal defects in individual dismissal were considered to be the cause of impropriety and not of invalidation, thereby considerably decreasing risk. On the other hand, causes were modified, reformulating numerous assumptions in which the employer could legally dismiss employees. In regards to the negotiation of collective redundancies, following the parliamentary proceedings of the Government Decree,[11] it aimed to facilitate the procedure in cases of companies (or work centers) lacking legally elected representatives, and reduced the duration of the consultations. Thus, the previous minimum (thirty or fifteen days), was now a maximum.

Almost two years later, in December of 2011, Rajoy Brey took control of the Spanish government, receiving absolute majority support of the conservative party, the PP (*Partido Popular*). A few

[9] Here we refer to the Memorandum from Royal Decree Law 10/2010, of 16 June, of urgent measures for labor market reform (BOE from 17 June).

[10] This is a public organism financed by mandatory employer shares, whose main function is to ensure employees in the face of company insolvency. Traditionally, it has also financed some of the dismissals in companies with less than 25 workers.

[11] In the Spanish constitutional system, in the case of extreme cause and urgent need, the government may approve provisions having the status of a law, so-called "Decree-Law". They must be approved or rejected by the Spanish Parliament which can decide to proceed as if they were projects of the law, introducing modifications. The socialist government needed the parliamentary support of other parties, so diverse changes were made. The result was Law 35/2010, from 17 September, of urgent measures for labor market reform.

months later, an intense labor reform measure was approved, which, among many other areas, attempted to affect dismissal costs. Although it is beyond the scope of this work, it should be noted that the extensiveness of these reforms, which greatly facilitated the adoption of all sorts of measures by companies, hindered this analysis. The study of dismissal as a cost should be carried out with the understanding that at times, the employer has distinct options. For this, they shall "purchase" the most profitable option, thus the lowering of direct and indirect costs of dismissal does not necessarily generate more decisions of this type if the difficulties in adopting other relaxation measures are also reduced (restructurings, salary reductions, workday changes…).

At the time of the governmental change, unemployment rate had reached 24.2%, and the percentage of temporary contracts had decreased to 23.5%. The previous measures were either insufficient or useless. Based on the legal system adopted in the 2012 reform, it appears that the new government considered them insufficient, since essentially it expanded upon some already adopted measures. The legal causes of dismissal were reformulated in an even broader manner. Compensation for unfair dismissal was generalized to thirty three days of salary per year of service (compared to the forty five days of the general system), and was limited to twenty four monthly installments (as compared to the forty two that were applicable up to this point). Regarding the procedure, aside from the successive modifications that were made to clarify some issues presented before the courts, one of the most notable elements was the suppression of administrative authorization in collective redundancies. In practice, this meant a decreased negotiating power for the worker representation, while at the same time, approval by the administrative authority runs the risk of being subject to political interests.

3. Costs associated with individual dismissals

The decision to terminate is ultimately an economic decision. Aside from irrational attitudes, it may be assumed that an employer shall terminate his/her relationship with an employee once it is profitable to do so. On the one hand, the general rule is that dismissal should be individual. Over the last eight years, the weight of these individual dismissals has led to indefinite workers receiving unemployment benefits in some 80% of the cases of these terminations. In Figure 3 we see that not even during the worst moments of the recession were collective dismissals the majority. Over forty percent of all workers are employed in companies having less than fifty employees, while an additional twenty percent work in companies with less than 250 workers. Therefore, staff reductions are often carried out little by little, as inevitably the companies can do without some workers. Therefore, it is difficult to reach the necessary thresholds in order for the dismissals to be collective, which are calculated in ninety day intervals. Therefore, the cost of individual terminations is quite relevant from a quantitative perspective. In the OECD index, to which we have made reference, it has a weight of 71 percent (5/7).

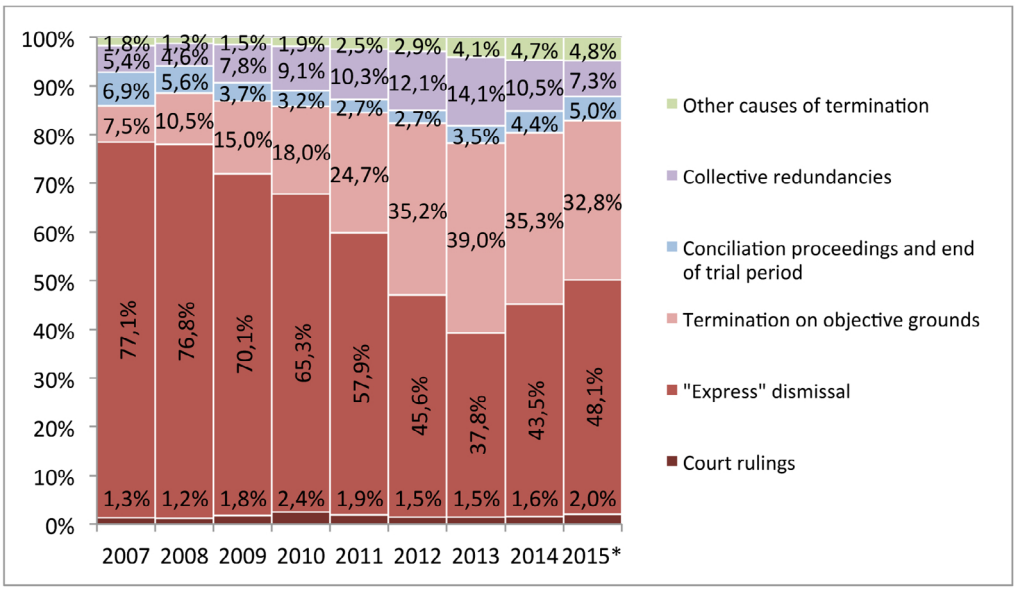
Following the order proposed by this institution, the first element that should be considered is that of the so-called procedural inconvenience, including "notification procedures" and the "delay involved before notice can start". In general, the Worker's Statute (art. 53) demands written notice to the worker, an element that is common in many countries.

The importance of this notice is not negligible; other than the fact that the notice period runs from that moment (there is, therefore, no delay), in an eventual judicial appeal, the acts included in this document are the only ones that may be alleged by the business owner in his defense. Along with this notice, the law requests the availability of employee compensation based on their salary and time of service with the company. This payment or its availability serves as a legal requirement of the dismissal except when the cause is "economic" and a lack of liquidity has been proven. Thus, the mere lack of cash in the company is not sufficient justification if the alleged cause is not "economic" but rather, is "technical, organizational or production-based". And even when the cause is economic, if payment measures are available for (such as a credit policy[12]), this payment or availability of the corresponding employee compensation is imperative. Thus, relative dismissal cost is added to the company's financial manage-

ment. The employer may not prioritize certain payments over others, except when having the means to do so and they should pay the compensation to ensure that the dismissal is fair. Therefore the fact that the failure to pay subsequent debts may have serious consequences on the company and the employment that it generates is irrelevant. Company fears that a provider may fail to service them or that there is risk of realization of essential assets for the company operation, are not sufficient causes for considering employer failure to deposit the owed compensation as fair.

However, in one of the recent reforms, there has been a major resulting cost reduction, albeit indirectly. Until the reform of 2010, the formal defects meant the invalidation of the dismissal, whereby an inadequate expression of causes or an inexcusable error in the compensation amount could result in mandatory employee readmission with the corresponding payment of missed salaries. However, as of this year, it only results in an unfair dismissal, with the employer deciding whether to pay the compensation or to assume a greater debt with the employee.

Figure 3: New unemployment benefit recipients losing a permanent job, by cause of termination.



Source: Spanish Ministry of Employment and Social Security.

The second group of costs included by the OECD is related to compensation and duration of the notice period. Unlike that which occurred previously (until 1994[13]), Spanish law does not differentiate the notice period based on the worker's tenure with the company. In all cases, fifteen days must pass between the date of notification and the execution of the same. Once again, here these recent reforms have cheapened dismissals, as before 2010, the required period was double this amount. Regardless, it should be noted that this period may be replaced by the payment of the corresponding salaries, thus it often serves as a mere fifteen day increase of the compensation payment. As for the compensation, it has already been suggested that this is calculated by multiplying the daily salary by twenty and the years of the employee's service to the company. The determination of each of these factors has led to numerous legal problems, which have been resolved by case law. Thus, the fact that the daily salary was calculated as the ratio of annual retribution divided by 365 or 366[14], the inclusion in this calculation of complementary payment or irregular or salary accrual payments and the use of stock options as benefits[15] all

[13] Law 11/1994, of 19 May, modifying specific articles of the Worker's Statute and of the text included in the Labor Protection Act and the Law on Social Oder Infractions and Fines, BOE from 23 May.

[14] Judgments of the Spanish Supreme Court from 27 October 2005 (Rº 2531/04), 30 June 2008 (Rº 2639/2007) and 24 January 2011 (Rº 2018/2010).

[15] Judgments of the Spanish Supreme Court from 1 October 2002 (Rº 1309/2001), 26 January 2006 (Rº. 3813/2004), 3 June 2008 (Rº 2532/2006).

served to complicate the calculation of the first factor. The inclusion of previous temporary contracts to the indefinite[16] or business subrogation[17] type, or the assessment of the periods of leave all hindered the estimation of the second. These issues are not particularly relevant if they merely alter the amount of the employer debt with the employee. However, as previously suggested, the non-excusable error–and not those issues that have already been resolved by the Supreme Court[18]– in the calculation of compensation that is recognized at the time of the notification, determines the qualification of the dismissal as unfair. Therefore, given the technical complexity of the compensation calculation, the need for appropriation suggests a source of judicial uncertainty and additional cost, which may increase the compensation.

The third and final group referred to in the OECD is the difficulty of dismissal. Here, there are a series of heterogeneous concepts that are related only in an indirect manner.

First, there is the definition of the causes justifying the dismissal. In Spanish law, this is a closed set of assumptions and not the mere "reasonableness" of the business measure. This is one of the areas where the 2012 reform suggested a major change. These are some specific causes of individual dismissals, and in the next section we shall present the economic, technical organizational and production-based causes that are common in collective redundancies. The first alleged employer cause is that of unexpected inadequacy (in its existence or in its knowledge), which may refer to the physical capacities of the worker or the legal ones, as in the case of a loss of licenses.

There is an even greater interest in the lack of worker adaptation to technical modifications in the work position. In this case, it has traditionally been demanded that two months pass from the time of the introduction of the change, thus there is an implicit delay before notice can begin, with no proof of the impossibility of adapting to said moment. Along with this delay, the 2012 reforms added another additional cost, obliging the employer to offer employees a course to facilitate their adaptation. Apart from the cost of the same being covered by the company and the fact that the employer continues to receive his/her salary during the course period, without providing services, this implies an additional delay in the effectiveness of the dismissal.

To fight absenteeism, Spanish legislation has traditionally permitted the dismissal of an employee even for justified and intermittent absences, when this represents a real problem in the company. The specification of these two levels of "relevance" of absenteeism were made towards the end of the last reforms established in compliance with objective parameters that in practice, made its application difficult: 20 percent of the working days in two consecutive months or 25 percent in four months within a one year period; at the same time, in order for these absences to be considered sufficient cause, the absenteeism in the work center must have reached five percent during the same reference period. Given that the average absenteeism in Spain is only slightly higher than three percent, this additional condition is a notable restriction on the effectiveness of this cause of dismissal. Thus, in order to strengthen employer powers, in 2010, there was a reduction in the required percentage of absenteeism in the work center to only two and a half percent. Finally, in the 2012 reform, this requirement was suppressed, but it was made stricter in regards to employees. Thus, currently, it is irrelevant if the work center has a real absenteeism problem or not, in order for the worker to be dismissed, the intermittent absences, although justified, should simultaneously reach twenty percent in two months and five percent in the two previous months. This last demand, however, is not added to the assumption that the reference should be four alternate months within a period of twelve months.

The second element within this third group is the duration of the trial period. In Spanish law, this has been left to the will of the parties–always having to be agreed upon in writing before beginning the contract– within the limits established by the collective redundancy. When the collective agreement is silent in regards to this area, its maximum duration shall be six months for degree holding technical workers and two months for the other workers (three months in companies with less than twenty five employees). According to the most recent data available (2013), 47.47 percent of the workers covered

[16] STS of 15 November 2007, Rº3344/2006.

[17] For example, the failure to include the previous company in tenure in a case of business subrogation, STS of 15 April 2011, Rº 3726/2010.

[18] Such as, for example, STS from 6 May 2014 on the manner of calculating the tenure of the worker in regards to prior periods of less than a month; despite the fact that the error generates a relatively small difference, this is considered to be inexcusable.

by collective agreements have a specific arrangement; however, it should be noted that a decrease in duration is more frequent than an extension in the collective agreements. Thus, in only 23.5 percent of the workers covered by collective agreements in 2013 was the trial period longer.

It is clear that termination during the trial period has virtually no cost; to terminate a contract, it is not even necessary to have any specific procedure or cause and it is not necessary to pay any compensation; employer risks are minimal as challenging is only possible when there has been some infringement of fundamental rights[19]. Furthermore, the effects are immediate and there are no limitations of any sort. Thus, one of the clearest goals of the 2012 labor reform is the attempt to reduce costs. This created the "indefinite contract supporting entrepreneurs". Despite its name, it is aimed at strengthening employment in SMEs and it does not in fact attend to the direct or indirect creation of new activities, but only to the size of the company (less than 50 workers). The only peculiarity of the legal system regarding this contract is the duration of the trial period, which is "one year, in all cases". Despite establishing the possibility of requesting bonuses related to employee permanence, this modality has been used infrequently. Only 11.8% ofall indefinite contracts used this channel, suggesting that the extensive trial period is not a relevant element affecting permanent hiring.

The next element included in the OECD index relates to the consequences of unfair dismissal. As previously suggested, compensation is increased by thirteen days of the salary per year of company tenure, for a total of 33 days, and a maximum of two years. This is the compensation that, since 1997 was recognized only by the Contract to Promote Indefinite Hiring and that today extends to all workers. The direct costs of unfair dismissals have been greatly reduced from forty five days per year and a maximum of forty two monthly installments to the previously mentioned figures. But furthermore, procedural salaries have been suppressed, except in case of readmission, since either the employer or the employee decides to do so.

Thus, in practice, readmission is considered to be a clearly exceptional event, only being mandatory in the case in which the dismissal infringes upon the fundamental rights or other especially protected rights. Thus, in the case in which the worker who is dismissed without sufficient cause or without respect for the procedures is pregnant (even if the employer ignores this) or is receiving or has received certain parenthood benefits, the dismissal is considered null and readmission is thereby mandatory.

In the case in which a legal worker representative is dismissed, the unfair dismissal costs increase notably, since in addition to the need to pay the salaries that have not been received since the time of notification of the ruling, the option between readmission and compensation corresponds to this individual.

Finally, to end the discussion of the elements considered for this index on dismissal costs, we shall make reference to the challenge period against this dismissal. In this case, changes have not occurred, as it was already clearly reduced. The challenge should be made by the employee within a period of 20 working days (excluding Saturdays, Sundays and holidays), a period that is suspended when the mandatory preliminary conciliation is processed.

Along with this element, it is necessary to include as a cost the time passing until receiving a response from the judicial body. Apart from the duration of the process which means the payment of attorney fees and dedicating resources to the legal defense, uncertainty is a relevant factor. For this, it is necessary to highlight that even though no change in regulations has been produced, the average duration of the dismissal process has notably increased over recent years. In compliance with the Annual Report of the General Council of the Judiciary, until 2008 the dismissals were resolved in less than three months. This duration grew slowly until 3.8 months in 2011, but in the last two years (until 2013) it has extended to 6.5 months. On the other hand, it should be noted that only five percent of the judgments are altered by higher courts. Therefore, adding together all of the procedures, the average time passing since the dismissal until the court decision is approximately eight months.

We should mention another distorting element introduced by the latest reforms. Until 2012, the Worker's Statute established the possibility of the employer recognizing the unfair nature of the dismissal at the time of its communication. As this prevented the generation of procedural salaries, it became a

[19] Such as, for example, the notification to the employee of her failure to pass the trial period, when evidence suggests that this was due to her pregnancy (STSJ of Madrid from 20 May of 2008 (Rº 1170/2008)

frequent practice. The elimination of said compensation also meant not mentioning this possibility in the law. On the other hand, compensation for this dismissal is exempt from employee taxation until the time established by the law. Therefore, the Tax Authority interpreted that the employer acting in this manner, without legal support, is recognizing a compensation that is greater than the legal one. This is permitted, however, the difference is considered to be work output for fiscal purposes. Therefore, artificial costs were added, since the company and the dismissed employee were forced to stage a reconciliation act when there was no disagreement since the beginning. Thus, in 2013 there were 66 percent more preliminary conciliations than in 2011.

On the other hand, although it may be superficial, it is necessary to mention the legal system of disciplinary dismissal. The OECD excluded it from its index precisely because it is more agile[20], yet, when it may be unfair, it should not be ignored. Thus, except in the case of a worker representative or when establishing a collective agreement, it should be sufficient to notify the worker regarding the acts motivating the dismissal and their date of effectiveness. If there was labor union affiliation, union representatives should be heard. The dismissal has no notice whatsoever, so if the employer intends to recognize its unfair nature, it would be advantageous to classify it as disciplinary.

4. Collective redundancies and business costs

The definition of collective redundancy–which is the first element used in the OECD index–, as described in the first section, is an adaptation of Community law. Its qualifying element is that it affects a specific number of workers: ten in a company of up to one hundred workers, ten percent for companies between one and three hundred workers and thirty workers in larger companies. In order to prevent that through continuous individual dismissals the more demanding regulation of collective redundancies is avoided, two corrections are made. On the one hand, all of the dismissals that are made in a ninety day period (and eventually more) are taken into account and on the other hand, always when it is less than five, it should also include "terminations of an employment contract which occur on the employer's initiative for one or more reasons not related to the individual workers concerned".

To complete the definition of collective redundancy, it is necessary to analyze the causes leading to it. Here, the efforts made by the law to reduce dismissal costs have been notable. The objective declared in both the 2010 and 2012 reform, was to improve the legal certainty. So, it seeks to facilitate the terminations and to reduce the role of legal bodies. Thus, in the first, the measures were considered acceptable when the causes were deduced as "the reasonableness of the termination decision". This reasonableness, when involving decreases in income or the existence of losses (current or anticipated) was linked to the preservation or favoring of its competitive position. In the other causes, the goal of the dismissals was to "contribute to preventing a negative evolution of the company or to improving the situation of the same through a more appropriate organization of resources that favors its competitive position in the market or an improved response to market demands".

This definition, according to the government elected at the end of 2011, gave an excessive role to the jurisdictional bodies, allowing them to evaluate whether or not the business decision was "reasonable", which is beyond legal scope. Thus, the current definition aims to establish strictly objective parameters. In the regulations, it is the economic situation that permits the dismissal, not the appropriateness of the measures used to fight them; furthermore, any assessment capacity of the judge is eliminated when there are three consecutive months of decreased sales or income (as compared to the same period from the previous year). As for the other cases, likewise, only the current and real situation is described so that, in the present definition, there is no reference made to the anticipated effects of the dismissals on the financial situation or competitiveness of the company.

The second and third elements of this index on the restriction of collective redundancies refer, respectively, to communications and delays made by the employer when making the decision to terminate until this dismissal goes into effect.

[20] OECD, *OECD Employment Outlook 2013.* (Paris: Organization for Economic Cooperation & Development, 2013), 76.

Current regulation has aimed to grant legal certainty to the procedure, establishing clear criteria of who, what and how the negotiation should be carried out. So, after some problems in the interpretation of the rule, in August of 2013, it was clarified that the negotiation should take place in a unique negotiating commission (and not in work centers)[21]. The manner by which this commission is created was precisely regulated, as well as the fact that it is made up of both legal representatives from each work center, when relevant, as well as those designated (or delegated) by the workers when there are no select representation bodies. As shall be described later, the very existence of multiple labor reforms has meant a non-negligible cost, given the lack of legal certainty in the negotiation procedure which has provoked the declaration of invalidation of various collective redundancies.

Focusing on the duration of the proceedings, it has been established that its duration should be no longer than thirty calendar days, or fifteen days in the case of companies having less than fifty workers. However, before the start of the same, it is necessary that a worker representative commission has been created. This should be carried out within a maximum period of seven days if there were legal representatives in all of the affected centers, or within fifteen days if the designation of ad hoc representatives is necessary.

The obligation to negotiate in good faith has been revealed as a major source of company costs. Before the almost absolute flexibility of the causes of the dismissal, the judicial bodies have greatly increased the requirements for this point. Thus, if the court considers that this good faith has been violated, the entire process may be annulled, having to start over (if the company decides to do so), readmitting the employees during the meanwhile. For example, having separated a specific union from a referendum between workers to ratify the agreement[22], or the infringement of the right to strike during negotiation[23].

Although agreement or subsequent authorization by any public authority is not required, the labor authority does intervene, making warnings and recommendations or assisting if any party so requests. In any case, it should be noted that although the percentage of dismissal processes with agreement has lowered since the elimination of administrative authorization in 2012, in eight out of ten cases, agreement is reached with the worker representatives.

Having completed the consultation procedure, in which a list of documentation has been established, as considered minimal by the case law, the company has fifteen days to notify of its decision. As of this time, the employer may individually notify the workers of the dismissal, which may not take place before thirty days as of the date of communication to the labor authority of the start of the procedure. Furthermore, the formal aspects of the individual dismissals should be respected as previously noted, including the fifteen days of notice.

Thus, the delay occurring between the company decision to initiate the procedure and the occurrence of the same may range between thirty one (if the negotiating commission is created immediately and agreement is reached within fifteen days) and sixty days, if all of the periods take the maximum amount of time. The present agreement therefore, offers clear cost savings, as it not only shortens the process but also offers legal certainty to the decision, by preventing challenges against the oexistence of legal causes except in clearly exceptional cases.

The final item used in the index is the so-called "Other special costs to employers in case of collective dismissals". Here, it is surprising to see that over recent years, the trend has been to increase these, going against the general dynamic. Aside from some immaterial or difficult to assess items, such as impact on corporate image or cost of uncertainty, three additional costs may be supported by companies. Each of these has a great complexity and requires a specific analysis; therefore here we shall simply discuss their main features.

[21] In fact, the regulation of development of the previous law provided negotiation by work center. Case law considers that this regulation was illegal and annulled dismissals for not having created a unique commission (SAN (*Sentencia de la Audiencia Nacional*): Judgment of the Spanish National High Court (plural SSAN) from 1 and 4 June of 2013 (Proc. 17/2013 and 1/2013, respectively).

[22] Atento case, SAN of 11 November 2014 (Proc. 251/2014).

[23] Coca Cola Iberian Partners case, STS from 20 April 2015, in this case, the strike coincided with the negotiation period with one of the plants affected by the dismissal. The company moved production to other manufacturing plants to cover area demand.

First, and the oldest of the extra costs arises when there are employees over the age of 55 in the dismissals, obligating the company to sign a special agreement with the Social Security administration, ensuring the sufficiency of their pensions when reaching the corresponding age. As the payment amount is related to the age of early retirement, reforms in this area have indirectly impacted dismissal costs. By extending the age of retirement to 67 years (progressively), this also increases the cost of this agreement for the company.

Second, when the dismissal affects over fifty workers, the company should be responsible for an external relocation plan. This plan must extend for a period of at least six months and should include training and requalification measures. To some extent, this allows for the company (and not the general public) to take up some of the costs that are generated from the creation of new unemployed individuals.

Finally, and having a similar purpose, in 2011, in response to the collective dismissal of a large telecommunications company that had earned large profits, the company was obligated to make a contribution to the Public Treasury when this dismissal affected workers of over the age of fifty. Following some variation, the final determination of this obligation was limited to companies having profits with over one hundred employees in which the proportion of dismissed employees of over fifty years of age is greater than the percentage of workers of that age remaining in the company.

The notion of a company with profits has been surprising as it includes not only the fiscal year in which the dismissal was executed and the previous year, but also the four subsequent years, requiring that the positive results occurred in at least two consecutive years. The cost of this measure is quantified based on the imbalance of the proportion of workers over the age of fifty and the profits ratio. These elements are used to determine the coefficient by which the cost of the unemployment benefits must be multiplied.

5. Some final thoughts: dismissal cost and business strategy

Over recent years, dismissal costs have been the subject of great debate; recently, the International Monetary Fund, in its annual report on Spain from Article IV once again suggested the problem of duality and its relationship with this area. Aside from the multiple criticisms that may be made of simplistic analyses such as those suggested by experts from this institution, inefficiencies clearly exist. This is not a problem of excessive costs or rigidness. Figure 1, at the beginning of this work, clearly reveals that rigidness has not only seriously decreased over recent years, but is also lower than many of the large European economic powers such as France or Germany. The issue lies in the incentives offered by the system.

The Spanish legal system believes that hiring should be indefinite and that dismissals should be based on cause. In practice however, employers often fail to consider the reasons established by the law when hiring for a limited amount of time or when making dismissals.

To clearly understand this issue, it should be noted that in the cost of dismissals, there are essentially two elements. On the one hand, there is the compensation that should be paid directly by the company to the employee. On the other hand, there is a series of more or less defined economic costs that the business should incur.

In the termination of a temporary contract, the formal will of the parties is not required. There simply must be compliance with the original purpose of the contract. As described in the first section, since 2015, compensation shall be of 12 days of salary per year of service, with no further restrictions. As previously described, the extensive use of service and temporary contracts leads to the conclusion that temporary contracts are not limited to the scenarios envisaged by the law. In fact, during the economic recession, the destruction of employment focused on temporary contracts, given that its function in companies tends to be a fast and procedure-less staff adjustment to market needs.

Thus the employer decision may be summarized based on three options. They may hire a temporary worker (or various, successively). They may hire a permanent worker and when this employee is no longer necessary, comply with all of the procedures to carry out an objective (justified) dismissal. And finally, they may ignore the legal procedure by carrying out an unfair dismissal.

The difference in compensation is not very great between these three options, with the employer paying twelve, twenty or thirty three days per year of worker service. For five years of company service,

they must pay sixty days of the temporary worker's salary (or successive workers), one hundred days of the indefinite worker's salary when they are correctly dismissed and one hundred and sixty five days of the unfairly dismissed worker's salary. In the first two cases, it is necessary to provide (or pay for) the corresponding period of notice.

But furthermore, in the case of legally established dismissals, the series of costs described in this study must also be paid. To these, it is necessary to also add the risk that despite having attempted to comply with all of these procedures, the dismissal shall be considered unfair or in worse case, may be ruled invalid. Thus, the anticipated cost of the dismissal shall be the sum of the compensation, the procedural costs, and the delay in the execution of the measure, plus the probability of paying compensation for an unfair dismissal.

If the employer opts to breach these regulations, there are two possibilities. The first is to renounce stable workers and to use temporary contracts from the get-go. This results in very low termination costs, given that compensation is quite low and the procedure is virtually inexistent. Theoretically, there is the risk that the worker may sue for unfair dismissal, alleging fraud based on the temporary hiring. However, given the short duration of these contracts, it is not likely that the worker shall sue for a few euros, in the hope of a new contract or at least some good work references. On the other hand, employers using this strategy shall have workers who are not overly experienced or committed in their work positions. So they should only act in this way if the employment positions require limited learning and if there are sufficient workers to cover their needs.

The second inappropriate alternative is to hire permanently but, as soon as the worker is no longer necessary, renounce justified termination. Here, there is legality at a very low cost. Formalizing the termination as a disciplinary dismissal and recognizing the unfair nature of this, the dismissal cost increases by thirteen days per year of service, but this prevents the notice and justification of cause requirements and the uncertainty regarding the judgment.

Ultimately, it is necessary to reform the system of dismissal costs, but the problem does not lie in the compensation level or rigidness, which it not excessively high, or in the number of types of work contracts. The problem stems from the cost differences for the different behaviors. Legislation is actually resulting in the support of less profitable behavior. Furthermore, constant legislative changes occurring with these frequent reforms, has led to legal uncertainty, which in itself is a cost.

Indeed, there has been an attempt to decrease the difference between termination costs for temporary and indefinite contracts. The occurrence of the causes of termination has been facilitated and the cost of collective redundancies has been reduced; procedural salaries have also been eliminated in order to reduce the risks associated with the challenges, increasing compensation for terminating a temporary contract. However, the difference continues to be excessive, as seen in the hiring data, with a lack of effective channels. Therefore, it is necessary to consider this topic from a new perspective, searching for improved techniques and using a broader consensus. The reform should not only be positive, it should also be stable. Various alternatives have been suggested, with their respective advantages and disadvantages, but their analysis extends beyond the scope of this study.