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This Survey is published on the responsibility of the Economic and Development Review Committee of the OECD, which is charged with the examination of the economic situation of member countries.

The economic situation and policies of Poland were reviewed by the Committee on 6 February 2014. The draft report was then revised in the light of the discussions and given final approval as the agreed report of the whole Committee on 21 February 2014.

The Secretariat's draft report was prepared for the Committee by Hervé Boulhol, Antoine Goujard and Balazs Égert under the supervision of Peter Jarrett. Research assistance was provided by Patrizio Sicari.

The previous Survey of Poland was issued in March 2012.

Basic statistics of Poland, 2012

Numbers in parentheses refer to the OECD average[a]

LAND, PEOPLE AND ELECTORAL CYCLE

Population (millions)	38.5		Population density per km^2	123.2	(34.5)
Under 15 (%)	15.1	(18.1)	Life expectancy (years)[b]	76.9	(80.0)
Over 65 (%)	14.0	(15.3)	Men	72.7	(77.3)
Foreign-born (%, 2011)	1.8		Women	81.1	(82.8)
Latest 5-year average growth (%)	0.2	(0.5)	Latest general election	October	2011

ECONOMY

Gross domestic product (GDP)			Value added shares (%)[b]		
In current prices (billion USD)	490.5		Primary	3.9	(2.5)
In current prices (billion PLN)	1 594.4		Industry including construction	32.5	(27.4)
Latest 5-year average real growth (%)	3.4	(0.6)	Services	63.6	(70.1)
Per capita, PPP (thousand USD)	22.2	(37.1)			

GENERAL GOVERNMENT[b]

Per cent of GDP

Expenditure	42.3	(42.8)	Gross financial debt	62.4	(102.4)
Revenue	38.4	(36.4)	Net financial debt	33.6	(64.0)

EXTERNAL ACCOUNTS

Exchange rate (PLN per USD)	3.251		Main exports (% of total merchandise exports)		
PPP exchange rate (USA = 1)	1.868		Machinery and transport equipment	37.8	
In per cent of GDP			Manufactured goods	21.0	
Exports of goods and services	46.7	(53.8)	Miscellaneous manufactured articles	12.4	
Imports of goods and services	46.3	(50.4)	Main imports (% of total merchandise imports)		
Current account balance	-3.7	(-0.5)	Machinery and transport equipment	32.0	
Net international investment position	-66.6		Manufactured goods	17.2	
			Chemicals and related materials, n.e.s.	13.8	

LABOUR MARKET, SKILLS AND INNOVATION

Employment rate (%) for 15-64 year olds	59.7	(65.0)	Unemployment rate, LFS basis (15 and over) (%)	10.1	(7.9)
Men	66.3	(73.1)	Youth (15-24) (%)	26.5	(16.2)
Women	53.1	(57.0)	Long-term unemployed (1 year and over) (%)	3.5	(2.7)
Participation rate (%) for 15-64 year olds	66.5	(72.6)	Tertiary educational attainment 25-64 year-olds (%)[b]	24.5	(31.5)
Average hours worked per year	1 929	(1 769)	Gross domestic expenditure on R&D (2011) (% of GDP)	0.8	(2.4)

ENVIRONMENT

Total primary energy supply per capita (toe)	2.5	(4.2)	CO_2 emissions from fuel combustion per capita (tonnes, 2011)	7.8	(10.2)
Renewables (%)	8.8	(8.5)	Water abstractions per capita (1000 m^3, 2011)	0.3	
Fine particulate matter concentration (urban, PM10, µg/m^3, 2010)	32.9	(20.1)	Municipal waste per capita (tonnes, 2011)	0.3	(0.5)

SOCIETY

Income inequality (Gini coefficient, 2010)	0.305	(0.304)	Education outcomes (PISA score, 2012)		
Relative poverty rate (%, 2010)	11.0	(10.9)	Reading	518	(496)
Public and private spending (% of GDP)			Mathematics	518	(494)
Health care (2011)	6.9	(9.5)	Science	526	(501)
Pensions (2009)	11.8	(8.7)	Share of women in parliament (%, December 2013)	21.8	(26.2)
Education (primary, secondary, post sec non tertiary, 2010)	3.7	(4.0)	Net official development assistance (% of GNI)	0.1	(0.4)

Better life index: *www.oecdbetterlifeindex.org*.

a) Where the OECD aggregate is not provided in the source database, a simple OECD average of latest available data is calculated where data exist for at least 29 member countries.

b) 2011 for the OECD.

Source: Calculations based on data extracted from the databases of the following organisations: OECD, International Energy Agency, World Bank, International Monetary Fund, Inter-Parliamentary Union and Narodowy Bank Polski.

Executive summary

- *Main findings*
- *Key recommendations*

Main findings

Poland's overall economic performance has been impressive over the last decade, allowing living standards to converge steadily towards the EU average. Yet, the economy slowed abruptly in 2012-13. This *Survey* focuses on making the labour market work better and strengthening product-market competition as ways to foster firms' competitiveness, overcome strong demographic headwinds and boost both short- and longer-term economic prospects. While substantial progress has been made in these areas since the nineties, important weaknesses are still restraining the country's economic potential.

Boosting employment. Despite long working hours, labour utilisation is only average due to structurally low employment. Insufficient product market competition and obstacles to internal mobility induce significant misallocation of labour resources. Employment protection is not particularly stringent, but the labour market is heavily segmented. This is likely to weigh on economic performance by limiting investment in human capital and making some specific groups bear a large share of adjustment costs. The public employment services suffer from a lack of resources and function inefficiently. Local labour offices have limited incentives to adopt best practices; the government plans to start benchmarking them. There is ample scope to tighten jobseeker obligations and reform social and tax policies to make work pay. The female employment rate is especially low, in part due to poorly designed family and pension policies.

Strengthening product market competition. Although notable progress has been made, restrictive product market regulations still hinder activity substantially. These take the form of heavy barriers to entrepreneurship and the extensive involvement of the state, even in potentially competitive sectors. Business registration procedures are cumbersome, and the bankruptcy process is lengthy and costly. Public procurement plays a key role in Poland, but public ownership may lead to non-neutrality of the bidding process, and the criteria for awarding contracts rely excessively on the lowest price. Competition is weak in network industries, apart from telecoms. The presidents of most regulatory agencies have open-ended contracts and can be dismissed by the relevant Ministry in charge of their supervision.

Macroeconomic policies. Labour cost pressures have been moderate, and consumer price inflation has fallen sharply. Given the accommodative monetary stance and a moderate impact of fiscal tightening on activity, growth is projected to pick up and surpass its potential rate by mid-2014. Inflation could move back towards the official target, and the output gap is expected to close around the start of 2016. Even though loan quality has deteriorated to some extent, prudential policies have been effective, and foreign-currency denominated loans have been curbed. Both household and corporate debt are relatively low, and the banking system is well capitalised. However, the financial system still has a considerable amount of foreign funding. The macro-prudential policy framework is being modified by the introduction of a Systemic Risk Board.

The public deficit widened unexpectedly in 2013 due to a cyclical shortfall in tax receipts and higher social expenditure and public consumption. Since EU accession, fiscal objectives spelled out in convergence programmes have often been missed, pointing to a need to strengthen the fiscal framework. Most of the 2014-15 fiscal efforts involve the change in the second-pillar pension system. Given real GDP growth dynamics, sticking to the target of 3% of GDP for the 2015 deficit so as to ensure the government debt-to-GDP ratio is firmly on a downward path would still require additional fiscal tightening.

Key recommendations

Boosting employment

- Reduce labour market dualism by: making all contracts subject to the same tax and social contribution regime as Labour-Code contracts; extending the maximum length of trial-period contracts; streamlining legal dismissal procedures; and setting a maximum cumulative duration for temporary contracts with the same firm.
- Expand the resources of public employment services to hire more skilled staff, and ensure that overall resources are better allocated to front-line placement tasks. Promote the adoption of best practices by labour offices through performance management and benchmarking.
- Tighten work availability and job-search requirements for jobseekers. Reduce passive social assistance by making more transfers conditional in part on being employed or seeking work.
- Boost female employment by: developing childcare and long-term care facilities, and pre-school education; and increasing women's retirement age at a more rapid pace than scheduled. Monitor closely the impact of the long maternity leave on the employment of mothers.

Strengthening product market competition

- Lower further the costs of entry and exit, such as cumbersome business registration. Reduce the length and cost of bankruptcy procedures.
- Pursue privatisation, and substantially reduce government ownership in competitive segments of the economy while ensuring sound governance of remaining state-owned enterprises.
- Modify public procurement practices to select the contractors offering the best value for money rather than the lowest price. Focus procurement decisions on a mix of prices and technical bid details, including environmental impact assessments. This will require enhancing staff skills to deal with complex selection criteria.
- Introduce fixed-term non-renewable mandates for the presidents of the Competition Authority and sectoral regulators during which they cannot be dismissed without fault. Create an independent regulator for water and sanitation services.

Macroeconomic policies

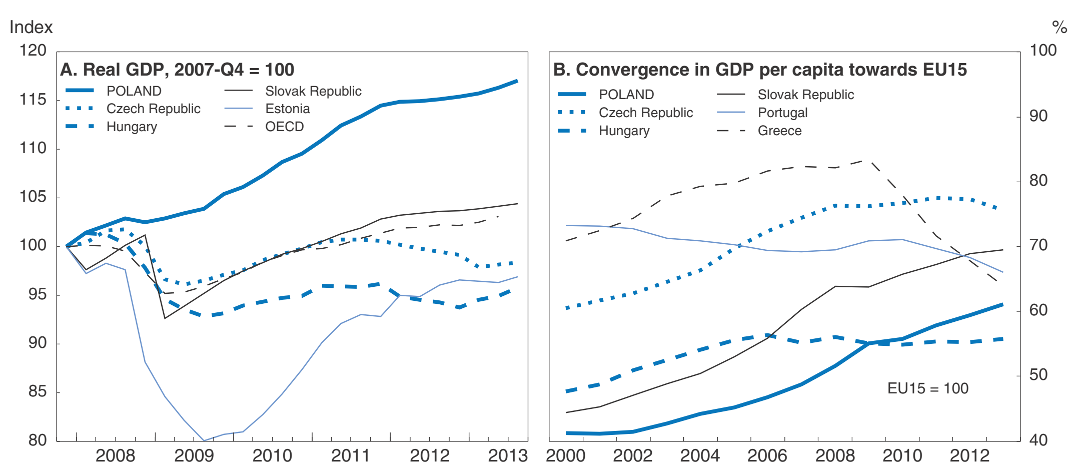
- If activity and inflation accelerate as projected by the OECD, gradually increase the official monetary policy rate.
- Ensure that the Systemic Risk Board (SRB) has the independence and power to make recommendations coupled with a "comply or explain" mechanism. Ensure a clear allocation of roles between the SRB and the current regulators; in particular, retain the ability of the financial supervision authority (KNF) to issue prudential recommendations.
- Achieve greater fiscal consolidation in 2015 than currently planned to be able to meet the below-3%-of-GDP general government deficit target.
- Create an independent institution to monitor underlying budget assumptions and fiscal performance relative to targets. Strengthen the fiscal framework by implementing detailed multi-year budgeting, basing budgets on unbiased assumptions and harmonising the domestic and Maastricht debt definitions.

Assessment and recommendations

- *The economy is projected to rebound towards potential rates*
- *Monetary and financial policy*
- *Fiscal policy*
- *Achieving sustainable and inclusive growth*

Following important reforms which have deeply transformed the structure of the economy, Poland's economic performance has been impressive since the beginning of the 2000s, allowing it to catch up steadily with the EU15 in GDP-per-capita terms (Figure 1). By 2013, the country had achieved levels of income and quality of life likely never experienced before (Piatkowski, 2013). Yet, in 2012-13 the economy slowed abruptly, and important challenges remain ahead. Boosting job prospects (Chapter 1) is critical, because employment rates are low and because the country is facing strong demographic shrinkage (Figure 2) and persistent emigration risks. In the context of rapid population ageing, improving the health-care system remains a priority, as analysed in the last *Survey* (OECD, 2012; Boulhol et al., 2012). Enhancing the business environment and strengthening product market competition (Chapter 2) are keys to maintaining a high level of competitiveness and raising medium-term economic prospects. Structural reforms in these areas are prerequisites for climbing the technological ladder, developing knowledge-based capital and becoming a more innovation-based economy. Macroeconomic imbalances are limited and policy settings appropriate for now, but fiscal consolidation should be pursued to achieve the Medium-Term Objective (MTO) of a structural deficit of 1% of GDP.

Figure 1. **Poland has outperformed other OECD countries in GDP growth outcomes**



Source: OECD, *OECD Economic Outlook 94 Database* and updates.

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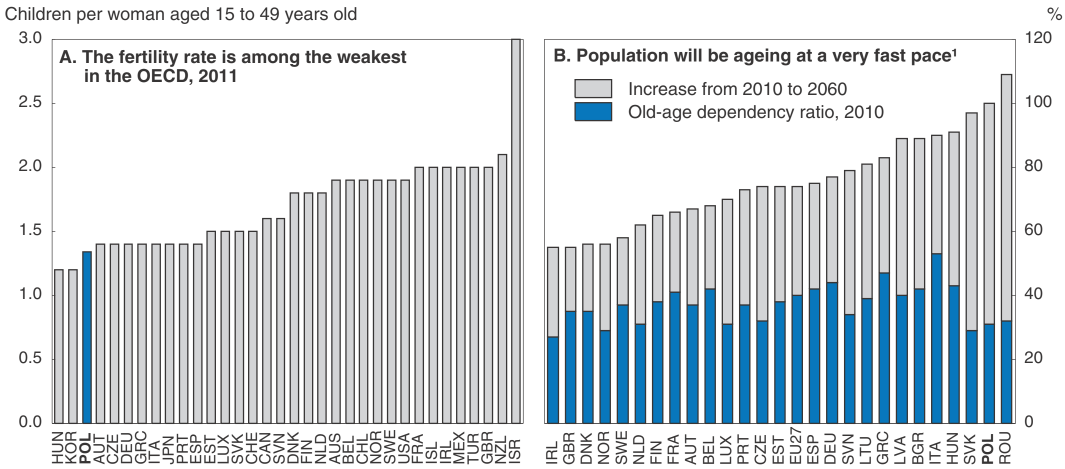
The economy is projected to rebound towards potential rates

Economic activity slowed sharply in 2012-13, with year-on-year real GDP growth plummeting from 4.8% in mid-2011 to 0.8% in early-2013 (Table 1; Figure 3, Panel A). Public investment collapsed after the 2012 construction boom generated by large road infrastructure investments, mostly financed by EU funds, and the European football championship (Figure 3, Panel B). While the absorption of EU funds remains an important driving force behind the idiosyncratic part of the Polish economic cycle, the fall in public

Figure 2. **Demographic prospects are unfavourable**



1. Effective economic old-age dependency ratio, measured as inactive population aged 65 and over as a ratio to the 20-64 employed population.

Source: OECD, *Population Statistics* and *OECD Health Indicators*; European Commission (2012), *The 2012 Ageing Report*.

StatLink http://dx.doi.org/10.1787/888932999260

investment also resulted from fiscal pressure on local governments. Such a big swing contributed to the strong growth in 2010-11 and the sharp deceleration in 2012-13. Moreover, weak external demand due to euro-area difficulties heavily penalised both exports and private investment, while rising unemployment and fiscal consolidation damped household consumption. As recommended in the 2010 *Survey*, macro policies should adequately take into account the full impacts of EU transfers and the potential imbalances they may induce. In particular, co-financing needs to be accommodated by reducing other budget lines, and a more efficient fiscal framework (see below) would help in designing and implementing the appropriate fiscal response.

Euro-area prospects have improved of late, and the Polish economy has rebounded. Given the currently accommodative monetary stance and an only moderate impact of fiscal tightening on activity, quarterly growth is projected to gain momentum and surpass its potential (annualised) rate of about 3% by the middle of 2014. Construction activity should be supported by a resurgence in EU funds but remains fragile, as sectoral bankruptcies have risen substantially. While labour market weakness still weighs on private consumption, joblessness should decline sustainably albeit slowly.

Risks to Polish growth are now broadly balanced. The most severe risks to the euro area have diminished, improving external-demand prospects, even though important risks remain. In addition, as happened in the recent past, investment and private consumption could respond strongly to swifter confidence improvements, although the extremely low household saving rate might limit the upside. Polish banks have a considerable amount of foreign funding (see below) and might be vulnerable to a delayed resolution of European banking problems. However, their strong capital positions provide some cushion against unfavourable developments. While the narrowing of the current account deficit has diminished contagion risks, Poland may be affected by emerging-market volatility through the foreign-investment channel.

A favourable competitiveness position and weak domestic demand have fuelled a sharp improvement in the external goods and services balance, which has been in surplus

Table 1. **Macroeconomic indicators and projections**

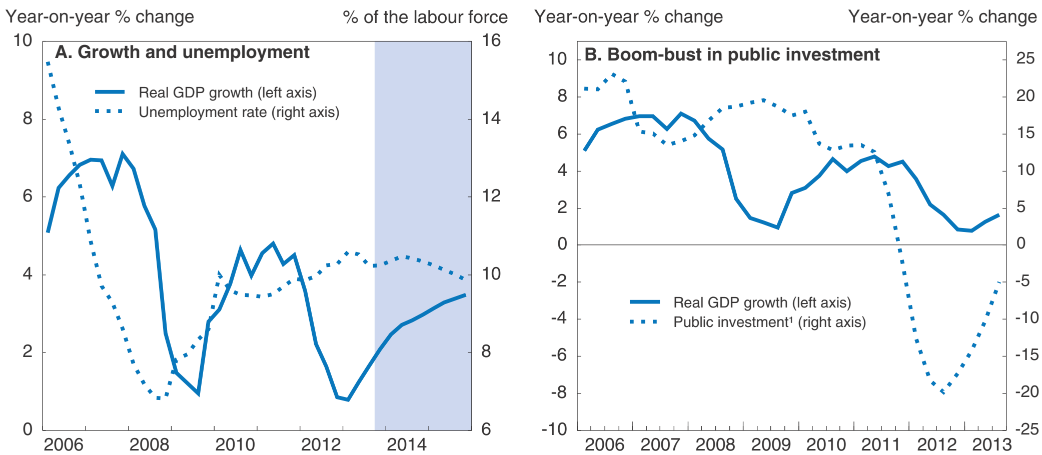
	2010	2011	2012	2013	2014	2015
	Current prices PLN billion	Percentage changes, volume (2005 prices)				
GDP	1 414.7	4.5	2.0	1.4	2.7	3.3
Private consumption	868.5	2.6	1.2	0.7	2.2	3.1
Government consumption	266..9	-1.3	0.1	2.3	1.0	1.0
Gross fixed capital formation	278.2	8.2	-1.9	-1.7	4.4	5.7
Of which: Housing	37.5	4.4	9.4	-4.9	5.6	5.2
Final domestic demand	1 413.5	3.0	0.4	0.5	2.4	3.2
Stockbuilding[1]	19.5	0.5	-0.5	-0.7	0.2	0.2
Total domestic demand	1 433.0	3.4	-0.2	-0.2	2.6	3.4
Exports of goods and services	596.7	8.4	3.3	4.7	5.0	6.3
Imports of goods and services	615.0	5.8	-1.7	1.1	4.2	6.4
Net exports[1]	-18.3	1.0	2.3	1.7	0.4	0.0
Other indicators (% change, unless otherwise specified):						
Potential GDP	-	3.1	3.1	2.9	2.9	3.0
Output gap[2]	-	1.8	0.8	-0.7	-0.8	-0.5
Employment[3]	-	0.6	0.2	-0.4	0.2	0.5
Unemployment rate[4]	-	9.6	10.1	10.4	10.4	10.1
GDP deflator	-	3.1	2.5	0.8	1.4	2.1
Consumer price index	-	4.2	3.6	1.1	1.9	2.2
Household saving ratio, net[5]	-	-0.2	2.6	1.0	-1.5	-3.3
Trade balance[6]	-	-1.2	0.3	1.7	1.4	1.2
Current account balance[6]	-	-5.0	-3.7	-2.6	-2.7	-2.7
General government financial balance, ESA-1995[6]	-	-5.0	-3.9	-4.8	4.6	-3.1
General government financial balance, ESA-2010[6, 7]		-	-	-4.8	-4.1	-3.8
Underlying government financial balance[2]	-	-6.6	-4.7	-5.0	-4.1	-3.9
Underlying government primary balance[2]	-	-4.4	-2.4	-2.7	-1.8	-1.8
General government gross debt, OECD definition[6]	-	63.1	62.4	66.0	58.7	58.9
General government debt, Maastricht definition[6]	-	56.2	55.6	59.2	52.0	52.1
General government net debt, OECD definition[6]	-	32.5	33.5	37.6	31.5	33.0
Three-month money market rate, average	-	4.6	4.9	3.0	2.9	3.8
Ten-year government bond yield, average	-	6.0	5.0	4.0	4.3	4.6

1. Contributions to changes in real GDP, actual amount in the first column.
2. As a percentage of potential GDP.
3. Based on LFS data.
4. As a percentage of the labour force aged 15 or more.
5. As a percentage of household disposable income.
6. As a percentage of GDP.
7. According to ESA-2010 rules to be adopted in September 2014, asset transfers will no longer reduce the deficit.

Source: OECD, *OECD Economic Outlook 94 Database* plus updates.

since the middle of 2012 (Figure 4). Businesses still benefit from a competitive exchange rate following the sharp depreciation of the zloty in 2009, and labour-cost pressures have been moderate (Figure 5), with real wages having risen less than labour productivity by a cumulated 20% since 2002 (Figure 8 below, Panel B). Hence, after some sluggishness in 2010-12, export volume increases have clearly outpaced export market growth. On the other hand, imports have been lethargic amid depressed domestic demand. As a result, the current account deficit has been substantially reduced, from 6.5% of GDP in 2008 to less than 1% in recent quarters, the lowest level since 1995. This has contributed to limiting spillovers on Poland from the emerging-market turmoil triggered by US monetary tapering.

Figure 3. **Economic activity is projected to rebound**



1. Deflated by the total gross fixed capital formation deflator.
Source: OECD, *OECD Economic Outlook 94 Database* plus updates.

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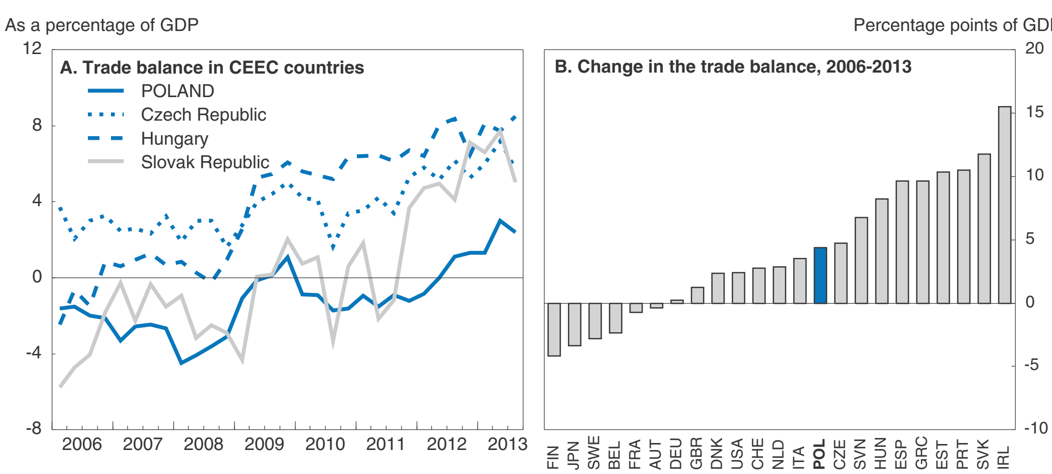
Figure 4. **Sharp improvement in the balance of goods and services**[1]

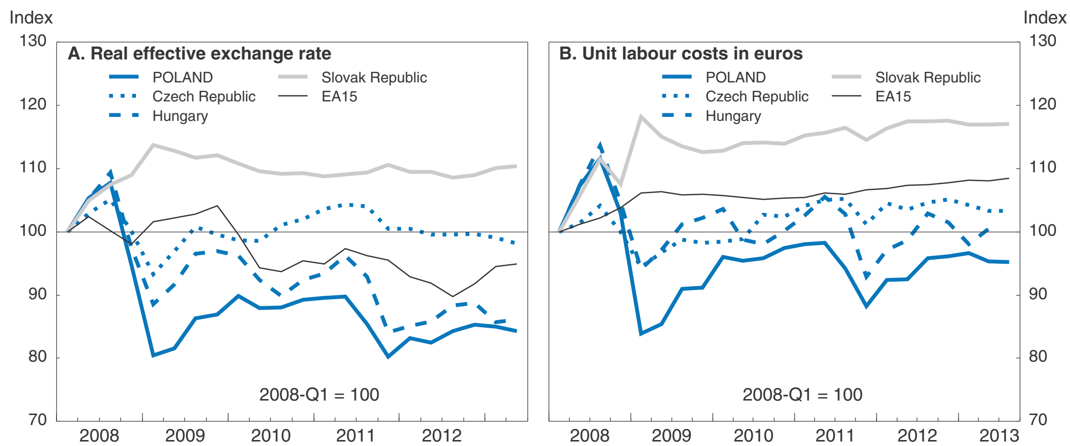


1. Value, National Accounts basis.
Source: OECD, *OECD Economic Outlook 94 Database*.

StatLink http://dx.doi.org/10.1787/888932999298

Long-term government bond rates have nevertheless increased in Poland more than in other central and eastern European countries (CEECs), following foreign investors' heavy sales in June and August 2013 (Figure 6, Panel A). Poland had attracted massive portfolio inflows in 2008-12, accounting for cumulative liabilities of about 15% of GDP, more than twice that in other CEECs (Citibank, 2013). This led to an upsurge in the share of non-resident holdings of domestic sovereign debt to 37% in April 2013 (Panel B), posing a risk as capital flows could quickly reverse course. In the early-2014 episode of renewed emerging-market turmoil, Poland's long-term yield rose to a limited extent, and the zloty weakened only slightly. The IMF's USD 34 billion flexible credit line (for which Poland's eligibility was confirmed in 2014), the broadly adequate level of international reserves (IMF, 2013a) and the swap agreement with the Swiss National Bank diminish contagion risks.

Figure 5. **Poland benefits from competitive exchange rates and moderate labour costs**



Source: OECD, *OECD Economic Outlook 94 Database* plus updates.

How to read this figure: Real effective exchange rates (REERs) – displayed in Panel A – measure the value of a country's currency relative to a weighted average of other currencies, with weights reflecting the importance of trading partners, and adjust for cross-country inflation differentials. A decreasing REER implies competitiveness gains as the relative value of the currency depreciates in real terms, and vice versa. Unit labour costs – displayed in Panel B – are labour costs per unit of (real) output, converted to euros. The figure shows, for example, that Poland's unit labour costs decreased by more than 25% in the period following the onset of the crisis (from 2008Q3 to 2009Q1), more than elsewhere.

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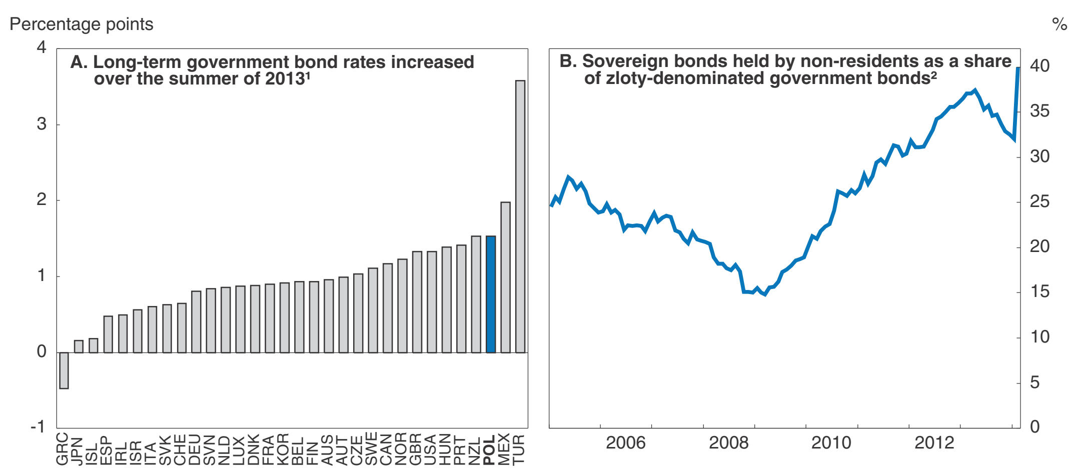
Figure 6. **Bond yields and non-resident holdings**



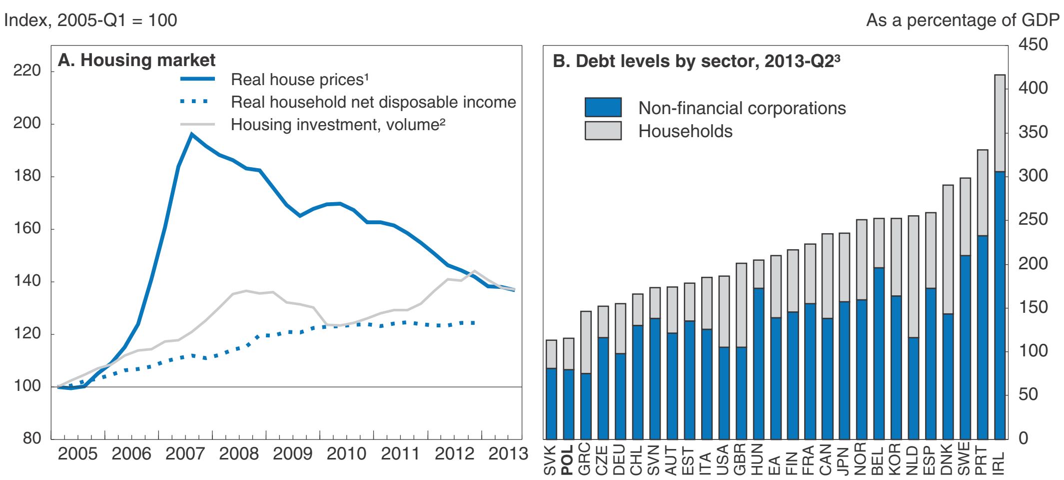
1. Difference in percentage points between 1 May and 5 September. The specific dates correspond to the trough and peak of the average long-term government bond yield across OECD countries excluding Greece. Greek yields have been excluded from the computation of the averages due to their extreme volatility: they fell from 13.08% on 27 March 2013 to 8.12% on 20 May 2013 before bouncing back to 11.71% on 24 June 2013.
2. The February 2014 sharp increase is due to pension system changes detailed in Box 1.

Source: OECD, *OECD Economic Outlook 94 Database* and Ministry of Finance.

StatLink http://dx.doi.org/10.1787/888932999336

Monitoring of the housing market and therefore conducting macroeconomic policies remain complicated, since satisfactory overall house price indices do not exist (OECD, 2008a). The best indicator, the average price of apartments in the 16 main cities, has stabilised since the middle of 2013 after a decline of about 30% in real terms since its 2007Q1 peak. Thanks in part to tighter prudential regulations applying to mortgages (OECD, 2012), the bursting of the housing bubble led to a correction of about two-thirds of the rise recorded in the 2005-07 boom (Figure 7, Panel A). However, the impact of tumbling house prices has been contained owing to modest wealth effects, interest rate cuts and restrictions on borrowing by low-income households. As a result, although the share of non-performing mortgages has increased steadily, it remains limited (see below).

Figure 7. **Housing market and private debt**



1. Simple average of house prices for the existing stock of dwellings in 16 of Poland's bigger cities, deflated by the CPI. Data prior to 2006Q3 are taken from the NBP's information note on home prices in Poland in 2013Q1.
2. Four-quarter moving average.
3. 2013Q1 for Korea; 2012 for Germany, Ireland and the Netherlands. Debt by sector is computed by subtracting shares and other equity, as well as financial derivatives, from total liabilities.

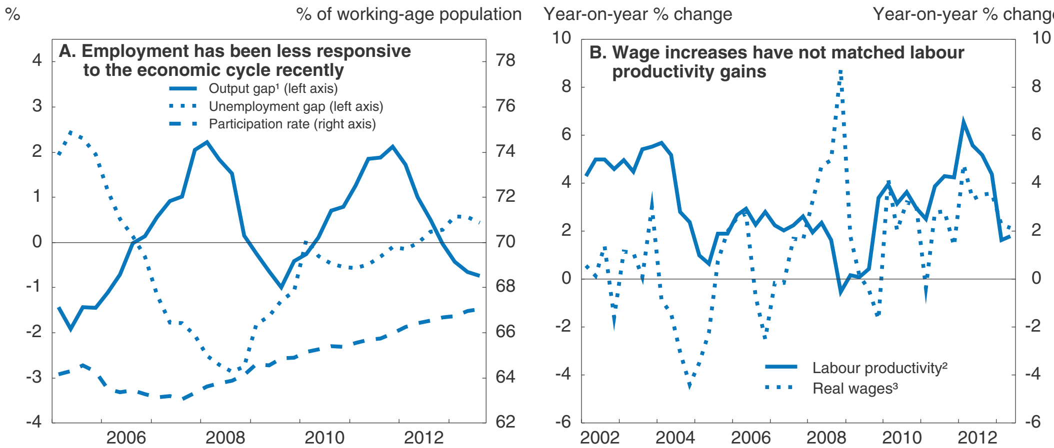
Source: GUS; NBP; *OECD Economic Outlook 94* (plus updates) and *Quarterly National Accounts Databases*.

StatLink http://dx.doi.org/10.1787/888932999355

Credit expansion has been sluggish due to both lacklustre loan demand and tightened lending terms. Despite the low household saving rate, there is no problem with leverage, as both household and corporate debt are reasonable (Figure 7, Panel B). In March 2013 the government launched a loan-guarantee programme to facilitate micro firms' and SMEs' credit access. The maximum working-capital loan amount (PLN 3.5 million, or about EUR 0.8 million) and length (27 months) are low enough to ensure exemption from EU state-aid regulations. Since November 2013, investment loans of up to 99 months duration have also been included. The rules restricting consumer lending (Recommendation T) were also relaxed in 2013.

The 2012-13 slowdown left its mark on the labour market. The unemployment rate rose to a high of 10.6% in 2013Q1, up from a record low of 6.8% in 2008Q4 when the economy was overheating. Despite strong growth in 2010-11, the unemployment rate did not recede, in part due to stronger participation (Figure 8, Panel A). Its current level (10.2%) is close to the OECD estimate of the NAIRU (10%), which remains among the OECD's highest. This suggests that high unemployment is largely structural, although current low inflation could mean the NAIRU is overestimated, implying some slack in the labour market. Wage increases have indeed been consistently smaller than productivity gains (Panel B). Following the December 2011 expiry of earlier measures (OECD, 2012), in November 2013 the government began providing direct financial assistance (*de minimis* aid) to employers experiencing a decrease in turnover.

Figure 8. **Recent growth has had a weak labour content**



1. As a percentage of potential GDP.
2. Labour productivity is measured as real GDP per worker.
3. Dependent employment.

Source: OECD, *OECD Economic Outlook 94 Database*.

How to read this figure: The output gap measures the difference between the level of real GDP and its potential. Hence, a positive output gap indicates that real GDP exceeds its potential, which is likely to trigger inflationary pressure, and conversely a negative gap should put downward pressure on inflation. The unemployment gap measures the difference between the unemployment rate and its estimated equilibrium level (NAIRU). The unemployment gap is an important component of the output gap, and a positive unemployment rate gap tends to be associated with a negative output gap (and vice versa). But this is not always the case, as the output gap is also influenced by other components such as deviations from trends in total factor productivity and labour force participation. The chart shows that in the 2007-08 boom employment was very responsive to the economic cycle, and the unemployment rate fell below its equilibrium level as real GDP increasingly exceeded its potential level. However, in 2011 the employment response to the acceleration in activity was relatively muted, in part due to the increase in labour supply as reflected by the higher participation rate.

StatLink http://dx.doi.org/10.1787/888932999374

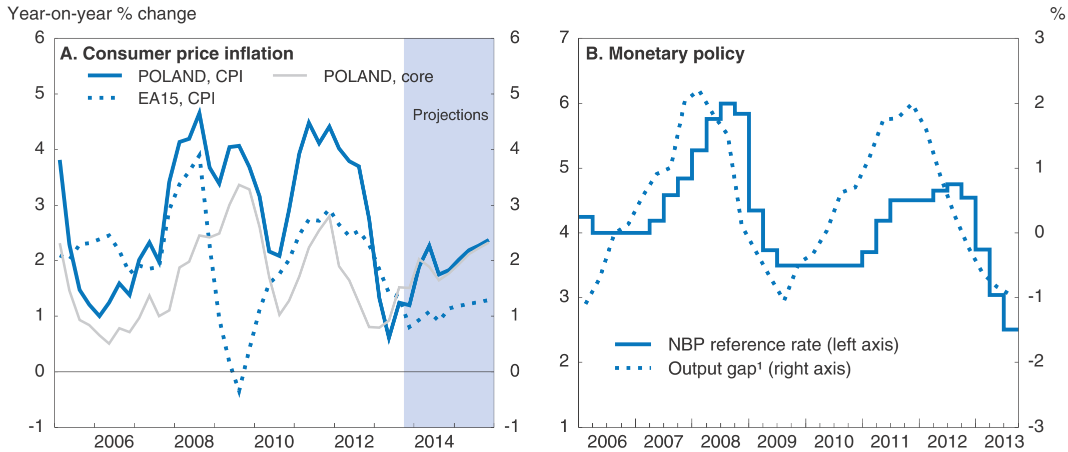
Monetary and financial policy

Short-term interest rates may need to be raised as inflation moves closer to the target

Consumer price inflation fell considerably below the NBP target in 2013 (Figure 9, Panel A), driven by the rise in unemployment, subdued wage pressure and the slowdown in food and energy prices, attributable in part to lower administered prices (NBP, 2013a). Core inflation has also drifted below 1%. The Monetary Policy Council (MPC) reacted progressively to the deterioration in the outlook by easing policy rates from 4.75% in May 2012 to 2.50% in July 2013 (Panel B). This should mark the end of this cycle. Indeed, the pick-up in activity projected by the OECD is expected to move inflation back towards the 2.5% official target. In November 2013, the MPC extended its forward guidance of no rate change until at least the end of June 2014.

Summing up, economic imbalances are limited and broadly shrinking, and inflation, while historically low, should move back towards target. While the macroeconomic policy mix has been appropriate so far, given that the growth impact of announced fiscal consolidation is likely to be only slightly negative (see below), monetary policy will need to be less accommodative following the expiry of the current period of forward guidance. The exact timing and scope of interest rate normalisation should, however, depend on incoming data and the resulting risks for the inflation target in the medium term. The OECD

Figure 9. **Inflation and monetary policy**



1. As a percentage of potential GDP.
Source: OECD, *OECD Economic Outlook 94*; NBP.

StatLink http://dx.doi.org/10.1787/888932999393

projections assume stable nominal exchange rates, and therefore the extent of monetary tightening should be adjusted to account for exchange-rate developments. For example, if rising short-term interest rates in a context of persistently easy global monetary conditions were to spur excessive capital inflows, strengthening the zloty and increasing the vulnerability of the financial system, the extent of monetary policy tightening consistent with the inflation target would be lower *ceteris paribus*. Also, as argued below, more fiscal efforts than currently planned will be needed to meet public-deficit objectives in 2014-15. If these are implemented, monetary tightening can similarly be more gradual.

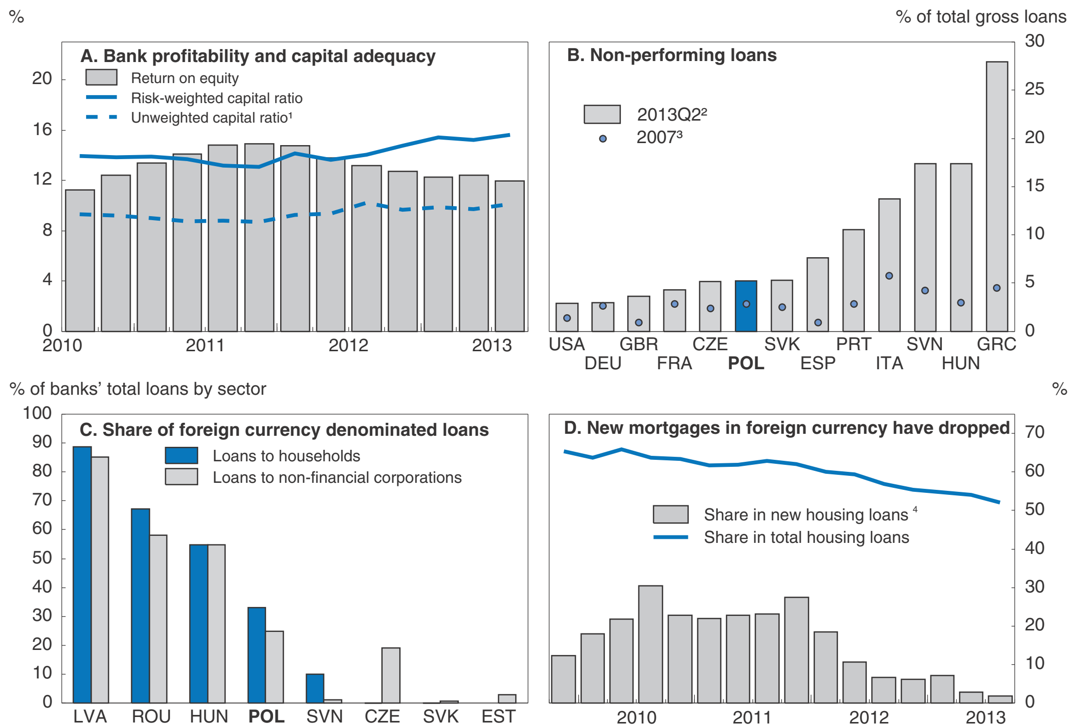
As discussed in past *Surveys*, the insufficient continuity of monetary policy making should be addressed to increase its effectiveness. Continuity is weakened by the lack of overlapping terms for MPC members, as the whole Council (other than the Governor) turns over at virtually the same time (every six years). This results in a periodic severe loss of human capital, experience and institutional memory. The government is working on a draft bill that could address these concerns.

Successive governments have had the objective of adopting the euro, although euro-area economic difficulties have cooled enthusiasm. The 2010 *Survey* focused on conditions to be met for its safe adoption. Concerning the timing, the key is not to pre-commit before the economy is ready, as this could destabilise expectations. Improved product and labour market flexibility would bolster the economy's resilience to asymmetric shocks. For a catching-up country experience has illustrated the threat from domestic booms that can no longer, under a common currency, be controlled by monetary policy. A well designed fiscal policy and strong prudential supervision are needed to avoid the development of such imbalances.

The financial system remains sound, despite deteriorated loan quality

The growth slowdown and euro-area turmoil did not significantly affect the resilience of the financial sector. Poland's largely foreign-owned banking system has remained profitable, well capitalised and liquid (Figure 10, Panel A). The average ratio of capital to risk-weighted assets increased to 15.8% at end-November 2013, with core Tier 1 capital

Figure 10. **Banking sector developments**



1. Median bank capital ratio (core capital over unweighted assets).
2. Or latest available observation.
3. Or first following available observation.
4. Currency structure of new housing loans to households.

Source: Narodowy Bank Polski; KNF; ECB and IMF, *Financial Soundness Indicators* (FSI).

StatLink http://dx.doi.org/10.1787/888932999412

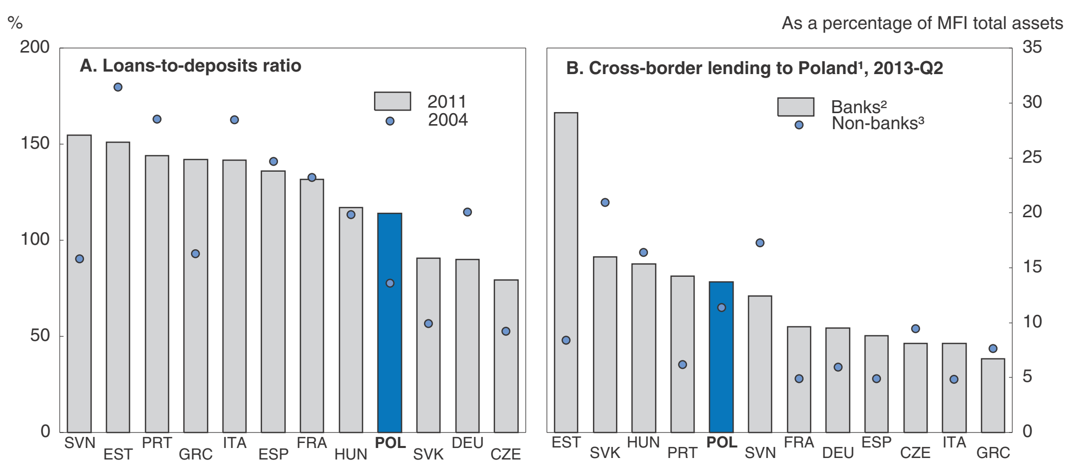
adequacy at 14.3%, well above the level required under Basel III. The unweighted capital ratio has also increased and is among the highest in EU countries.

Loan quality deteriorated during the 2012 slowdown, reflecting rising bankruptcies and an increase in mortgage defaults. However, the share of non-performing loans has stabilised at around 5%, a moderate level although much higher than US or German levels (Figure 10, Panel B). In 2012, in a welcome move to address banking-sector credit risk stemming from its high outstanding foreign-currency-denominated (FX) loan portfolio (Panel C), the financial supervision authority (KNF) increased the risk weight of FX loans from 75 to 100%, well above the 35% applied to domestic-currency loans. As a result, the share of new FX housing loans dropped from 27% at end-2011 to less than 2% (Panel D). KNF has restricted banks to providing FX mortgages only to households with a steady income in the same currency from July 2014.

Although financial stability is not threatened, some mortgages still appear to carry excessive risk. In 2013Q2, 47% of the newly issued mortgages had a loan-to-value (LTV) ratio in excess of 80% (AMRON-SARFiN, 2013). In line with 2012 *Survey* recommendations, in June 2013 the KNF decided to gradually reduce maximum LTV ratios from 95% in 2014 to 80% in 2017. But, in February 2013, the KNF also removed its already high debt-service-to-income (DTI) ceilings (50 to 65%, depending on income), indicating that prudent DTI policies should be set by the banks themselves, while the KNF has the right to challenge banks' choices as part of the regular supervisory process. Survey data published by the NBP indicate that around 20% of loans originated in 2011 and 2012 had DTIs above 50% (NBP, 2013c). If household indebtedness becomes excessive, the KNF should not hesitate to introduce tight DTI ratios, well below 50%.

The banking system is deeply integrated with international (especially euro area) banks and has a considerable amount of foreign funding (Figure 11). The loan-to-deposit ratio is much greater than before the boom (Panel A), although it has drifted down since 2009 (NBP, 2013b) as competition for deposits has increased among domestic banks. The ratio of Polish liabilities to foreign banks as a percentage of total assets of the domestic banking sector remains relatively high in international comparison (Panel B). External shocks, such as strong deleveraging of euro area banks, could reduce credit supply and generate liquidity problems as foreign liabilities may become difficult to roll over. The decline in FX mortgages will gradually curb dependence on foreign funds, and developing the domestic covered bond market would further strengthen banks' funding structure. Also, the strong capital positions of Polish banks provide some cushion against unfavourable developments.

Figure 11. **External funding dependence remains substantial**



1. Cross-border liabilities are divided by total assets of monetary and financial institutions, excluding central banks' assets.
2. Banks' liabilities towards foreign BIS-reporting banks on a locational basis.
3. Non-banks' liabilities towards foreign BIS-reporting banks on a locational basis. Non-banks include other financial companies, government and the non-financial private sector.

Source: World Bank, *Financial Development and Structure Dataset* (November 2013) and IMF (Panel A); BIS and ECB (Panel B).

StatLink http://dx.doi.org/10.1787/888932999431

Strengthening macro-prudential and supervisory arrangements

Poland is reforming its macro-prudential policy framework to introduce a Systemic Risk Board (SRB). A draft law stipulates that the NBP would hold the Chair position with a casting vote. Voting membership would include the Minister of Finance (Vice-Chair), the Chair of the KNF and the President of the Bank Guarantee Fund. The draft empowers the SRB to issue recommendations (publicly, if it so wishes) on a "comply or explain" basis as well as warnings and opinions. The presence of the Minister of Finance would improve information exchange and political commitment. But it may also undermine the SRB's role to lean against the financial cycle because of political considerations and give rise to potential conflicts of interest, given the Treasury's control of three commercial banks (including the largest), representing about a fifth of total banking sector assets (excluding the public investment bank, BGK). The full privatisation of state-owned commercial banks would mitigate potential conflicts of interest.

The reform should ensure a clear separation of roles between the SRB and other financial regulators. In particular, the KNF, which has been praised for its independence and prudential policies (OECD, 2012), should retain its capacity to react effectively to banking-sector distress by issuing non-legally binding regulations ("recommendations"). In any case, KNF's ability to issue such recommendations should be extended to insurance and securities markets. Ideally, they should be made legally binding (IMF, 2013b), though this may be inconsistent with Poland's constitution. The Bank Guarantee Fund's independence from the banking sector should also be strengthened, as its council currently includes two representatives of the Polish Bankers Association, which creates potential conflicts of interest.

Monetary and financial policy recommendations

Key recommendations

- If activity and inflation accelerate as projected by the OECD, gradually increase the official monetary policy rate.
- Ensure that the Systemic Risk Board (SRB) has the independence and power to make recommendations coupled with a "comply or explain" mechanism. Ensure a clear allocation of roles between the SRB and the current regulators; in particular, retain the ability of the financial supervision authority (KNF) to issue prudential recommendations.

Other recommendations

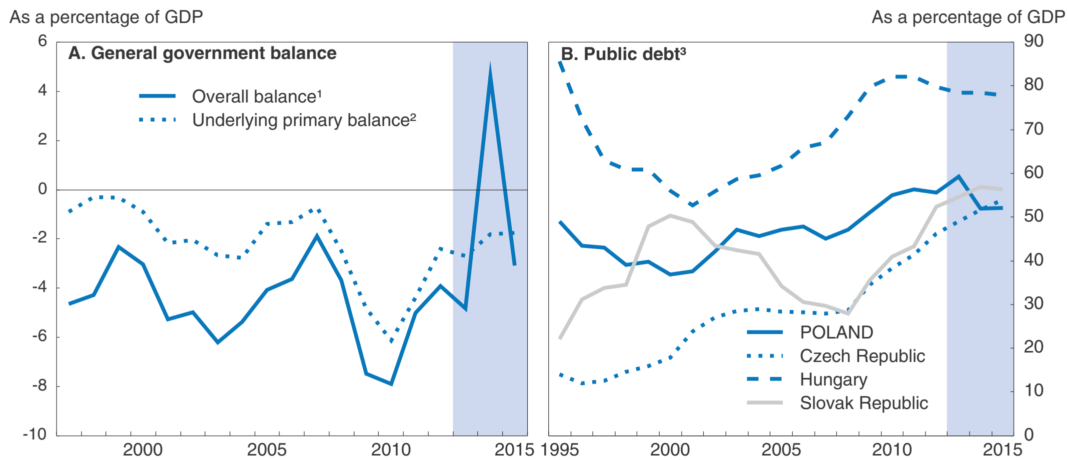
- Closely monitor debt-service-to-income ratios, and introduce binding caps on them if household-sector leverage becomes excessive. Reduce banks' external vulnerabilities by developing the domestic covered-bond market.
- Introduce staggered non-renewable terms for MPC members' appointments to strengthen policy continuity.

Fiscal policy

Deficit targets have been missed

After halving to 3.9% of GDP between 2010 and 2012, the general government deficit widened in 2013 to an estimated 4.8% of GDP, against the planned 3.5% in the April 2013 convergence programme (Figure 12). In 2013, despite freezes on public wages and personal income tax (PIT) thresholds, fiscal slippage resulted from lower-than-expected tax receipts due to the sharp economic slowdown and higher social expenditure and public consumption. The current fiscal rules incorporate two government debt thresholds (50% and 55% of GDP, according to the national debt definition) that trigger corrective actions to prevent it from reaching the constitutional limit of 60% of GDP. To allow the automatic stabilisers to operate the government suspended the 50% debt threshold for 2013-14, which otherwise would have required an additional tightening of around 1.2 percentage points of GDP in 2013. An additional spending rule based on a moving average of GDP growth was introduced in December 2013 (see below).

Figure 12. **After improvements in 2011 and 2012, the fiscal position deteriorated in 2013**



1. According to ESA-95. According to ESA-2010 rules to be adopted in September 2014, asset transfers will no longer reduce the deficit, and the general government financial balance would be -4.1 and -3.8% of GDP in 2014 and 2015, respectively.
2. As a percentage of potential GDP.
3. Maastricht definition.

Source: OECD, *OECD Economic Outlook 94 Database*.

StatLink http://dx.doi.org/10.1787/888932999450

Convergence programmes and their associated budget laws have spelled out profiles for restoring fiscal balance that have often subsequently not been achieved. This is in part due to growth forecasts that turned out to be optimistic (Table 2), but that does not fully explain the recent tendency to miss the target. Postponing official fiscal targets and the slower return to the 1% of GDP Medium-Term Objective (MTO) for the structural deficit may have tarnished the credibility of multi-year budget planning and more broadly of the conduct of fiscal policy. To regain this credibility the government should base future budgets on unbiased assumptions, as was done for 2014.

Most of the fiscal effort in 2014-15 is focused on a change in the second-pillar pension system (Box 1 and Figure 12), which will have limited short-term effects on economic activity. It will reduce the 2015 government deficit by a cumulative 1.4% of GDP under the current accounting rules (ESA-95), but by only 0.8% of GDP under the new rules (ESA-2010) that will enter into force in September 2014. Modest additional measures (worth about 0.3% of GDP), including increases in excise duties as well as the continuing freeze of public employee wages and the personal income tax (PIT) thresholds, should reduce the headline (ESA-2010) deficit from 4.8% of GDP in 2013 to 3.8% of GDP in 2015 and bring Maastricht debt to 52% of GDP in 2015. The underlying primary deficit (excluding interest payments and one-offs) would fall from 2.7% of potential GDP in 2013 to 1.8% in 2015.

More medium-term consolidation

Poland recently agreed with the European Commission to reduce the headline deficit to under 3% of GDP in 2015 to correct its excessive deficit (European Commission, 2013a). This target appears appropriate, given a 2015 projected growth rate above potential. Indeed, such efforts will be needed to reach the MTO and put debt on a sustainable declining trend. They would also help to rebuild fiscal buffers, as public debt will remain close to the fiscal rules' ceilings (even when taking into account the impact of the pension

Table 2. **Budget balance and growth rate forecasts included in convergence programmes**

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Convergence programme	A. Real GDP growth (%)										
December 2004	5.0	4.8	5.6								
January 2006		4.3	4.6	5.0							
November 2006			5.1	5.1	5.6						
March 2008				5.5	5.0	5.0					
December 2008					3.7	4.0	4.5				
February 2010						3.0	4.5	4.2			
April 2011							4.0	4.0	3.7	3.9	
April 2012								2.5	2.9	3.2	3.8
April 2013									1.5	2.5	3.8
GDP growth outcome[1]	3.6	6.2	6.8	5.0	1.6	3.9	4.5	2.1	1.4		
Convergence programme	B. General government budget balance (% of GDP)										
December 2004	-3.9	-3.2	-2.2								
January 2006		-4.6	-4.1	-3.7							
November 2006			-3.4	-3.1	-2.9						
March 2008				-2.5	-2.0	-1.5					
December 2008					-2.5	-2.3	-1.9				
February 2010						-6.9	-5.9	-2.9			
April 2011							-5.6	-2.9	-2.5	-2.0	
April 2012								-2.9	-2.2	-1.6	-0.9
April 2013									-3.5	-3.3	-2.7
Budget balance outcome[1]	-4.1	-3.6	-1.9	-3.7	-7.5	-7.9	-5.0	-3.9	-4.8		

1. OECD projections for 2013.
Source: OECD based on successive convergence programmes and *OECD Economic Outlook 94 Database*.

Box 1. **The 2014 pension changes**

The 2014 pension changes reverse part of the 1999 reform, which gave rise to transitional costs as pension contributions were diverted to the mandatory second pillar, increasing public debt cumulatively by an estimated 17.5 percentage points of GDP as of 2012 (Ministry of Labour, 2013; IMF, 2011). The changes will reduce both measured public debt and the deficit (Table 3) but will raise implicit public pension liabilities. On 3 February 2014, 51.5% of the net assets of open pension funds (OFEs) were transferred to the public social security institution (ZUS). OFEs' Treasury securities holdings – the major part of the assets transferred – were cancelled. The changes in the pension system lowered gross general government debt by around 9.3% of GDP. Under ESA-95 rules, the fiscal balance will become a large surplus in 2014 before being reversed again. However, this transitory swing will not occur under ESA-2010 rules to be adopted in September 2014, which will better capture the underlying deficit dynamics. In 2015, the headline and structural deficits would be reduced by 1.4% of GDP according to ESA-95 rules and 0.8% according to ESA-2010 rules.

While the default option is to contribute to the public pension system, workers can opt-in to allocate 2.92% of their gross wages (15% of their pension contributions) to the privately managed funds. The government assumes that 50% of contributors will choose to opt-in. These additional social security contributions would reduce the general government deficit by 0.2 percentage point of GDP in 2014 and 0.4 percentage point in 2015. Moreover, the assets of those individuals choosing to stay in OFEs will start being

Box 1. **The 2014 pension changes** *(cont.)*

transferred to the public pension system 10 years prior to the retirement age, generating receipts of 0.3 and 0.7% of GDP in 2014 and 2015, respectively.

Table 3. **The effect of the 2014 pension changes on general government budget balances**

As a per cent of GDP

	2014		2015	
	ESA-95	ESA-2010	ESA-95	ESA-2010
Cancellation of OFEs' Treasury bond holdings	8.5	0	0	0
Asset transfers from the OFEs for employees 10 years prior to retirement	0.3	0	0.7	0
Savings on debt service payments	0.3	0.3	0.3	0.3
Additional social security contributions	0.2	0.2	0.4	0.4
Total excluding asset transfers	0.5	0.5	0.8	0.8
Total	**9.3**	**0.5**	**1.4**	**0.8**

Source: European Commission (2013a), "Analysis of the Budgetary Situation of Poland", *European Commission Staff Working Document*, No. 605, November.

The combination of the 1999 reform and its partial reversal might well damage social trust in the pension system and harm the credibility of future structural reforms more broadly. The 2014 changes also reduce the total amount to be invested in financial assets and thus may cut already low future replacement rates by restricting investment portfolio choice. The increased role of the public pay-as-you-go system in a context of rapid population ageing may further lower future replacement rates. Another result of the recent reforms will be somewhat less liquidity on the domestic Treasury bond market, which serves as a benchmark in the region. Moreover, the cancellation of OFEs' Treasury bond holdings increased the share of non-resident investors in zloty-denominated public debt (from around 32% in January 2014 to 41% in February 2014) and curtail the participation of local investors with a long-term investment horizon. The upsides of the 2014 changes would be to reduce debt service payments and the high OFE operating costs, although it might have been possible to reduce these costs through better regulation of the funds (Égert, 2012a).

changes) and as medium-term health-care and pension spending pressures will increase. An additional fiscal tightening worth about 0.8% of GDP in 2015 will be required compared to the October 2013 programme presented to the European Commission.

Fiscal consolidation should be implemented in a way that minimises potential adverse side effects on short- and long-term growth but also on equity (Cournède et al., 2013). A number of consolidation options are possible, as argued in the previous *Survey* (OECD, 2012). Savings could be achieved by: i) enhancing cost efficiency in the public administration; ii) reforming the farmers' social-security scheme; iii) eliminating certain occupations' pension privileges, scaling back survivors' pensions and increasing women's retirement age faster (see below); and iv) revising the formula used to calculate disability pensions to limit their attractiveness (see below). The tax system should also be reformed to remove distortions, improve tax administration and compliance and raise additional revenues as needed (OECD, 2012; World Bank, 2013); the government plans to present a new simplified tax code in 2015 and to develop improved tax information systems. Additional revenues could be derived by: i) cutting tax expenditures, in particular eliminating reduced VAT rates (European Commission, 2013b) and abolishing child tax credits for high-income households; ii) linking social-security contributions of the self-employed to actual earnings; iii) increasing environmental taxation (Poland is one of the few European countries without explicit vehicle taxes based on fuel efficiency [OECD, 2012]); iv) increasing property taxes by establishing market-value-based property taxes and taxing capital gains on rented properties; and *v)* further privatisations in competitive segments of the economy. The potential conflicts between fiscal consolidation measures and equity objectives should be minimised by, for instance, targeted transfers, which could alleviate any regressive effects of tax expenditure cuts and environmental taxes.

Further strengthening the fiscal framework

There are positive features of the current process of the budget preparation: the MPC provides an official opinion on underlying macro-economic assumptions, and the social partners are likewise consulted. Yet, creating an independent institution, composed of high-profile national or international fiscal-policy experts, in line with the EU directive of 8 November 2011, would help to further improve the credibility of multi-year budgeting. It could monitor fiscal plans, including underlying growth assumptions, debt outcomes and deficit and spending targets. It could also be mandated to provide an independent analysis of current and planned fiscal policies on long-term debt sustainability. The OECD has recently developed principles for such institutions (OECD, 2013a).

The debt thresholds in the national fiscal rules should also be strengthened. The debt measure used for the thresholds is a national one, which has left it open to manipulation (OECD, 2012). Harmonising it with its Maastricht counterpart would make the ceilings more transparent and ultimately increase financial-market confidence.

In a welcome step Poland has recently introduced a new spending rule, covering 90% of general government expenditures. Spending growth will be capped by nominal targets based on a moving average of GDP growth, which will enhance transparency and credibility. It is also based on two corrective debt thresholds at 50 and 55% of GDP. The new spending rule could help to smooth the effects of EU transfers and the related public investment cycle. Following the pension system changes (see Box 1), the public debt thresholds are expected to be lowered by 7 percentage points. The fiscal rules (the current rules plus the new spending rule) would then take into account four debt thresholds: the two thresholds of the spending rule at 43 and 48% of GDP, a preventive debt threshold at 55% of GDP and the 60% of GDP constitutional limit, while the 50% of GDP debt threshold of the current rule would be abolished. Progress has also been made in extending budget discipline to local governments. Local government deficit rules were introduced in 2011, and, in line with the 2012 *Survey*'s recommendation, individual debt service limits will henceforth prevent excessive debt levels. However, safety buffers should still be included in the central government's budget to account for local governments' slippages or revenue shortfalls.

Fiscal policy recommendations

Key recommendations

- Achieve greater fiscal consolidation in 2015 than currently planned to be able to meet the below-3%-of-GDP general government deficit target.
- Create an independent institution to monitor underlying budget assumptions and fiscal performance relative to targets. Strengthen the fiscal framework by implementing detailed multi-year budgeting, basing budgets on unbiased assumptions and harmonising the domestic and Maastricht debt definitions.

Other recommendations

- Reduce government spending as needed by: enhancing cost efficiency in the public administration, substantially reducing subsidies to the farmers' social security scheme from current levels and eliminating social security privileges available to some other occupations, scaling back survivors' pensions, increasing women's retirement age faster and avoiding that disability pensions become attractive relative to old-age pensions.
- Raise additional revenues as needed by: cutting tax expenditures, linking social security contributions of the self-employed to actual earnings, increasing environmental taxation, raising property taxes by establishing market-value-based property taxes and taxing capital gains on rented properties, and making further privatisations in competitive segments of the economy and improving tax compliance.

Achieving sustainable and inclusive growth

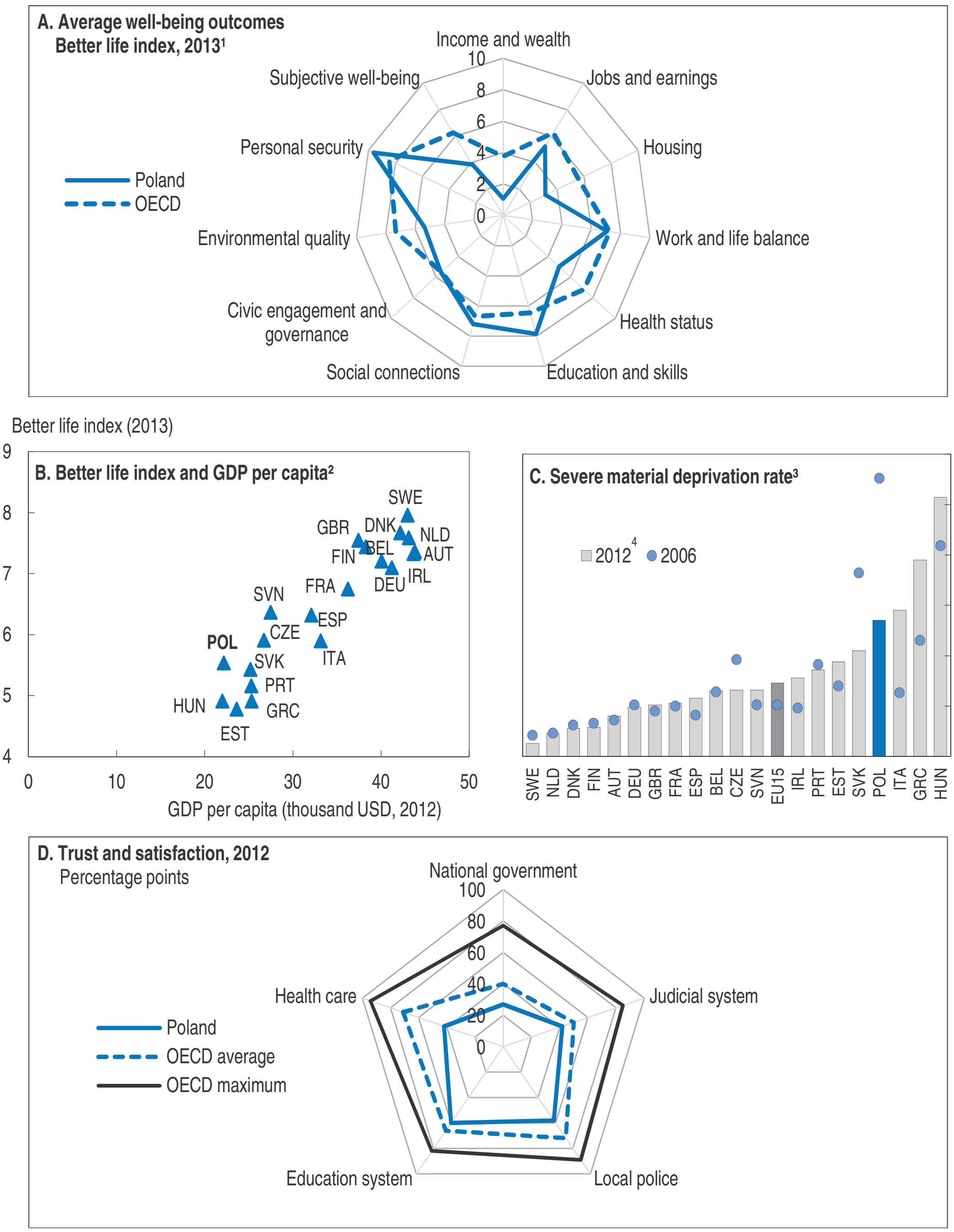
Enhancing sustainable growth is crucial if Poland is to keep catching up to the best performers in well-being terms (Figure 13, Panels A and B). Well-being gaps are related to the still relatively high incidence of material deprivation – despite considerable progress (Panel C). This *Survey* focuses on making the labour market work better and strengthening product-market competition as ways to improve well-being. With slow implementation of reforms, there is always a risk that the full potential of the economy will not materialise, and in the case of Poland that risk is compounded by the general distrust in key public institutions (Panel D). The lack of affordable quality housing, low self-reported health and high emissions of some air pollutants are also among the most pressing concerns (OECD, 2013b) (Panel A).

Ensuring environmental quality

The chapter on climate-change policies in the last *Survey* (OECD, 2012; Égert, 2012b) showed that progress has been made in reducing energy intensity and greenhouse gas emissions over the past decade (Figure 14, Panel A). Nevertheless, the potential for cutting emissions remains substantial and should be realised in a least-cost fashion. An economy-wide single carbon price is key to minimising abatement costs, but current explicit and implicit carbon prices vary widely across sectors.

Air pollution levels are high on average (Panel B), particularly in cities (WHO, 2011), partly due to the predominance of fossil-fuel-based energy production, outdated heating systems and transport-sector emissions. Pollution from private vehicles should be reduced by better reflecting their environmental performance in annual vehicle taxes and by developing the railway network (Panel C). Also, exploiting Poland's shale gas reserves – potentially Europe's biggest – needs to be handled carefully to avoid local pollution,

Figure 13. **Social indicators**



1. Each well-being dimension is measured by one to three indicators from the OECD Better Life indicator set. Normalised indicators are averaged with equal weights so they range between 10 (best OECD country) and 0 (worst OECD country).
2. For illustrative purposes, the Better Life Index is calculated here with equal weights on the 11 dimensions (see *www.oecdbetterlifeindex.org* for details). GDP per capita in US dollars at current prices and purchasing power parities; 2011 for Greece.
3. Severely materially deprived people are those unable to pay for at least four of nine items (e.g. rent, mortgage or utility bills; a washing machine or a car).
4. 2011 for Ireland and the United Kingdom.

Source: OECD (2013), *OECD National Accounts Statistics* (database), June and OECD Better Life Index; *OECD Government at a Glance 2013*; Eurostat (2013), *Income and Living Conditions*, *Eurostat Database*, June.

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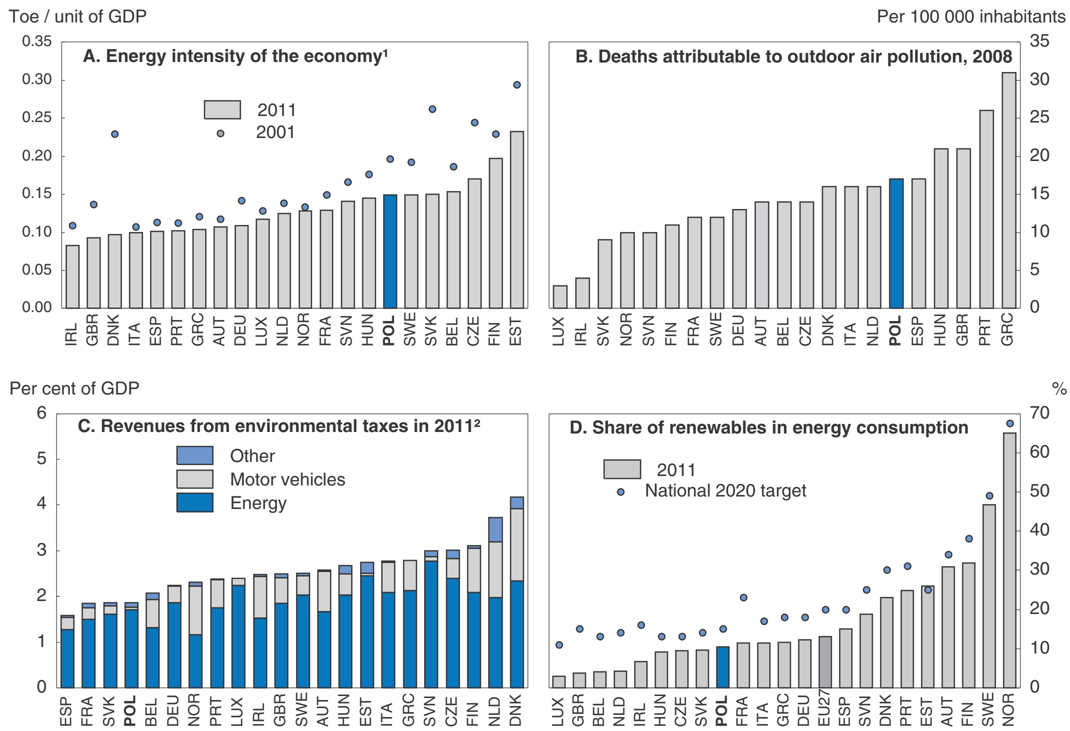
Figure 14. **Environmental indicators**



1. Total primary energy supply (estimated for 2012) in tonnes of oil equivalent (toe) per thousand USD. GDP in constant prices and purchasing power parities.
2. Data for Poland refer to 2010.

Source: *OECD/EEA Database on Instruments used for Environmental Policy*; WHO (2013), *Global Health Observatory Data Repository*; IEA (2013), *Energy Balances of OECD Countries 2013*, International Energy Agency.

StatLink http://dx.doi.org/10.1787/888932999488

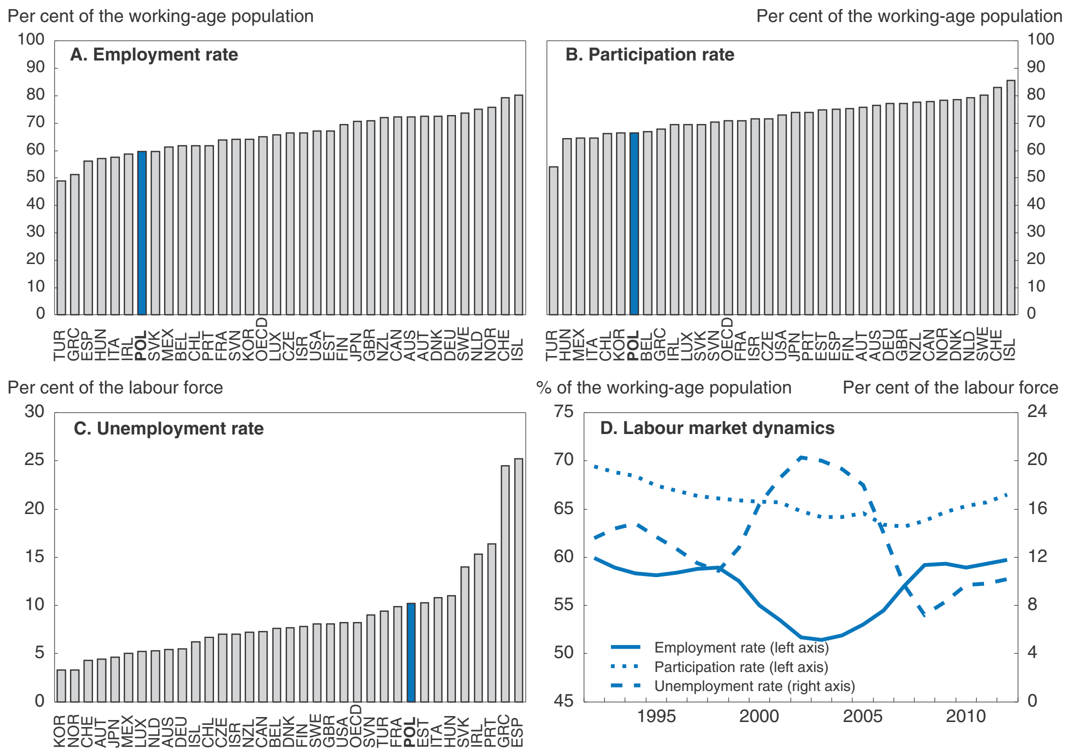
especially from water contamination and methane leakages. Improving water quality and waste management are other important environmental challenges: fertiliser and pesticide use has risen, and Poland still uses mainly landfill-based solid waste management, while wastewater treatment should be further developed. Despite considerable progress, a third of the population was still not connected to a sewage network in 2011.

Renewable forms of electricity remain underdeveloped (Figure 14, Panel D). The National Renewable Energy Action Plan sets a 2020 target of 15% for such energies. Since 2005, mandatory quotas for power companies and a green-certificate market have pushed many state-owned coal-fired power plants to co-fire with biomass, but the development of other technologies has been limited. Better pricing of externalities could make other renewables more competitive. Yet, grid capacity and management also need to improve. Extending interconnection capacity with neighbouring countries would foster competition and facilitate supply-demand balancing in the context of increasing wind and solar-powered generation whose availability is typically intermittent (OECD, 2012a).

Making the labour market work better

Despite significant improvements since the mid-2000s, employment remains one of Poland's major structural weaknesses, impeding firms' competitiveness and the nation's potential output. The employment rate, at 59.7% in 2012, is among the lowest in the OECD (Figure 15). Unemployment is at a high level and seems to be mostly structural.

Figure 15. **Labour market indicators, 2012**



Source: OECD, *Labour Force Statistics 2013 Database.*

StatLink http://dx.doi.org/10.1787/888932999507

Participation has increased since 2007, breaking its declining trend thanks to relatively strong growth, tightened accessibility to early-retirement and disability pensions, cohort effects related to the 1980s baby boom and a decrease in the labour tax wedge.

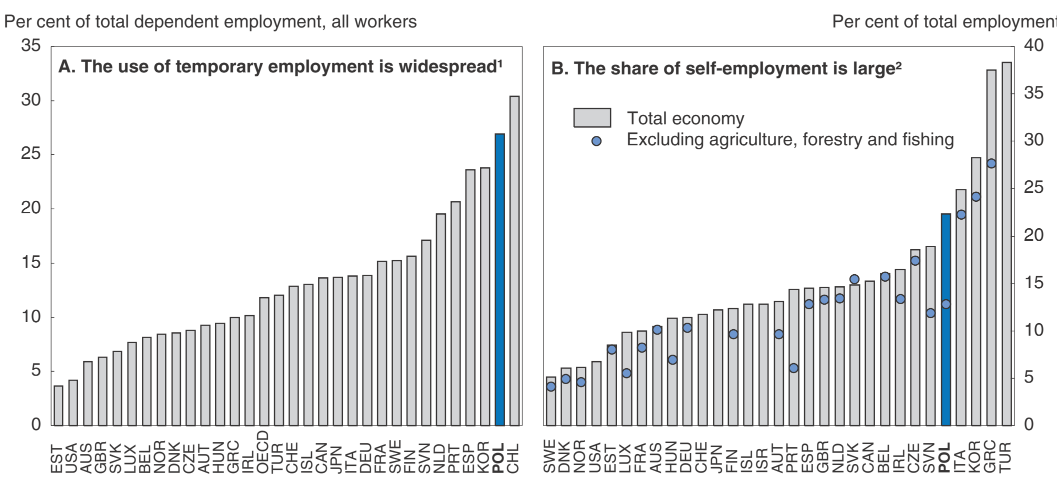
Poor labour market performance is by no means attributable only to labour market policies. Numerous inefficiencies induce significant misallocation and waste of labour resources. There is substantial scope to enhance competition, which could generate numerous job opportunities (Chapter 2). Moreover, there are important impediments to internal labour mobility. The quality of transport infrastructure, discussed in the 2008 *Survey* (OECD, 2008a; Kierzenkowski, 2008), has improved recently thanks in part to EU funds, but remains insufficient, especially for rail. Urban housing is expensive because of a lack of private rental supply. As recommended in the 2013 *Going for Growth* (OECD, 2013c), the release of zoning plans by municipalities should be made mandatory and transaction taxes on housing purchases replaced by *ad valorem* property taxes. On the other hand, compulsory escrow accounts to protect buyers' advances were introduced in 2012, consistent with OECD's recommendations. Other barriers to labour mobility are also attributable to wage distortions and the design of unemployment and social assistance policies (Chapter 1). In particular, the advantages resulting from the farmers' social insurance system induce people to hold onto small plots of land, even those no longer actively farming.

Reducing labour market segmentation

Employment protection is not particularly stringent. The notice period for dismissals is average, severance pay low and the definition of unfair dismissals among the OECD's least constraining. But legal procedures for disputed separations tend to be long and unpredictable, reinstatement obligations heavy and trial-period contracts, which can be used for both temporary and open-ended employment, rather short. According to a 2013 amendment to the Labour Code, working-time regulations have been made more flexible, as the reference period used to compute working-time limits was extended from four to twelve months, conditional on branch or firm-level agreement.

The labour market is nevertheless heavily segmented in a rather complex way. Shares of both temporary and self-employment are among the OECD's highest, although for the latter this is mainly due to the large share of agriculture (Figure 16). Although only two consecutive fixed-term contracts with the same firm are allowed, there is no cap on their duration. About 7% of total employment is governed not by the Labour Code but rather by civil-law provisions, which are less costly for employers, as such worker-contractors have only limited social protection and are not subject to minimum-wage regulations. Poland is also one of the OECD countries where informal employment poses the most serious challenges (OECD, 2008b). Simplifying and better enforcing tax regulations would reduce its incidence and scope, as would phasing out the various advantages granted to the self-employed (Chapter 1). Such profound dualism may induce in-work poverty, limit investment in human-capital formation, lengthen the transition from school to stable work and make some specific groups, in particular the young and the low-skilled, bear a disproportionate part of the costs of adjustment to economic shocks (Lepage-Saucier et al., 2013).

Figure 16. **The labour market is heavily segmented, 2012**



1. 2011 for Korea; 2009 for Sweden and 2005 for the United States.
2. 2011 for Australia.

Source: OECD, *Labour Force Statistics*; *OECD Economic Outlook 94* and *OECD National Accounts Databases*.

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Better activating the unemployed

The unemployment benefit (UB) system has strict eligibility rules – only 20% of registered unemployed were eligible in 2012 – and the benefit is a low flat rate that falls by 20% after three months. Yet, strong incentives to register as unemployed stem from having access to free health-insurance coverage. This creates a situation where many registered unemployed are not searching for a job, having registered just to get the insurance. It also implies that some job-search support is bound to fail, thus discouraging both public employment service (PES) staff and employers posting job offers. Moreover, the general entitlement period of six months is doubled for older workers, reducing work incentives for that group, as well as in high-unemployment districts. It helps to maintain minimum living standards during job search, but it also discourages migration out of economically depressed areas.

There is a broad consensus that the PES functions poorly (Kaluzna, 2009). It suffers from a lack of human resources, both quantitatively and qualitatively, inefficient use of those in hand, insufficient relevant information at local levels and serious coordination problems. Merging local labour offices with UB and social assistance administration to create one-stop shops, and, more fundamentally, integrating their management, would help overcome those weaknesses. Job-seeker profiling should be expanded as the government intends, as well as the scope of private employment services. The umbrella function of the Ministry of Labour and Social Policy should also be strengthened, including by promoting the adoption of best practices through performance management and the introduction of a benchmarking system such as those developed in Australia or Switzerland (OECD, 2013d). The government plans to start benchmarking labour offices soon.

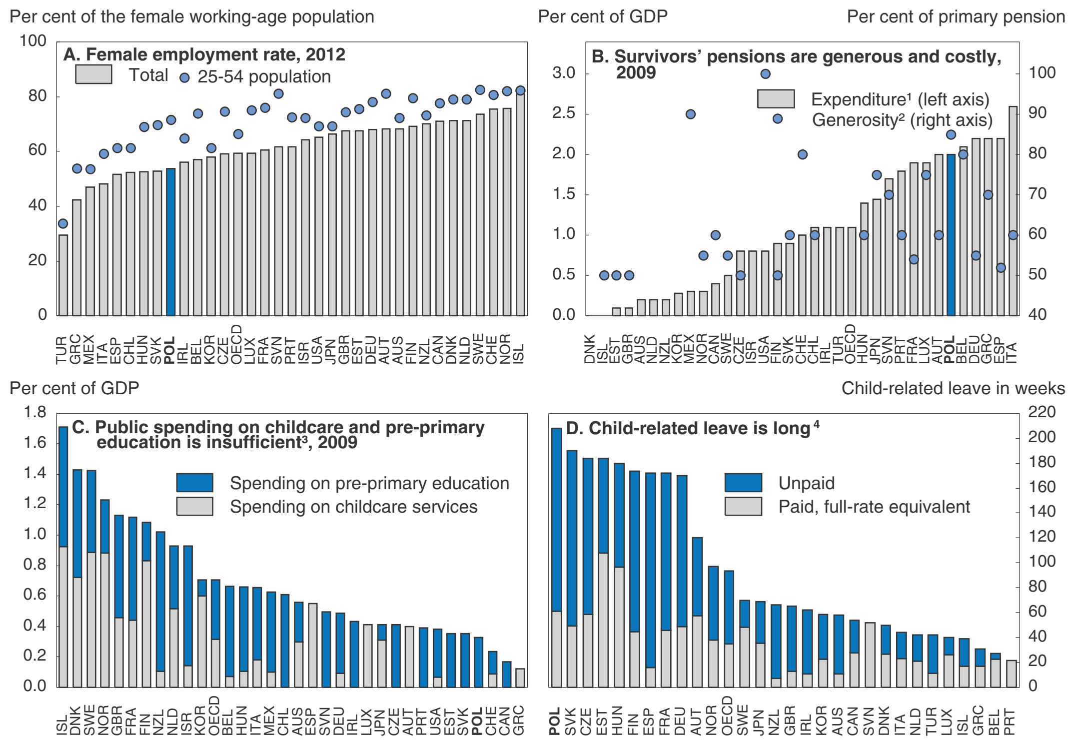
Jobseeker activation could also be improved. Work-availability and job-search requirements in the UB and social-assistance systems are minimal (Venn, 2012). Tighter obligations and better monitoring would sharpen incentives to return to work. Moreover, the provision that a suitable job offer need not be limited to a beneficiary's previous occupation is not effectively enforced. Although crude UB replacement rates are low, when combined with other transfers and relatively high tax wedges for those on low incomes, situations arise where effective replacement rates become very high. Gearing more assistance to being in work would help make work pay. This could be done by making more transfers (such as childcare subsidies) conditional on working or seeking work.

Improving policies targeted at specific groups

The female employment rate is especially low (Figure 17, Panel A). The 2012 pension reform – which is supposed to raise statutory retirement ages to 67, by 2020 for men (from 65 today) and by 2040 for women (from 60 today) – goes in the right direction, but its pace should be accelerated for women. The survivors' pension regime, about 90% of whose beneficiaries are women, is expensive and might undermine work incentives for some recipients (Panel B). Indeed, the ratio of the deceased partner's pension awarded to the survivor, at 85%, is among the highest in the OECD, and greater than the estimated ratio needed to sustain the surviving spouse's living standards. Moreover, the benefit falls if the survivor earns income, reducing work incentives. Such a system implies redistribution from women who engage in paid work to those who do not and from singles and dual-career couples to single-earner couples (James, 2009). Scaling back this programme and reducing the marginal implicit tax involved would increase employment and reduce the overall tax burden.

The insufficient development of childcare and pre-primary education in Poland is a major structural weakness (Figure 17, Panel C; OECD, 2013c). Yet, important recent progress has been made. In 2011, pre-school education became compulsory from the age of five, and primary education will start at age six in 2014. In June 2013, the government reduced parents' direct costs of accessing kindergarten. According to a July 2013 regulation, every four year-old will have the right to participate in pre-school education from September 2015 and every three year-old from 2017. However, paid maternity leave has been increased several times since 2006 (including in 2013) to an OECD record of 52 weeks (Panel D), in principle to promote fertility. For each child, maternity leave consists of a first six-month period paid at 100% of past salary and

Figure 17. **Female employment rate is low and work incentives are weak**



1. Public expenditure on survivors' pensions.
2. Survivors' benefits, as a percentage of individuals' primary pension entitlements.
3. Disaggregated spending data are not available for Spain.
4. Child-related leave periods by duration of unpaid leave and the duration of the full-rate equivalent of the leave period if paid at 100% of last earnings; child-related leave is the sum of maternity and parental leave. Poland's numbers take into account the 2013 extension of the maternity leave.

Source: OECD, *Labour Force Statistics 2013 Database*; for Panel B: Whitehouse, E.R. (2013), "Adequacy and Sustainability of Pension Systems: Evidence from Europe", *OECD Social, Employment and Migration Working Paper*, OECD Publishing, forthcoming; James, E. (2009), "Rethinking Survivor Benefits", World Bank, *Social Protection and Labor Discussion Paper*, No. 928.

How to read Panel D: The figure is constructed by summing the paid and unpaid periods of maternity and of parental leave. In Poland as an example, maternity leave comprises 26 weeks paid at 100% of salary and 26 weeks paid at 60% for a total of 52 weeks. On a full-rate equivalent (FRE) basis, this means 26 * 100% + 26 * 60% = 41.6 weeks paid and 10.4 weeks unpaid. On top of this, parental leave is granted for a maximum of 156 weeks, two thirds of which are partially paid at the monthly benefit of PLN 400. This breaks down into 19.4 weeks of FRE paid leave and 136.6 weeks of unpaid leave: the 19.4 weeks of FRE paid leave are obtained by computing the replacement rate for the average-wage worker as the ratio of the monthly benefit (PLN 400) to the average wage (PLN 2 144), adjusted for the length of the paid period (two thirds), i.e. 400/2144 * 2/3 * 156 = 19.4 weeks. Combining maternity and parental leave leads to 61.0 weeks paid at the FRE basis and 147.0 weeks unpaid.

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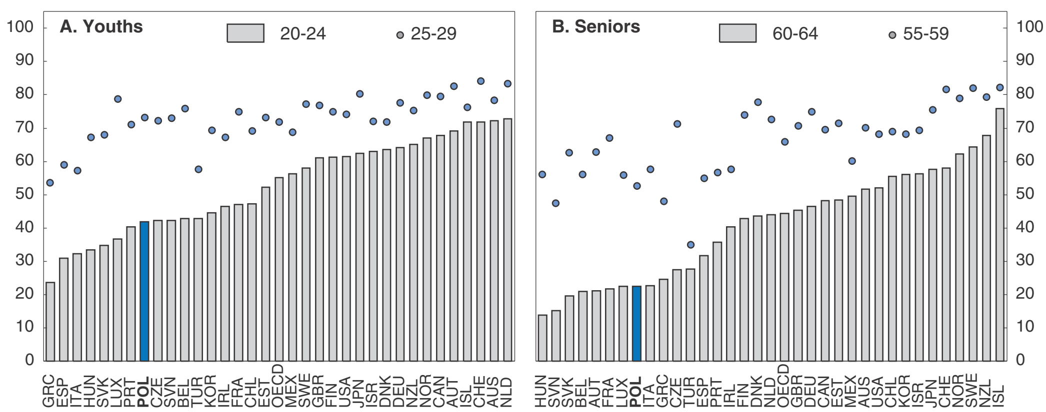
of a second six-month period paid at 60%; the second period can be shared between the mother and the father. On top of this, the parental leave of 156 weeks is also the longest among OECD countries. Such long leaves are costly for public finances and could result in mothers not returning to the workforce with no observed advantages for children (see e.g. Dahl et al., 2013). To enhance second-earners' employment the government should adopt an individualised tax system; develop childcare and long-term care facilities, and pre-school education; and encourage flexible working-time arrangements. The government intends to continue to develop a variety of child-care arrangements. Moreover, the impact of long child-related leave on the employment of mothers should be closely monitored.

Poland's poor labour-market performance is also concentrated at both ends of the age spectrum (Figure 18). For young people the shortfall in employment rates is concentrated in the 20-24 age group and is to a large extent attributable to their greater enrolment in education, which rose sharply up to 2005, and to the limited combination of work and study. The rise in educational attainment among youths is a major achievement, but the demand for skills has risen even faster (Chapter 1). Less-educated youth in particular tend to go through an arduous transition through temporary contracts, which are widespread and seem to serve not as a springboard to stable employment (OECD, 2009a), but rather as a screening device (Baranowska et al., 2011). Precarious employment is therefore pervasive among youths.

Figure 18. **Employment rates are especially low at both ends of the age spectrum**

As a percentage of the population by age bracket, 2012



Source: OECD, *Labour Force Statistics 2013 Database*.

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Following earlier reforms, the improvement in educational performance over the past 20 years has been impressive. Yet, youth employment prospects could be improved by further enhancing work-based learning in Vocational Education and Training (VET) programmes, by boosting social partners' involvement, including in school boards, and by raising the quality of teaching. In line with past OECD recommendations (OECD, 2007), a clearer distinction between vocational and academic Higher Education Institutions (HEIs) is being introduced. Because employers have little incentive to hire apprentices (European Commission, 2013b), subsidies to cover employers' training costs of VET students should be expanded. The system of quality-based HEI financing could be bolstered, and promoting practical modules in tertiary curricula and strengthening the link with businesses should be continued.

The employment and participation rates of older workers have both risen strongly since the mid-2000s. Yet, the current levels remain well below OECD averages. Although recent measures are helpful, special old-age pension regimes (for farmers, miners, uniformed services, prosecutors and judges) should be phased out and remaining pre-retirement schemes eliminated. Important progress has been made since the mid-2000s to tighten access to disability pension schemes. However, the employment of the disabled is very limited and should be promoted by: reducing the employer quota of 6%, while raising the penalty for firms failing to reach it; and better training and activation of disabled workers (OECD, 2006). Moreover, following the 1999 old-age pension reform, which will reduce replacement rates by automatically decreasing initial pension values as life expectancy improves, the ratio of average disability to old-age pensions will increase significantly, boosting incentives to retire early under the disability regime when possible (IMF, 2013a). Therefore, the formula used to calculate disability pensions should be revised in line with that used for old-age or minimum pensions. Finally, prohibiting worker lay-offs less than four years before retirement also deters hiring of older workers and should be removed.

Recommendations to boost employment

Key recommendations

- Reduce labour market dualism by: making all contracts for labour services subject to the same tax and social contribution regime as Labour-Code contracts; extending the maximum length of trial-period contracts; streamlining legal dismissal procedures; and setting a maximum cumulative duration for temporary contracts with the same firm.
- Expand the resources of public employment services to hire more skilled staff, and ensure that overall resources are better allocated to front-line placement tasks. Promote the adoption of best practices by labour offices through performance management and benchmarking.
- Tighten work availability and job-search requirements for jobseekers. Reduce passive social assistance by making more transfers conditional in part on being employed or seeking work.
- Boost female employment by: developing childcare and long-term care facilities and pre-school education; and increasing women's retirement age at a more rapid pace than scheduled. Monitor closely the impact of the long maternity leave on the employment of mothers.

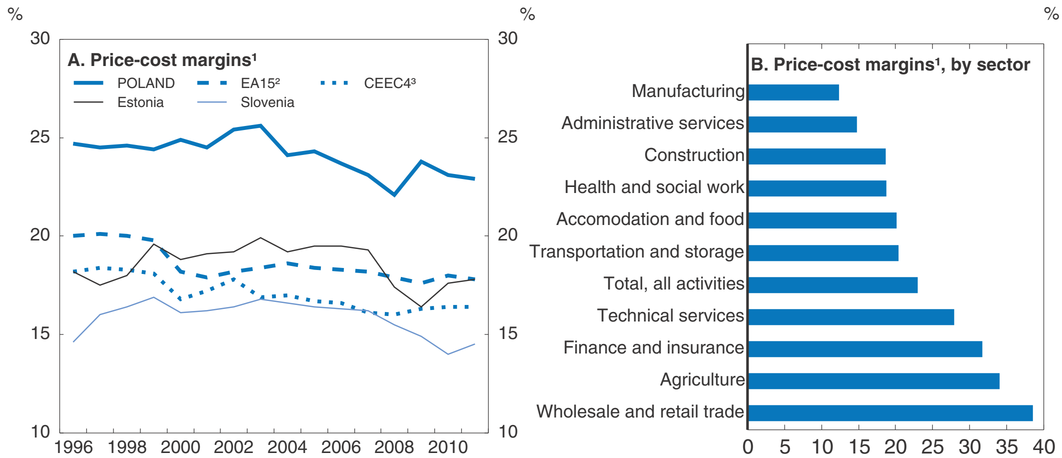
Other recommendations

- Reduce obstacles to internal mobility by: continuing to develop transport infrastructure, in particular by upgrading the quality of the rail network; reforming housing policies by requiring the release of zoning plans by municipalities, and replacing transaction taxes on property by annual *ad valorem* taxes.
- Disconnect health-insurance entitlement from unemployment registration. Eliminate regional and age-related differences in the maximum length of unemployment benefits.
- Accelerate the reduction of government subsidies to the farmers' social insurance system. Phase out all special occupational regimes, eliminate pre-retirement schemes, and avoid that disability pensions become attractive relative to old-age pensions. Remove the prohibition to lay off workers less than four years before retirement.

Strengthening product market competition

Boosting product market competition is crucial for Poland to speed up convergence towards euro-area income levels, given the large remaining productivity gaps. The extent of economic rents seems higher than in most other OECD countries (Figure 19). Although tremendous progress has been made, restrictive product market regulations still hinder activity substantially. Poland has the OECD's largest potential to increase productivity by aligning regulations with best practices, especially in network industries (Bouis and Duval, 2011). While improvements have been significant in terms of the competition policy framework, changes have been less so for barriers to entrepreneurship and state control.

Figure 19. **Economic rents are much higher than in most other OECD countries**



1. Adjusted for self-employment: self-employed are assumed to earn the average wage in the sector, except for agriculture. For Panel B, the reference period is 2008-11, and sectors which comprise less than 2% of Polish employment – mostly public activities (education, public administration and defence) – are not displayed.
2. Excludes Ireland for which data are missing.
3. Excluding Poland.

Source: *Eurostat's National Accounts Database* and OECD calculations.

How to read this figure: Price-cost margins represent the difference between sales and variable costs – intermediate inputs and labour – divided by sales. Higher margins indicate lower competitive pressures and higher economic rents.

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Reducing competition-distorting public ownership

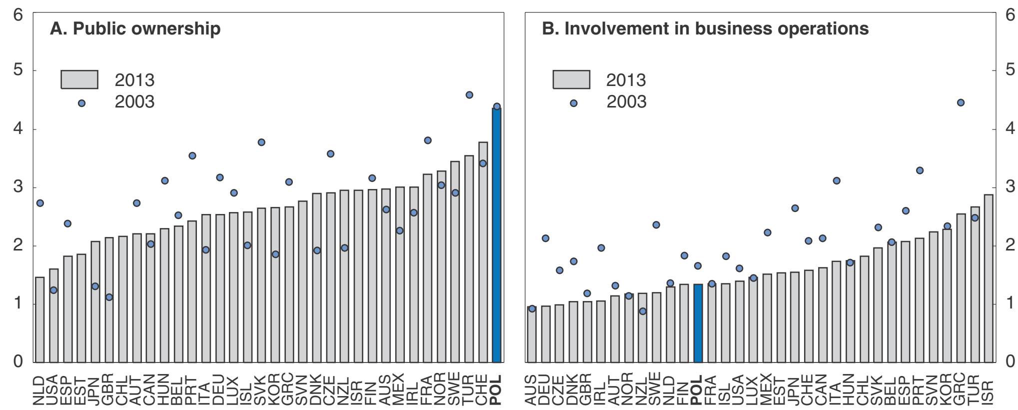
Polish public ownership is one of the most extensive in the OECD (Figure 20): the state is involved in many potentially competitive sectors such as mining, banking, real estate and chemicals. The government launched ambitious privatisation plans in 2008-11 (during the world economic crisis) and 2012-13, and the process is still on-going. In several cases it has opted for partial privatisation and kept a controlling stake in many state-owned enterprises (SOEs), largely in the energy, financial and mining sectors, which are in most cases considered to be of strategic importance, thereby reducing the benefits of private ownership. In 2013, the government created an investment fund fed by future privatisation revenues and government assets to co-finance infrastructure and investments mainly in chemical, energy and extractive industries. While this might help improve access to long-term finance (which may not be available solely in the private market) and therefore stimulate economic growth, it could also mean further state involvement in some competitive segments of the economy.

Strengthening competition enforcement

Poland's Competition Authority appears to be efficient. Yet, there is scope to strengthen it. Its size and budget are limited: with 132 people working on competition enforcement, its staff is a smaller share of total employment than in many other countries. Its President has an open-ended contract and can be removed at any time by the Prime Minister. Indeed, the President was dismissed in February 2014. The Competition Authority also lacks the power to split up dominant firms or to force vertical separation. A welcome draft law would provide it with some power in this area and increase incentives for cartel disclosure and whistleblowing by setting up an US-inspired "leniency plus" programme.

Figure 20. **State involvement in the economy, 2003 and 2013**[1]

Index scale from 0 to 6, from least to most restrictive



1. 2008 for the United States.

Source: OECD (2014), preliminary *Product Market Regulation Database*.

How to read this figure: The OECD public ownership indicator – displayed in Panel A – measures the presence of public ownership in 30 sectors, the extent of state-ownership in network industries and the level of public control in enterprises where the state owns shares. The indicator is based on qualitative information, for example the presence or absence of SOEs in a given sector. It measures the scope of public ownership across sectors rather than the quantitative scale of public ownership in the economy. Measures of the scale of the privatisation process between 2003 and 2013 are presented in Chapter 2. The OECD indicator of involvement in business operations – displayed in Panel B – measures the use of regulated prices and command and control regulations. The reported indicators for Mexico, Poland and Turkey are based on preliminary estimates as some of the underlying data have not been validated with national authorities. Subsequent data validation may lead to revisions to the indicators for these countries.

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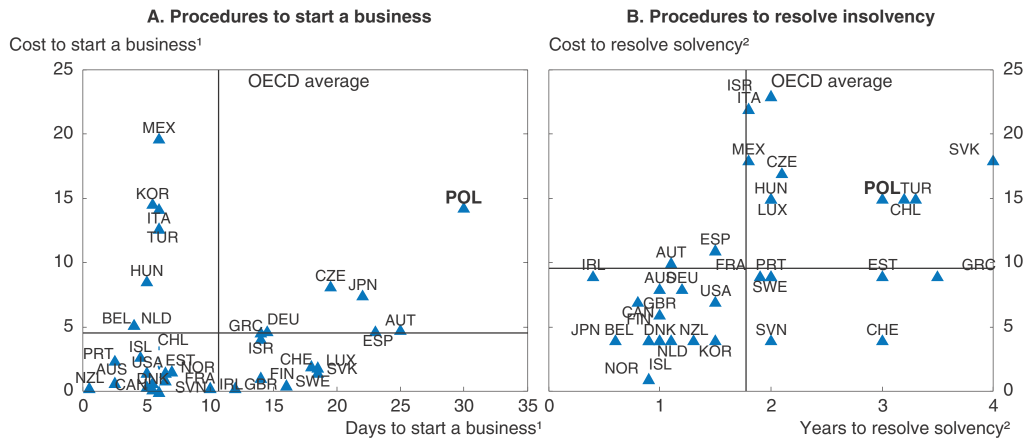
However, judicial system inefficiencies slow court procedures that would help to end cartels; more use of information and communication technologies would help (Palumbo et al., 2013). Furthermore, private enforcement of competition laws remains rare. Class actions were introduced into Polish law only in 2010, but consumer claims applying to antitrust infringements and anti-competitive practices are scarce, in part because of judicial weaknesses.

Substantial barriers to the entry and exit of firms weaken competition and entrepreneurship. The transposition of EU single-market legislation is unsatisfactory, according to the European Commission (2012). Red tape has been significantly reduced in recent years, and on-line procedures to register a limited liability company were used in more than 20% of all 2013 registrations. Although starting a business remains costly in terms of both time and money (Figure 21, Panel A; World Bank, 2013), reform of the procedure, approved by the government in early 2014, should reduce the registration time from more than 20 to 7 days (Ministry of Justice, 2014). The government reduced the paperwork related to the collection of taxes and social security contributions in June 2013 and recognises the need to further ease the administrative burden by implementing new streamlining measures.

Bankruptcy procedures are lengthy and costly (Figure 21, Panel B), restricting the ability to save viable firms and deterring entrepreneurship. Polish bankruptcy law is also limited to corporations, exposing small unincorporated businesses to huge uncertainty about potential personal liability. As proceedings remain open as long as valid creditor claims are outstanding, the process can be lengthy, and consequently few bankruptcies

Figure 21. **Procedures to start a business and resolve insolvency remain long and costly**



1. The cost to start a business is recorded as a percentage of the economy's annual GDP per capita. It includes all official fees and fees for legal or professional services if such services are required by law. Time to start a business captures the median duration that corporate lawyers indicate is necessary in practice to complete a procedure with minimum follow-up with government agencies and no extra payments.
2. The cost of insolvency proceedings is recorded as a percentage of the value of the debtor's liabilities. Time to resolve insolvency represents the time for creditors to recover their credit in calendar years. The period of time measured by *Doing Business* is from the company's default until the payment of some or all of the money owed.

Source: World Bank (2013), *Doing Business,* 2014.

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actually occur, curbing resource reallocation. The government is preparing a reform of bankruptcy procedures for 2014 and developing second-chance policies for entrepreneurs.

Improving public procurement

Public procurement amounts to about 20% of GDP, among the highest shares in the OECD. Ensuring fair competition and selecting the best suppliers are therefore critical. Public ownership, especially in local-government-dominated sectors, may lead to non-neutrality of the bidding process. A waste-management law implemented in June 2013 transferred responsibilities to local governments, requiring them to establish public procurement processes. However, in Poland, sub-central governments have often tried to shield local public enterprises from competition, for example in areas such as waste collection, water services and public transportation (OECD, 2009b). Moreover, awarding public contracts relies heavily on the criterion of lowest price, rather than on effective implementation of complex projects or environmental impacts. This led to serious problems, which the government intends to address. Proposed legislation includes both improved assessment of the likelihood of successful contract completion as a criterion for contractor selection and dissuasive sanctions in case of abnormally low prices. Adopting more complex criteria will require an increase in administrative capacity.

Raising competition in network industries

Competition is weak in network industries except telecoms. Strengthening it in the potentially competitive upstream and downstream segments should be combined with non-discriminatory third-party access to the natural monopoly segment. Other than in telecommunications, the independence of sectoral regulators needs to be enhanced by awarding their presidents fixed-term and non-renewable contracts during which he or she cannot be dismissed without fault, and preventing revolving-door opportunities.

Production, transmission and distribution of electricity and gas are largely dominated by SOEs. For example, despite legal unbundling, the incumbent gas operator (PGNiG) controlled 95% of the market in 2012. Yet, the energy market is gradually being liberalised. At the end of 2012, a gas exchange was created, and 97 entities were entitled to trade. The government laudably plans to oblige PGNiG to sell 55% of its gas production on the exchange in 2015. Yet, vertical ownership separation would further improve third-party access. Also, better pricing of externalities could encourage renewable electricity development. Finally, improving grid capacity and management, especially by expanding international interconnections, would keep costs down and safeguard reliability (OECD, 2012).

The water industry is very fragmented and dominated by municipally owned utilities, which are mostly not corporatised. They suffer from overstaffing, a lack of automation and low wages (OECD, 2011). There is no national regulator: water companies and tariffs are supervised by mayors or municipal councils. An independent water and sanitation services regulator could improve efficiency by imposing productivity targets using international benchmarking and yardstick regulation. This could push the nation's 1 600 water companies to merge to reap the benefits of scale economies and help finance badly needed investment.

The railway sector also suffers from inefficiency resulting from insufficient competition (OECD, 2008a; World Economic Forum, 2013). More than 90% of passenger transport is controlled by central or local governments. The historical operator was split into different entities for freight (PKP Cargo), long-distance passenger transportation (PKP Intercity) and infrastructure management (PKP PLK S.A.) within a holding company (PKP Group), while local governments are responsible for regional passenger transport. The holding company plays a key role and also dominates infrastructure management. There has been significant progress in freight, as PKP Cargo's market share fell from 80% in 2006 to about 60% in 2012. Yet, third-party access by non-government providers remains an issue. The main public manager of the rail network (PKP PLK S.A.) should be totally independent of the PKP Group.

Strengthening competition in professional services

The government recently launched an impressive programme to deregulate professional services. This is an area where OECD indicators suggest that entry requirements were substantially stricter than in best performing countries; by contrast, conduct regulations tended to be lax. About 70% of the currently 350 regulated professions have been selected for full or partial deregulation in three waves, the first of which included 51 professions, notably legal professions, occurred in early 2013. It is important that the two other waves be fully implemented.

Recommendations to strengthen product market competition

Key recommendations

- Lower further the costs of entry and exit, such as cumbersome business registration. Reduce the length and cost of bankruptcy procedures.
- Pursue privatisation, and substantially reduce government ownership in competitive segments of the economy while ensuring sound governance of remaining state-owned enterprises.
- Modify public procurement practices to select the contractors offering the best value for money rather than the lowest price. Focus procurement decisions on a mix of prices and technical bid details, including environmental impact assessments. This will require enhancing staff skills to deal with complex selection criteria.
- Introduce fixed-term non-renewable mandates for the presidents of the Competition Authority and sectoral regulators, during which they cannot be dismissed without fault. Create an independent regulator for water and sanitation services.

Other recommendations

- Give the Competition Authority more powers to split up firms to reduce dominant market positions and to impose vertical separation as a remedy for reduced third-party access.
- Increase competition in rail transportation. Insure total independence of the main public infrastructure manager from the operators.

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ANNEX

Progress in structural reform

This Annex reviews action taken on recommendations from previous Surveys. Recommendations that are new in this Survey are listed in the relevant chapter.

This annex presents under each theme:

- Past recommendations
  - ❖ ***Action taken and current assessment***

Product market competition and Competitiveness (see also Chapter 2 herein)

- Continue efforts to further ease the administrative burden on businesses.
  - ❖ ***Information requirements when starting a business were simplified, an e-registration process was introduced and tax registration procedures shortened, but the administrative burden remains high. In 2014, the government plans to streamline further the procedures to start a firm and to reform those dealing with insolvency.***

- Continue the privatisation of state-owned companies in the financial, mining and chemical sectors.
  - ❖ ***The 2012-13 privatisation plan was implemented. The Polish Investment Programme will use future privatisation receipts to ease access to long-term finance for infrastructure projects, but it could also allow further state involvement in chemical and heavy industries.***

- Ease competition-restraining regulations by reducing public ownership in the potentially competitive segments of network industries.
  - ❖ ***Action taken is limited to the selling of shares in three electricity companies in 2012-13.***

- Pursue gas and electricity market liberalisation by fully complying with EU regulations and possibly by implementing ownership unbundling in those sectors.
  - ❖ ***The energy market is gradually being liberalised. A gas exchange was set up in 2012 together with an obligation to sell on it at least 30% of production in 2013, 40% in 2014 and 55% in 2015 of the gas entering the gas network. Yet, the impact is partly blurred as most of the producers and distributers have strong vertical ties through state ownership, and the incumbent still controlled 95% of the gas sector in 2012.***

- Deepen financial development through a consolidation of co-operative banks and an improved legal framework for collateral.
  - ❖ ***The government is working on a new cooperative banking act.***

- Scale down regulations in professional services regarding both educational requirements and licensing.
  - ❖ ***Significant progress is being made: 51 occupations were deregulated in 2013. There are plans to deregulate 195 other professions in two on-going legislative procedures.***

Monetary, prudential and exchange-rate policies

- Introduce staggered terms for Monetary Policy Committee members' appointments to ensure continuity of monetary policy.
  - ❖ ***A welcome draft reform proposes that one third of the Monetary Policy Council members would be replaced every two years to ensure continuity.***

- Reduce currency mismatches in banks' balance sheets by appropriately calibrating liquidity requirements to strengthen their funding structure and diminish the reliance on foreign funding.
    - ❖ ***FX lending has been drastically curtailed (see Assessment and Recommendations). Loan-to-deposit ratios have diminished. Yet, the banking sector has a considerable amount of external financing.***

Fiscal policy and the budgetary framework

- Let the automatic stabilisers function within the debt ceiling constraints, if the economy slows more than projected.
    - ❖ ***The government let the automatic stabilisers play during the recent slowdown.***

- Cut tax expenditures. Broaden tax bases by making revenues from farming activities liable to income tax, introducing cash registers for all professional services to improve VAT collection, significantly tightening eligibility for the lump-sum income tax, and linking social security contributions of the self-employed to actual earnings.
    - ❖ ***Little progress has been made to cut tax expenditures. The PIT deductibility of expenses related to authorship contracts was limited, the eligibility to the internet tax relief was tightened, and high income households with one child were excluded from family tax relief, but relief for the third child and each subsequent child was increased. The sales threshold granting exemptions from keeping records was divided by two in 2013, raising the use of cash registers.***

- Redesign and increase the least distortive taxes, by establishing market-value-based property taxes, taxing capital gains on rented properties, eliminating the tax discrepancy between diesel used as a motor fuel and that used as heating oil, and implementing an economically meaningful carbon tax.
    - ❖ ***No action.***

- Further tighten eligibility criteria in the generous disability pension system. Reform the farmers' social security scheme, eliminate pension privileges for certain occupations, and equalise retirement ages for men and women at 67.
    - ❖ ***In 2012, the government decided to increase the retirement age to 67 for both genders. The reform phases in the increase until 2020 for men and 2040 for women. It also reduces pension privileges for uniformed services.***

- Enhance the efficiency of public administration.
    - ❖ ***A performance-based budgeting system was introduced in 2012-13, and its application will strengthen allocative and operational efficiency. The government launched an initiative to reform the civil service and increase e-procedures by 2020.***

- Strengthen the fiscal framework by: introducing a deficit rule, putting in place detailed multi-year budgeting and spending ceilings, creating an independent fiscal council, and harmonising the domestic and Maastricht definitions of government debt.
    - ❖ ***The 50% public debt threshold in the existing fiscal rules was suspended in August 2013. Additional debt thresholds of 50 and 55% of GDP were introduced in a new spending rule in December 2013. Following the pension system changes (see Box 1), these thresholds are expected to be reduced to 43% and 48%, respectively, while the preventive debt threshold of 50% of GDP in the existing fiscal rules is to be***

abolished. The new spending rule covers a larger share of the general government sector and aims to stabilise the general government deficit at the MTO level of 1% of GDP. An amendment has imposed the publication of detailed multi-year budgets and spending ceilings.

- Use some sort of period-average exchange rates, rather than end-of-year values, for the evaluation of foreign-currency public debt.
  - ❖ ***The government now uses the most favourable exchange rate, between the end-of year value and the annual average, to compute public debt. The temptation to influence the end-of-year exchange rate persists if its level is weaker than the annual average.***

Labour markets (see also Chapter 1 herein)

- Refrain from increasing the minimum-to-average wage ratio. Consider differentiating the minimum wage across regions depending on local labour-market conditions.
  - ❖ ***The minimum-to-average wage ratio increased from 0.36 in 2011 to around 0.39 in 2013 but remains fairly low by OECD standards.***
- Consider introducing an earned-income tax credit to encourage labour market participation of marginal groups.
  - ❖ ***No action.***
- Facilitate labour-market access for foreign workers to meet specific project needs. Provide easier access to workers from a broader range of countries than those on the eastern border.
  - ❖ ***In 2014, the access to the labour market will be facilitated at the margin for short-term workers from Armenia.***

Education

- Reduce the skills mismatch in the labour market by: improving the training system, developing a flexible lifelong learning system and promoting a clearly distinct tertiary VET system.
  - ❖ ***A new curriculum for vocational education, including at least 50% practical training and developed with employers, was introduced in 2013. A new programme based on grants aims at increasing internships in higher education institutions (HEIs). Furthermore, according to a 2013 draft law, HEIs would have to specialise in either academic or vocational (practice-oriented) education. The proposal would make three-month internships mandatory in vocational education and allow students to validate skills acquired outside the formal system. The Council of Ministers also adopted a strategic document "Perspective for lifelong learning" in September 2013.***
- Improve tertiary education by allowing public higher education institutions (HEIs) to introduce cost-related tuition fees for all students, developing student loans and reinforcing HEI quality assessment.
  - ❖ ***Following the 2011 reform, the assessment of HEIs was modified and quality-oriented subsidies have been implemented, amounting to about 2% of tertiary education spending. In October 2012, mandatory payments for the second and additional degrees were introduced at public HEIs.***

- Expand provision of free pre-school education at ages 3 to 5, focusing particularly on poor and rural areas.
  - ❖ ***Following the 2011 reform, the number of childcare institutions for children under 3 years old almost doubled from 2010 to 2012, but their total capacity remains extremely low. The enrolment rate in pre-school education for children at ages 3 to 5 increased from 47% in 2007 to 70% in 2012. Pre-school fees beyond the minimum five hours were capped at 1 PLN per hour in June 2013.***

Health care

- Broaden access to care and reduce inequality by: targeting extra resources to shorten waiting lists; extending dental services covered by public insurance, introducing co-payments on medical services while imposing a means-tested cap on the level of out-of-pocket payments; and increasing transparency of dual physician employment in the public and private sectors.
  - ❖ ***The coverage of dental services by public insurance was extended in November 2013, and further X-ray diagnostics were introduced in the basic benefit package.***

- Improve the allocation and use of current resources by: shifting resources from hospitals to primary and long-term care, potentially by integrated health-care delivery models; strengthening primary medicine's gate-keeping role; providing clearer incentives to hospitals to rationalise the their resource use; promoting the development of hospital management skills; and streamlining the responsibilities of the national health fund (NFZ) and central and local governments.
  - ❖ ***In 2013, the NFZ strengthened the role of outpatient specialists for some minor surgical procedures. Pilot projects testing different forms of coordinated care are expected to start in 2014. The government plans to decentralise the NFZ in 2014-5. This would streamline responsibilities between independent regional centres in charge of assessing health needs and investment planning, and a national authority in charge of pricing, quality control and technology assessment.***

- Avoid labour shortages in the health-care sector by: training more staff; improving retention, particularly through better management policies and delaying retirement; enhancing re-integration in the workforce of the departed; enhancing the role of advanced practice nurses and physicians' assistants; linking pay to performance; and developing targeted immigration policies.
  - ❖ ***A planned change would shorten doctors' specialisation training by 2 to 3 years.***

- Develop a comprehensive strategy to address growing long-term care needs, thereby facilitating female labour force participation.
  - ❖ ***The Health Ministry is preparing a strategic document analysing demographic pressures, utilisation of medical resources and patient behaviours to facilitate health planning.***

Housing

- Remove fiscal incentives supporting the residential sector.
  - ❖ ***VAT refund on building materials will be abolished in 2014.***

- Make the release of municipal zoning plans mandatory.
  - ❖ ***No action.***

- Publish official composite house price indexes for the country as a whole as well as different market segments.
  - ❖ ***No action. The Central Statistical Office has developed a house price index. However, it is not yet publicly available.***

- Work towards further easing of controls on rent increases.
  - ❖ ***The "occasional renting" scheme, which allows sub-letting part or all of the dwelling without restrictions on rent increases, was expanded to entrepreneurs.***

Transport

- Elaborate and publish a precise and comprehensive top-down strategy for the transport sector, addressing long-term prospects and interrelations among projects, based on cost-benefit analysis.
  - ❖ ***A top-down strategy for the whole transport sector until 2020 was published. However, the precise projects and their implementation schedule have not yet been presented.***

- For providing regional rail services, implement competitive tendering procedures, and consider creating independent system operators to plan traffic and rail connections.
  - ❖ ***No action.***

- Split the Polish Airports State Enterprise (PPL) into different entities, consider their privatisation, and introduce a formula for the transparent calculation of caps on take-off and landing fees.
  - ❖ ***PPL remains fully state-owned, but its corporatisation has started.***

Climate-change policies

- Equalise implicit and explicit carbon prices across sectors outside the EU-ETS, and align them to its prices, first by progressively eliminating tax exemptions for coal and gas for household use. Provide lump-sum cash compensation for the poor, and ensure that the costs of all negative global and local externalities are fully internalised by taxes on petrol, diesel and other fossil fuels.
  - ❖ ***No action. In July 2013, poor households became eligible for a lump-sum energy benefit.***

- Strengthen the price signal for investment by deepening the wholesale electricity market, improving cross-border interconnections and implementing a long-term plan for grid development.
  - ❖ ***A new connection of the electricity network with Lithuania is planned for 2015, and several international connections are included among the EU Projects of Common Interest for the period 2014-20.***

- Retain the cost-efficiency advantage of uniform support to renewables via green certificates.
  - ❖ ***The support scheme for renewable energy sources did not change.***

- Create a sustainable regulatory environment including: *i*) easing administrative burdens associated with connecting new generation capacity to the grid; *ii*) insulating the approval of the expert evaluation of the costs of future decommissioning and long-term waste disposal from political influence and strengthening the independence of the nuclear energy regulator by a fixed-term non-renewable nomination and during which he or she cannot be removed; *iii*) imposing and enforcing strict safety and environmental standards to minimise tail risks of nuclear energy; and *iv*) effective monitoring of environmental risks connected with the extraction of shale gas.

- ***Little progress has been made. Connections to the grid of micro-installations were exempted from fees in July 2013. Since 2012, applications for mining and shale gas extraction require provision of additional information about drilling technology and geological properties. An on-going project is monitoring the environmental effects of shale gas extraction to set mandatory requirements and recommend best practices.***
- ***Implementation in 2012-13 of amendments to the Atomic Law Act imposes strict safety and environmental standards in line with the 2012* Survey.**

Thematic chapters

Chapter 1

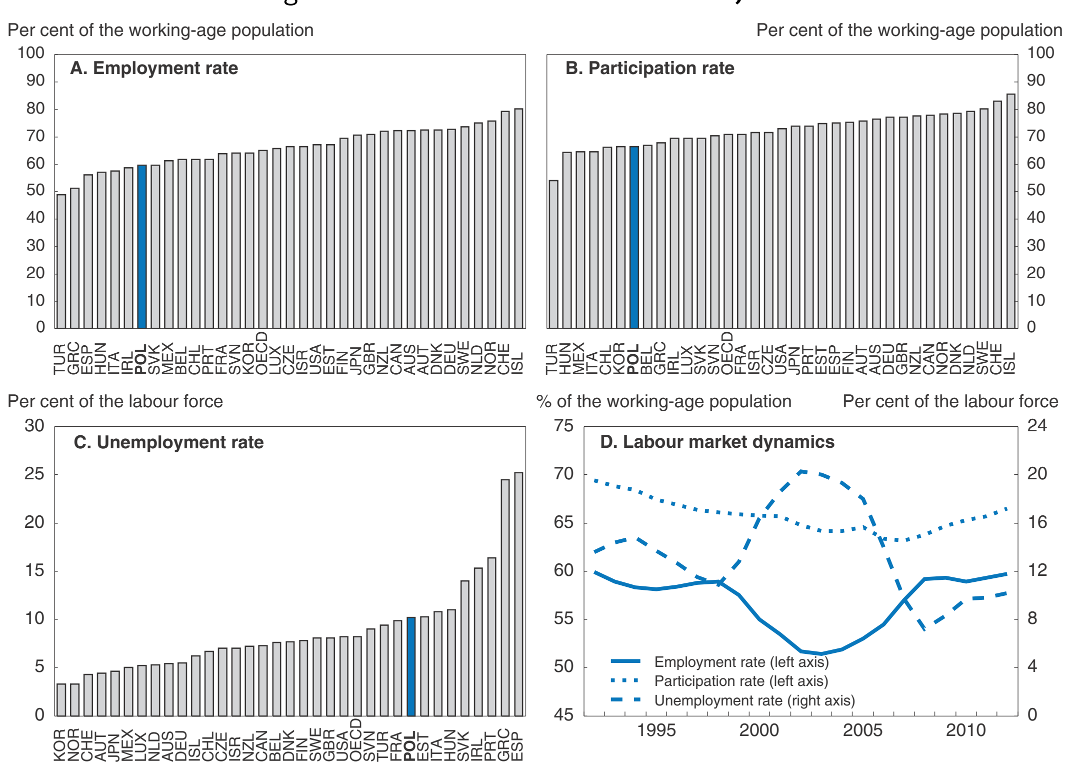
Making the labour market work better

Poor labour-market outcomes remain one of Poland's major structural weaknesses, impeding firms' competitiveness and the nation's potential output. Boosting employment prospects is also critical, as the country will soon be ageing at a fast pace. Despite long working hours, labour utilisation is only average due to structurally low employment rates, particularly at both ends of the age spectrum, with some marked regional differences. The female employment rate is especially low, in part due to poorly designed family and pension policies. Insufficient product-market competition and obstacles to internal mobility induce significant resource misallocation. Employment protection is not particularly stringent, but the labour market is nonetheless heavily segmented. This is likely to weigh on economic performance by limiting investment in human capital and making some specific groups bear a large share of adjustment costs. Public employment services suffer from a lack of resources and function inefficiently. Local labour offices have limited incentives to adopt best practices; the government plans to start benchmarking them. There is ample scope to tighten jobseeker obligations and reform social and tax policies to make work pay.

Boosting employment performance is key to enhancing Poland's economic prospects

Employment remains one of Poland's major structural weaknesses, impeding firms' competitiveness and the nation's potential output. The total employment rate, at 59.7% in 2012, is one of the lowest among OECD countries, resulting from both low labour-force participation and high unemployment (Figure 1.1). Poland ranks better in terms of labour utilisation measured as total hours worked per capita, close to the average of the top half of OECD countries in terms of GDP per capita (the metric used in *Going for Growth*), thanks to long average hours worked per employee, which are 23% greater than this top half average. All the main priorities for structural reforms identified by the OECD in its *Going for Growth* exercise (product-market competition, the tax structure and welfare system, infrastructure, education and housing) are relevant to enhancing labour market performance. Boosting employment prospects is also critical, because the country will be facing strong demographic shrinkage, given its low fertility rates and fast population ageing (Figure 1.2). The Central Statistical Office projects that between 2010 and 2035 total and working-age population will fall by 6% and 16%, respectively.

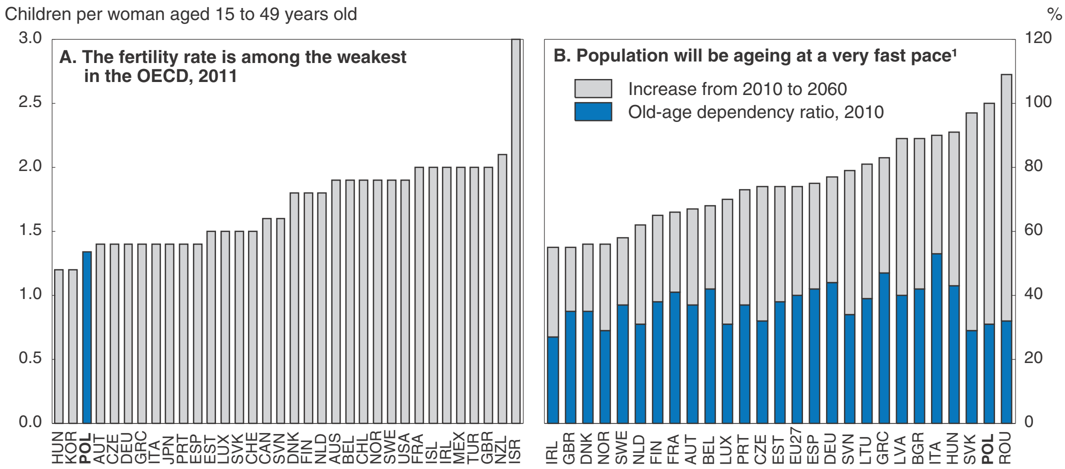
Figure 1.1. **Labour market indicators, 2012**



Source: OECD, *Labour Force Statistics 2013 Database*.

StatLink http://dx.doi.org/10.1787/888932999507

Figure 1.2. **Demographic prospects are unfavourable**



1. Effective economic old-age dependency ratio, measured as inactive population aged 65 and over as a ratio to the 20-64 employed population.

Source: OECD, *Population Statistics* and *OECD Health Indicators*; European Commission (2012), *The 2012 Ageing Report*.

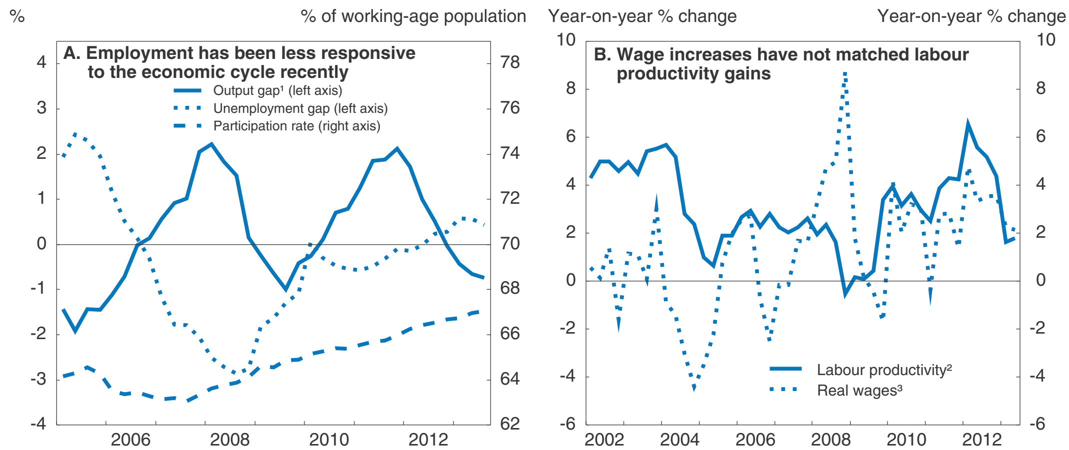
StatLink http://dx.doi.org/10.1787/888932999260

While the participation rate had fallen steadily between the beginning of the transition period and 2007, it has since increased by 3½ percentage points (Figure 1.1, Panel D). Beyond the favourable impact of relatively strong growth, the recent improvement in participation has been triggered by diminished accessibility to early-retirement and disability pensions, cohort effects related to the baby boom of the 1980s and a decrease in the labour tax wedge towards the OECD average level (OECD, 2012a).

The 2012-13 slowdown has left its mark on the labour market. The standardised unemployment rate rose as high as 10.6% in March 2013, up from a record low of 7.1% in 2008 when the economy was overheating (Figure 1.3). The strong growth in 2010-11 was insufficient to absorb the rise in participation, and the unemployment rate continued to rise. While the working-age population increased from 2008 to 2012 by 202 000 people (0.7%), the labour force surged by 846 000 (+5.1%), comprising rises of 273 000 in total employment (+1.8%) and 573 000 in unemployment. The latest unemployment rate (10.2%) is close to the OECD estimate of the NAIRU (Non-Accelerating Inflation Rate of Unemployment) level (10.0%), which remains one of the highest within the OECD. This suggests that the high level of unemployment is essentially structural, although current low inflation could mean that the NAIRU is overestimated, implying some slack in the labour market.

Poland's poor labour-market performance is due to particularly low employment rates at both ends of the age spectrum (Figure 1.4), with some marked regional differences. While the age structure of a country's employment rates is typically hump-shaped, with higher employment rates for prime–age people, Poland has a particularly marked hump (Panel D), translating into a high dispersion of employment rates across age groups (Boulhol and Sicari, 2013a). Limited labour supply is reflected in depressed participation rates for workers aged between 55 and 64 (between 35% and 50% in 2012, depending on the region). Moreover, the employment rate of older workers is especially weak for the less educated, and below 20% in some areas (Figure 1.5). More generally, the employment rate of workers with poor educational attainment is low overall and extremely low in some parts of the country. For example, for those aged between 25 and 34 with less than upper-secondary education, the range was from 37.5% in Kujawsko-Pomorskie to 57% in both Lubuskie (bordering Germany) and Malopolskie (bordering the Slovak Republic) in 2012.

Figure 1.3. **Recent growth has had a weak labour content**



1. As a percentage of potential GDP.
2. Labour productivity is measured as real GDP per worker.
3. Dependent employment.

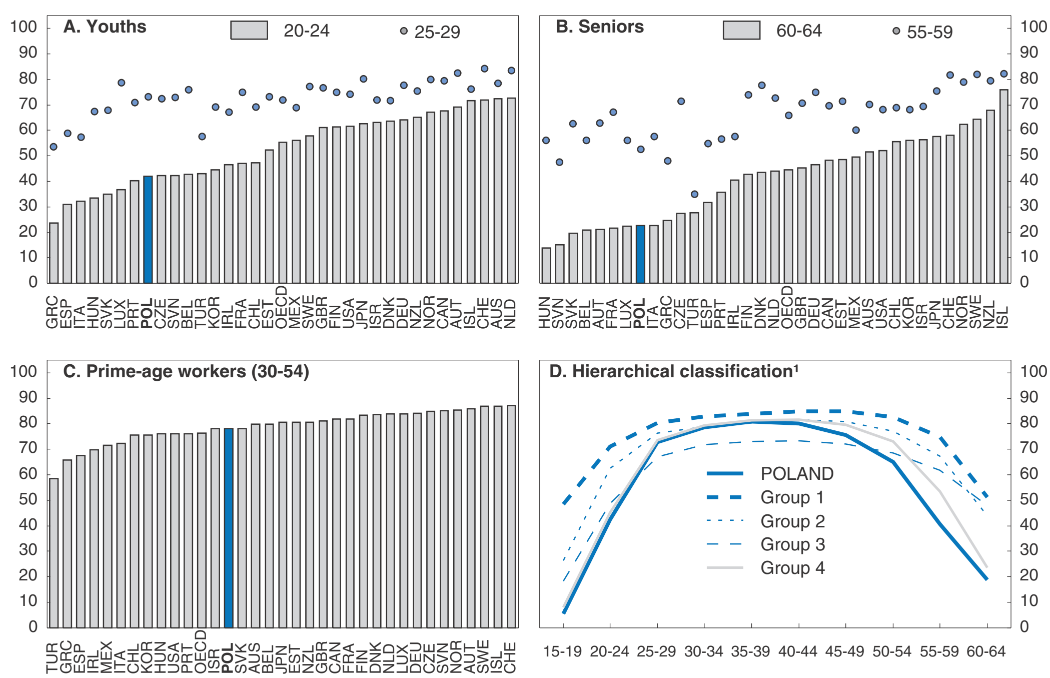
Source: OECD, *OECD Economic Outlook 94 Database*.

How to read this figure: See Figure 8 in the "Assessment and recommendations".

StatLink http://dx.doi.org/10.1787/888932999374

Figure 1.4. **Employment rates are especially low at both ends of the age spectrum, 2012**

As a percentage of the population by age bracket



1. A ranked classification was used to identify groups of OECD countries by the structure of employment rates by cohort; 2005-11 average. Group 1: AUS, CAN, GBR, DNK, NLD, ISL, NZL, NOR, CHE; Group 2: AUT, FIN, DEU, JPN, SWE, IRL, USA, MEX; Group 3: CHL, ISR, KOR; Group 4: BEL, LUX, POL, SVN, GRC, ESP, HUN, ITA, SVK, CZE, FRA, EST and PRT.

Source: OECD, *Labour Force Statistics 2013 Database*, and OECD calculations.

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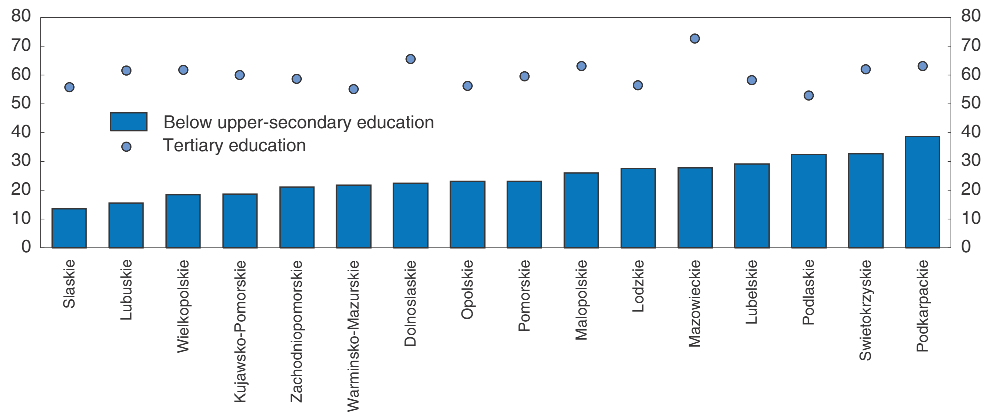
Figure 1.5. **Older workers' participation rates are low, especially for the low-educated in remote areas**

As a percentage of the 55-64 population



Source: GUS.

StatLink http://dx.doi.org/10.1787/888932999659

The specific labour market policy response to the crisis, which was in effect only between August 2009 and December 2011, was primarily aimed at limiting its impact on dismissals. The regulation of fixed-term contracts (FTCs) was modified and that of working time became more flexible. First, the Labour Code clause stipulating that only two consecutive FTCs were allowed, implying that a subsequent one was deemed permanent, was suspended. Moreover, following a decade-long debate (hence unrelated to the economic slowdown), a 24-month cap was introduced to the duration of FTCs. Second, the reference period for computing working time was extended from 4 to 12 months, a period during which employees could work shorter or longer weeks (without being paid overtime as long as total hours are below a specific threshold). This allowed for a better smoothing of the impact of economic fluctuations. Third, within the working day, starting and finishing times were also made more flexible. Fourth, employers experiencing temporary financial difficulties were provided with funding facilities and were allowed to reduce working time by up to 50% for a maximum of six months and were eligible for state assistance to partly compensate employees for lost income and training costs. However, this short-time work scheme was little used, because economic difficulties were relatively mild *ex post* and because the criterion used to define eligible firms (namely a fall of 25% in annual turnover) was too strict. Finally, spending on active labour market policies (ALMPs) was scaled up in 2009-10 to 0.45% of GDP per year, double the 2008 share. With the recent growth slowdown, the government implemented new measures in May 2013, providing direct financial assistance (*de minimis* aid) to employers experiencing a decrease in turnover.

This chapter highlights first the employment obstacles that extend beyond the realm of labour market policies. Indeed, a number of inefficiencies induce some substantial misallocation and waste of labour resources. Then, labour market policies to improve overall employment opportunities are discussed. The last part focuses on measures targeted at specific workforce groups.

Fostering a better allocation of resources

Increasing competition

Excessive product market regulation hinders productivity gains and the efficient allocation of resources both across firms within sectors and between sectors. It also affects job market performance. By expanding output, product market deregulation tends to boost aggregate labour demand, at least over the medium term, even though employment within the deregulated sectors might decline depending on the price-elasticity of sectoral demand (and therefore on substitution effects across consumed goods) (Fiori et al., 2012; Griffith et al., 2007). The most obvious depressive effects of product market regulations on employment are generated by barriers to entrepreneurship and administrative burdens. The broad reform undertaken by the Polish government to liberalise a large number of professions is thus likely to increase employment, but much more can be done to enhance competition: product market reforms should still feature prominently on Poland's employment-boosting agenda (Chapter 2).

Removing impediments to internal labour mobility

Regional differences in employment outcomes persist due to wage rigidities and impediments to labour mobility. The unemployment benefit system is more generous in high-unemployment districts (*powiats*), thereby potentially limiting internal migration flows towards more dynamic areas, whereas the minimum wage is undifferentiated across regions, despite differences in employment prospects, living costs and productivity. Moreover, in some cases social assistance provides high replacement rates (raising reservation wages), which are often not conditional on active job-search efforts (see below).

On top of this, the insufficient, though improving, quality of transport infrastructure prevents workers from commuting easily and responding to more favourable labour market conditions elsewhere. Indeed, despite some recent noticeable progress in developing road infrastructure, mostly financed by EU funds, internal labour mobility is still widely seen as insufficient, due in large part to the vastly underdeveloped railway system. Only 36% of railway lines in operation are in good technical condition (European Commission, 2013). The absorption of EU funds dedicated to modernising rail infrastructure has proved difficult, due to severe weaknesses in the governance of the state-owned incumbent operator (PKP SA) (see Chapter 2). The government investigated the possibility of reallocating a quarter of the dedicated funds to road construction, even though only 25% of the 2007-13 related programmes was initially allocated to rail (versus 57% for road), but the European Commission did not allow it. For the 2014-20 period, priority has to shift decisively towards upgrading rail infrastructure, as well targeted investments in this area will yield high returns beyond reducing greenhouse gas emissions.

The functioning of the housing market was analysed in depth in the 2008 *Survey* (OECD, 2008a; Kierzenkowski, 2008). Expensive housing in urban areas related to weak housing policies is a severe obstacle to relocating and thus to a better integrated national labour market. Poland is one of the OECD countries with the lowest housing per capita (Andrews et al., 2011a). Moreover, the high share of owner occupancy tends to reduce mobility. In 2013, the government submitted to the parliament an amendment that would introduce a voucher that would help people under 30 years old to cover housing expenses upon accepting a job offer involving a change in residence. However, no clear progress has been made in addressing the lack of supply in the private urban rental market. In 2010, the government lifted some rent restrictions for subletting and generalised the lower 8.5% tax rate on rental income to curb the informal rental market. Efforts should focus on the following actions set out in *Going for Growth* (OECD, 2013a). The release of zoning plans by municipalities should be made mandatory, as their absence generates lengthy administrative procedures and encourages local corruption. Taxes on housing purchases should be replaced by *ad valorem* property taxes. On the other hand, compulsory escrow accounts to protect buyers' advances in case of developer bankruptcy were introduced in 2012, consistent with OECD's recommendations. Finally, rent controls and tenants' protection should be further relaxed.

Reducing the distortions generated by the farmers' social insurance system (KRUS)

The KRUS was established in 1991 to provide low-income farmers with the same level of pensions and social benefits as people under the general social security system (ZUS), but for a much lower contribution. It has become a permanent source of income for farmers and their families, because of benefit sharing, as well as an implicit subsidy to agriculture, thereby slowing consolidation in the sector. In 2007, the average size of a Polish farm was about half that of farms in the European Union, and only 1% of farms were larger than 50 ha as against 5% in the EU27 and 11% in the EU15. However, things have improved since then, with the number of Polish farms being reduced by 16% between 2007 and 2010. Yet, agriculture still accounts for about 12.5% of total employment. Overall, the KRUS allows some low-productivity workers to remain in rural areas. Furthermore, with its labour productivity reaching only 16% of the EU15 level, Poland's agricultural sector is the least productive of all European OECD members.

Two laws that came into force in January 2013 will generate marginal changes. Health-care contribution rates for so-called special agricultural production activities were increased, but remain small; the possibility to benefit from early retirement (women at 55, men at 60) will be gradually eliminated; and the disincentive to undertake a non-farm job for farmers receiving disability benefits is being reduced. On the other hand, a new pre-retirement allowance was introduced for women and men aged 62 and 65, respectively, amounting to half the regular farmers' pension. Clearly, much more is needed. Accession to the EU in 2004 and thus eligibility for the Common Agricultural Policy (CAP) regime and the Structural and Cohesion Funds should have been an attractive opportunity to phase out the KRUS. Indeed, excluding KRUS expenditures but including CAP transfers, the share of agriculture in state budgetary expenditure increased from an average of 2.2% in 1997-2003 to 7.4% in 2008-10, with the application of CAP instruments alone having doubled farmers' real incomes (Nurzynska, 2012). Special rules regarding KRUS eligibility based on land ownership and the nature of the farming activity should be abolished, and treatment under the KRUS and the ZUS should converge steadily.

Downsizing the informal economy

Poland has been identified as one of the OECD countries where informal employment poses the most serious challenges (OECD, 2008b). According to the broadest study (Bühn et al., 2010, updated by Schneider, 2013), the shadow economy represents about 24% of Polish GDP, behind only Estonia, Turkey and Mexico among OECD countries. However, the methodology used in these widely referenced papers is subject to serious limitations, potentially leading to upward biases (Andrews et al., 2011b). In contrast, according to estimates by the Central Statistical Office (GUS), the shadow economy was about 13% of

GDP in 2010, while the number of people admitting to informal work decreased from 9.6% of total employment in 2004 to 4.6% in 2010. Nevertheless, according to Andrews et al. (2011b), based on various proxies, the size of the informal economy is probably high relative to other OECD countries.

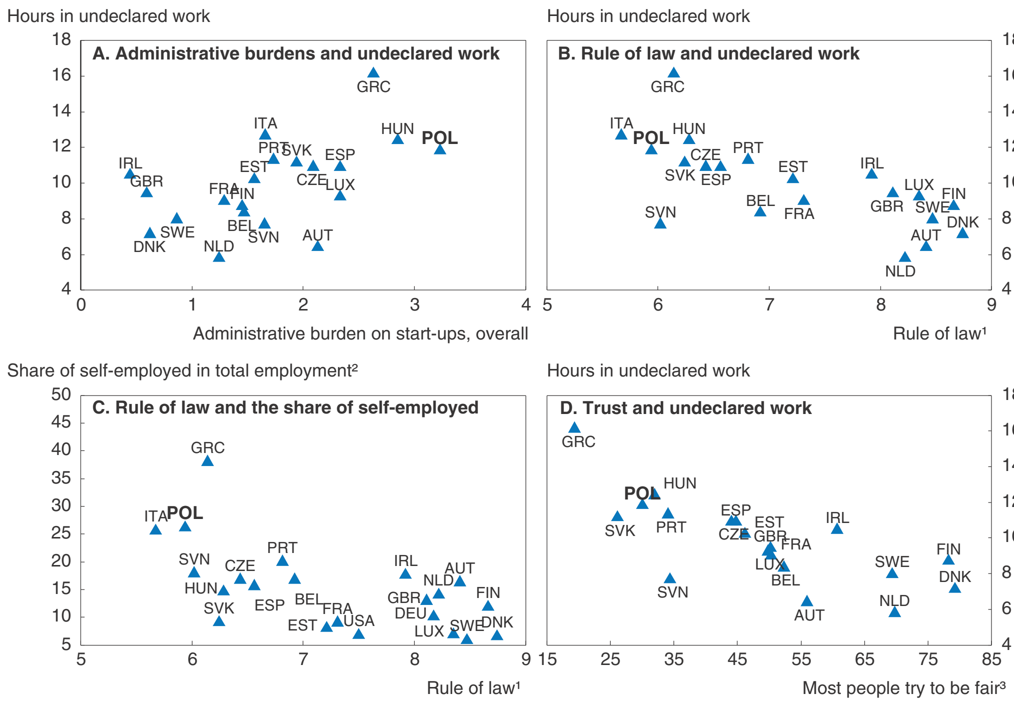
Informal employment is a significant labour-market problem for a number of reasons (see e.g. OECD, 2008b; and Andrews et al., 2011b) for a more detailed treatment). People working in the shadow economy have typically limited social protection and tend to face a high level of income insecurity; they are therefore more exposed to poverty risks. The shadow economy represents a shortfall in terms of tax revenues, limiting the quality of public services and putting greater tax pressure on the formal sector. It therefore induces distortions, as informal firms benefit from unfair competition advantages.

Under-declaration of income is widespread in Poland (although tax compliance has improved), and a large number of employees working in small firms do not have a written employment contract (OECD, 2008b). Informal employment seems to be triggered by the lack of job opportunities in the formal sector, but also by the potential for greater disposable income (Mroz, 2010; Walewski, 2011), owing to the avoidance of income tax and social security contributions, and the existence of unconditional provision of social assistance and the favourable treatment of the self-employed.

Policies and institutions can shape the incidence and scope of informal employment, and the authorities could act in the following dimensions to curb its costs. *First*, tax regulations should be simplified, as the complexity of the Polish tax system is regularly identified as a major obstacle to conducting business (OECD, 2010a; World Bank, 2013; World Economic Forum, 2013). Complex tax systems increase compliance costs, create opportunities for exploiting loopholes and increase collection and monitoring costs. Moreover. the monitoring and enforcement of the tax system should be enhanced to limit tax avoidance and evasion: unsurprisingly, the incidence of informality seems to be higher in countries where the expected penalty for not declaring earned income to the tax or social security authorities is less severe (OECD, 2008b). Even compared with other Central and Eastern European Countries, audit staffing and activity is underdeveloped in Poland and co-ordination between the tax, social security and labour-inspection agencies, which is a key enforcement mechanism, is insufficient (OECD, 2008b). *Second*, the advantages granted to the self-employed should be reduced, as self-employment facilitates tax avoidance and evasion. On top of the many exemptions and deductions in the personal and corporate income taxes, four different preferential tax and social contribution regimes exist for the self-employed, which are likely to favour gaming and abuse (OECD, 2008b). *Third*, significant barriers to market entry and costly administrative procedures (see Chapter 2) need to be removed, as they encourage unregistered work and under-declaration of income (Figure 1.6, Panel A).

Fourth, unemployment contributions should be reduced and part of the spending they currently finance funded from other sources. Indeed, unemployment benefits (UB) are very loosely related to contributions (see below), which does not encourage formal employment. Moreover, UB spending represents only about one quarter of contributions due to their low level and strict access conditions, and because contributions are also used to fund active labour market programmes and early-retirement schemes. *Fifth*, as already mentioned, the KRUS should be reformed, as it induces people to hold onto small plots of land even when not being active in farming, thereby encouraging underground employment. *Finally*, the rule of law should be strengthened. Andrews et al. (2011b) highlight a significant cross-country

Figure 1.6. **The informal economy**



1. Rule of law refers to Area 2 (Legal Structure and Security of Property Rights) of the Economic Freedom of the World Index. This index is based on seven components: judicial independence, impartial courts, protection of property rights, military interference in rule of law and the political process, integrity of the legal system, legal enforcement of contracts and regulatory restrictions on the sale of real property.
2. Average for the period from 1995 to the most recent observation.
3. The horizontal axis shows the proportion of respondents who answered they expect that most people try to be fair.

Source: Andrews et al. (2011b), "Towards a Better Understanding of the Informal Economy", *OECD Economics Department Working Papers*, No. 873.

StatLink http://dx.doi.org/10.1787/888932999678

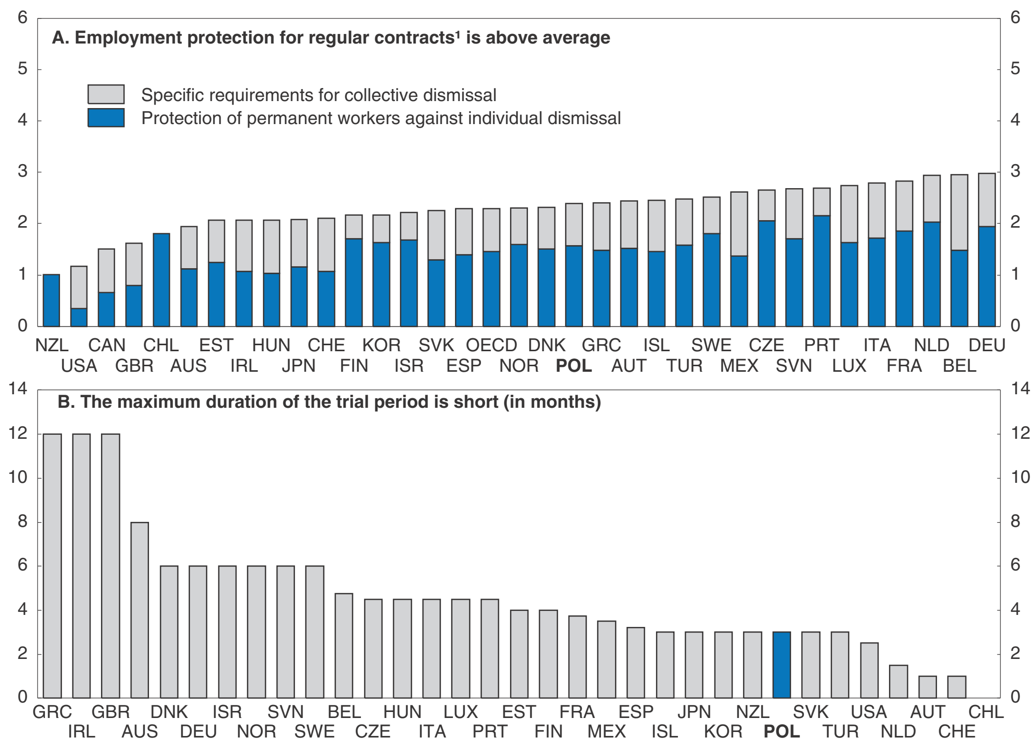
correlation between the size of the informal sector and the effectiveness of institutions securing property rights, establishing an impartial judiciary and limiting corruption (Figure 1.6, Panels B and C). Also, hours in undeclared work tend to be higher in countries where there is a perception that few citizens play fair, a proxy for the degree of trust between citizens and public authorities (Panel D). Improving government effectiveness and fighting corruption by improving trust in government can raise the willingness to pay taxes and more generally play an important role in reducing informality.

Labour-market policies to improve overall employment

Employment protection is deeply segmented

Employment protection legislation (EPL) is an important determinant of labour market outcomes. Poland is close to average in terms of EPL stringency for permanent contracts (Figure 1.7, Panel A). In case of dismissal, the union representative must be notified, the maximum length of the notice period is average and severance pay low. Regulation related to the definition of unfair dismissal is also one of the least constraining among OECD countries (OECD, 2013b), but legal procedures in case of disputed separation are long and their outcomes highly unpredictable. Re-employment obligations in case of unfair

Figure 1.7. **Employment protection, 2013**



1. Index scale of 0 to 6, from least to most restrictive; the indicators are displayed in their weighted version.
Source: OECD, *Employment Protection Legislation Indicators Database*.

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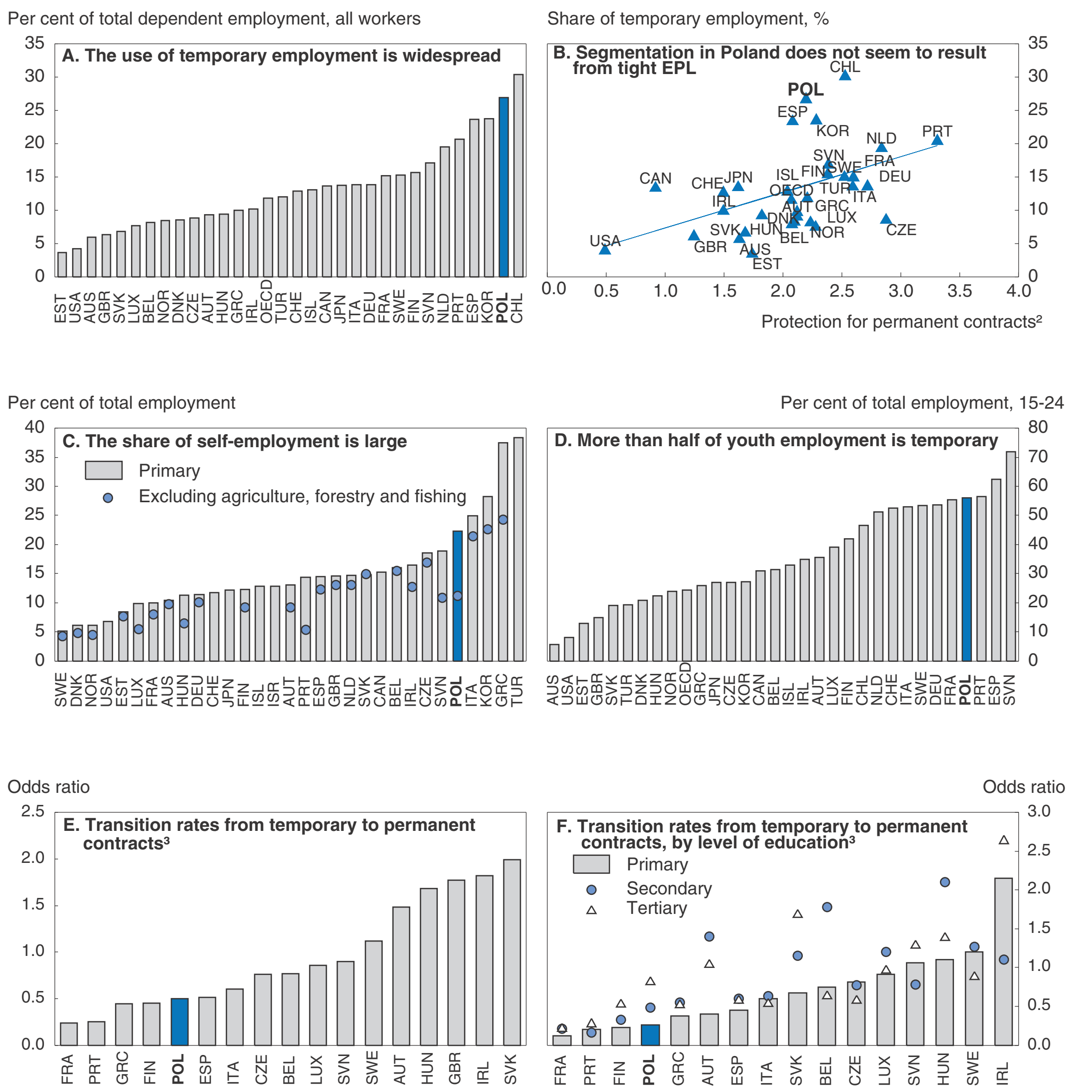
dismissals are heavy, although reinstatement is not often imposed by the court. The ceiling of three months on trial-period contracts, which can be used before an open-ended or fixed-term contract is offered, is one of the shortest, potentially limiting both hiring and the quality of matching (Panel B).

The labour market is heavily segmented and in a rather complex way. The share of temporary employment in total dependent employment is above 25%, a level exceeded only in Chile (Figure 1.8, Panel A). Regulations pertaining to fixed-term contracts (FTCs) have been lax since the reforms conducted between 2001 and 2003. In particular, since the end of 2011, there has been no duration limit either for a given FTC nor for their maximum cumulative duration. These soft provisions have fuelled a sharp increase in the incidence of temporary contracts from about 10% of total dependent employment in 2001 to more than 25% since 2005. After numerous changes since the end of the 1990s, a third consecutive FTC now triggers an automatic conversion into an open-ended contract, provided there has not been a break of more than one month – which is rather short – between them.

The reasons why FTCs are so widely used are not totally clear. *Prima facie*, the strictness of regular employment regulations does not provide a convincing explanation (Panel B). Rather, persistently high structural unemployment is likely to have contributed to this phenomenon by weakening workers' bargaining power and prompting them to accept offers for relatively precarious jobs.

In addition, 22% of the employed population is self-employed, which is also one of the highest in the OECD, although it has fallen since the mid-1990s when it stood at 30%

Figure 1.8. **The labour market is heavily segmented, 2012**[1]



1. For Panels A, C and D: 2011 for Korea; 2009 for Sweden and 2005 for the United States (limitedly to the temporary employment series for the latter).
2. Against individual dismissal.
3. Odds ratio moving to permanent vs. remaining in temporary contract; average 2005-07.

Source: OECD, *Labour Force Statistics Database* and *OECD Economic Outlook 94 Database*; Eurostat (2010), *Employment in Europe 2010* (for Panels D and E).

StatLink http://dx.doi.org/10.1787/888932999716

(Figure 1.8, Panel C). Self-employment was boosted by restructuring policies during the transition period, but the extensive use of this form of work reflects both the high share of individual farmers as well as the desire to avoid social-security costs and termination requirements (Trappmann, 2011). Indeed, on top of permanent and temporary contracts governed by the Labour Code, employment relations can take the form of a contract lightly regulated under civil-law provisions. Civil-law employment is less costly for employers and can be more rewarding in the short term for the "self-employed" employees, as it is subject to limited social-protection requirements, including social security contributions. It also escapes minimum-wage regulations. There has been a tendency by employers to "convince" employees to conduct the same work as self-employed providers under civil-law contracts (Zientara, 2008), which infringes the Labour Code and could theoretically trigger sanctions by labour inspectors. Kwiatkiewicz (2008) refers to "bogus" self-employment. According to her definition, a self-employed person is someone who provides services for his/her client(s) through a commercial contract, while self-employment is bogus if the relation is *de facto* one of subordination (dependent employment). These contracts (called "trash contracts" in Poland) represented 30% of total self-employment (i.e. about 7% of total employment) in 2012. Among non-agricultural workers declaring revenues from only one source, about 11% are civil-law contractors. The government plans to subject all civil-law contracts to social security contributions up to a salary equivalent to the full-time minimum wage. This would be a first step in the right direction.

While greater labour market flexibility might have fuelled employment growth between 2003 and 2007 (Ingham and Ingham, 2011), such profound dualism has its flip side and is likely to weigh heavily on other aspects of economic performance. The extensive use of temporary contracts might be detrimental to investment in human-capital formation by both employers and employees. Temporary employment is especially widespread for young workers (Figure 1.8, Panel D), and such a high incidence seems to lengthen school-to-stable-work pathways and make them more erratic (OECD, 2009). Fixed-term contracts seem to serve more as a screening device than a stepping stone to an open-ended job (Baranowska et al., 2011; Figure 1.8, Panels E and F). More generally, labour-market dualism might make some specific groups, in particular the young and low-skilled workers, bear a disproportionate part of the costs of adjustment to economic shocks. It might also induce in-work poverty, which is prevalent in Poland (European Commission, 2012b). Raising social contributions for FTCs and lowering them for permanent contracts (such that total labour taxes remain constant) would allow internalising some of the social costs induced by the disproportionate use of FTCs, while neutralising the total impact on the labour tax wedge.

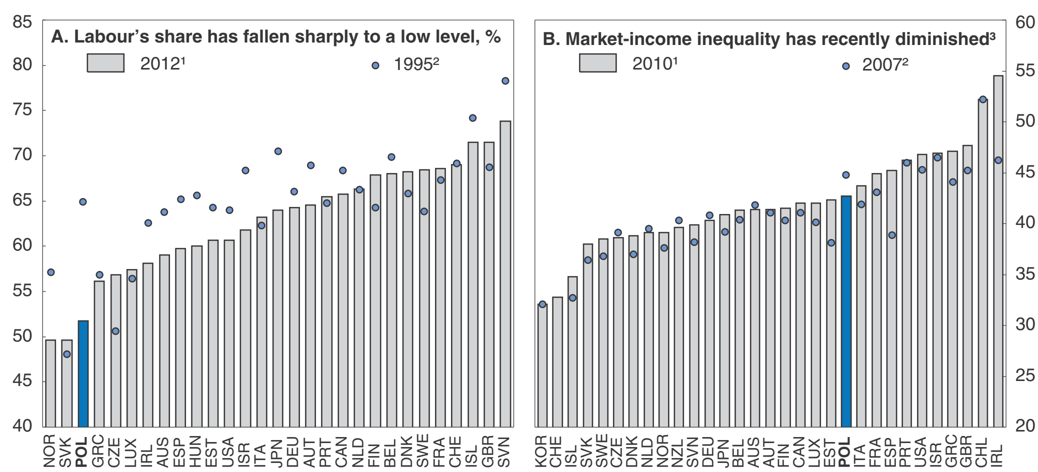
One form of temporary employment, temporary work agency (TWA) employment, faces important restrictions, which should be eased: it is allowed only for tasks whose timely performance by the company's permanent staff would be impossible. TWA workers can perform only seasonal work, ad hoc assignments, tasks that cannot be completed on time by the company's regular workers, and as replacements for a company's long-term absent employees (OECD, 2013c); setting up a TWA requires special administrative authorisation and entails periodic reporting obligations; and TWA employees cannot be treated less favourably than regular employees, including in terms of remuneration (OECD, 2013b). Consequently, and given FTCs' flexibility, TWA employment is not well developed, covering less than 2% of total employment (Trappmann, 2011).

Finally, until recently rules, concerning maximum working hours were relatively stringent. Basic working time is limited to an average of 40 hours over a five-day working week within a reference three-month period. An employee working overtime is entitled to a top-up of 50% (or 100% depending on the time and day). In exchange for overtime work, it is possible to grant compensatory time off to the employee. Work on Sundays and public holidays is restricted. The September 2013 law permanently amending the "Working Time" Chapter of the Labour Code increases working-time flexibility, thereby allowing firms to better cope with fluctuations in demand. The main change refers to the extension from three to 12 months of the reference period used to compute working-time limits, conditional on an agreement involving unions or employees' representatives at the branch or company level.

Alleviating the wage distortions affecting labour utilisation

Since 2002, wage increases have not matched the pace of labour productivity gains in any year except in 2008, thereby improving cost competitiveness (Figure 1.3). Thus, the labour share of national income has fallen steadily, leading to one of the lowest levels in the OECD (although level comparisons should be interpreted carefully) (Figure 1.9, Panel A). High unemployment, greater trade openness, privatisation and the free-fall in unionisation from 36% in 1990 to 15% in 2010 have lowered unions' bargaining power and might explain why workers have not reaped the full gains from faster economic growth. Moreover, economic inequalities have increased substantially since the end of the 1990s across a broad array of inequality measures (Brzezinski and Kostro, 2010), although Poland is one of the few OECD countries to have recorded a reduction in market-income inequality since 2007 (Figure 1.9, Panel B).

Figure 1.9. **Labour share and income inequality**



1. Or latest year available.
2. Or closest year available.
3. Gini index before taxes and transfers, working-age population.

Source: OECD, *OECD Economic Outlook 94*, *OECD Income Distribution and Poverty Databases*.

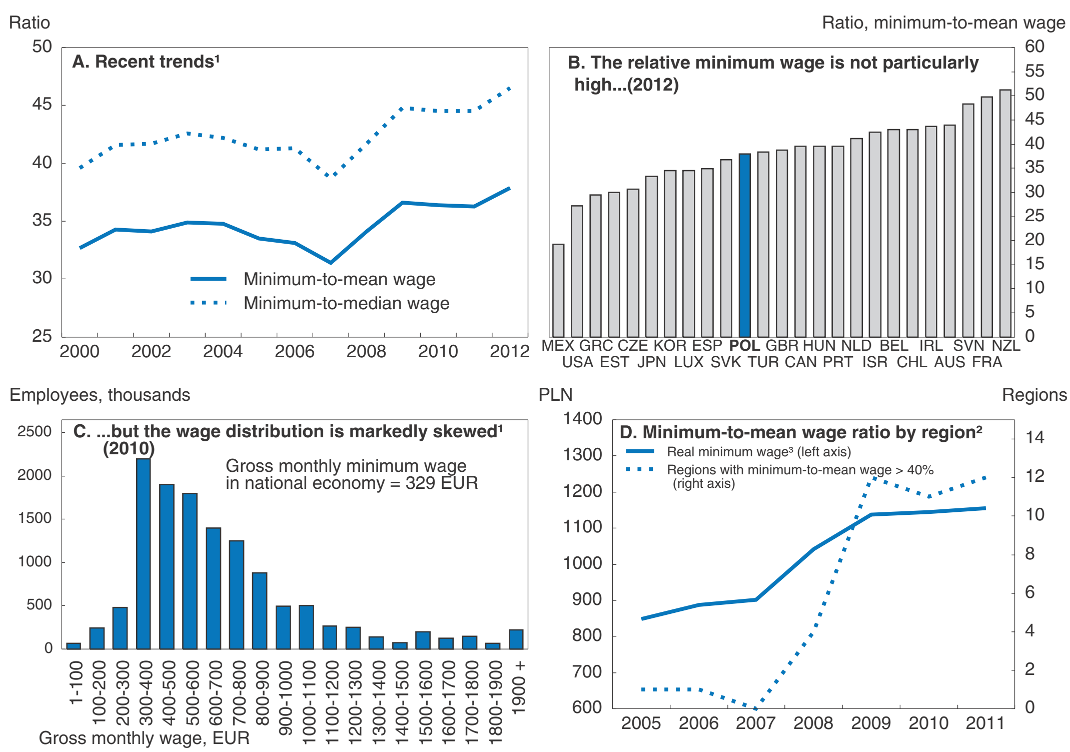
StatLink http://dx.doi.org/10.1787/888932999735

The wage distribution is much more compressed in the public than in the private sector, even when controlling for educational attainment. The private sector offers higher wages on average to the most qualified workers, while the public sector pays relatively higher wages for the low-skilled (Ministry of Labour and Social Policy, 2008). For example, monthly earnings of cleaners working in the public administration are on average more than 40% higher than in the industrial sector. Caretakers, janitors and porters earn about 15%, 30% and 60% more, respectively, in public administration. On average, despite the restraint imposed on the public-sector wage bill since 2009, the average compensation rate of public employees remains high in relative terms at about 150% of the average private-sector compensation compared with 100% at the end of the 1990s. Moreover, pay tends to increase faster with seniority in the public sector, reflecting more rigid compensation schemes that might not reflect individual productivity. These features are likely to generate inefficiencies in the allocation of labour resources.

Private-sector coverage by collective agreements is relatively low at about 40% compared with an OECD average of 53%, and wage bargaining is to a large extent decentralised to the firm level, similar to the situation in Hungary, the United Kingdom and the United States (Du Caju et al., 2008). The main source of private-sector wage rigidities is the minimum wage. It is negotiated first within the Tripartite Commission and then between the Commission and the Council of Ministers, which has the final say. By law, the minimum wage is indexed to inflation, plus at least two-thirds of real GDP growth as long as the minimum-to-mean wage ratio is lower than 50%. Unions have an explicit target of 50% for the minimum-to-mean wage ratio, and even though they are relatively weak, except in some occupations such as miners and teachers, they have fairly strong nationwide political power and exert pressure on the government in the minimum-wage-setting process.

On the one hand, the minimum-to-mean wage ratio, equal to 38% for full-time employees in 2012, is not high by international standards (Figure 1.10, Panels A and B). On the other hand, the wage distribution is clearly skewed, suggesting that the minimum wage might be an important constraint (Panel C). While the minimum-wage level is unlikely to affect labour demand substantially in the relatively rich Mazowieckie region, for example, it might penalise employment opportunities for youth and the low-skilled in remote high-unemployment areas (Panel D). A uniform minimum wage is at odds with the fact that the productivity of a given individual may vary geographically because of agglomeration effects,

Figure 1.10. **Minimum wage**



1. Data on the wage distribution should be interpreted with caution, as the underlying survey covers only firms with at least 10 employees.
2. The graph shows the increasing number of regions in which the minimum-to-mean wage ratio exceeds 40%.
3. Deflated by the CPI.

Source: OECD, *Minimum Wage Database*; Ministry of Labour.

StatLink http://dx.doi.org/10.1787/888932999754

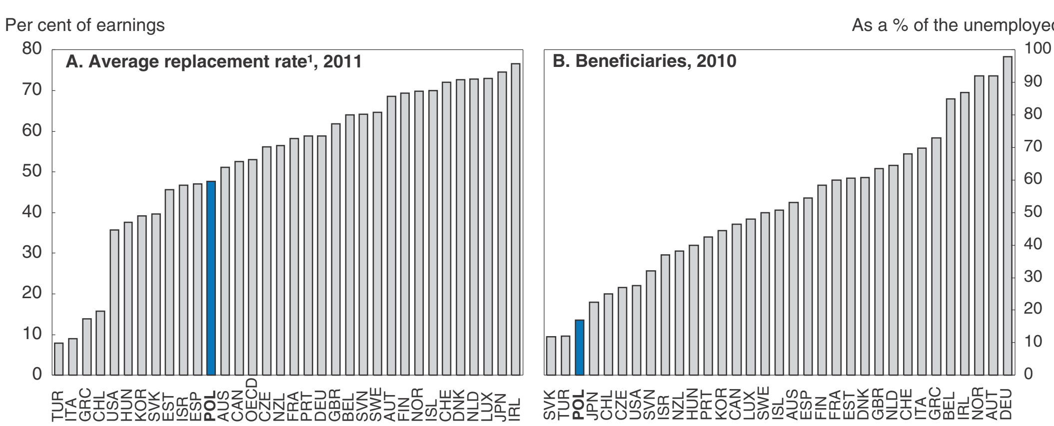
amply documented in the economic geography literature (Fujita et al., 1999; Melo et al., 2009). The cost of living also varies greatly across the country, implying large regional differences in the purchasing power of the minimum wage. Therefore, as suggested in past *Surveys* of Poland (e.g. OECD, 2010a), performance might be improved by decentralising minimum-wage setting to the regional level, especially given persistently low internal mobility. However, given that the heterogeneity of employment performance is also substantial within regions, regionalised minimum wages might help only partially.

Better activating the unemployed

The unemployment benefit system has strict eligibility rules, but some features should be modified

Eligibility for the unemployment benefit (UB) system is strict, and replacement rates are typically low (Figure 1.11, Panel A). To be eligible, an unemployed person needs to register at the local labour office and have a year's work history during the 18-month period preceding registration and be paid at least the full-time minimum wage, thereby excluding most part-time workers. Overall, in 2012 fewer than 20% of registered unemployed were entitled to UB, much less than in most other OECD countries (Panel B). UB is thus unlikely to reduce employment incentives substantially, except potentially for specific groups (see below). The benefit is a flat-rate payment, i.e. unrelated to past individual wages and contributions, which are equal to 2.45% of gross wages. In 2012, UB amounted to slightly more than half the minimum wage for the first three months and is diminished by 20% after that. The benefit is reduced (increased) by 20% for those having less than five (more than 20) years of work experience. For those who were paid close to or above the average wage, this implies very low replacement rates. The entitlement period lasts six months, but it is extended to 12 months in three cases: in districts where the unemployment rate exceeds 150% of the national rate; if the unemployed person is over 50 with at least 20 years of work experience; or if s/he supports a child under 15 and the spouse is also unemployed but no longer eligible for UB.

Figure 1.11. **Unemployment benefit is not generous**



1. Average of the net replacement rate in the first five years of unemployment for four different family types (single and one-earner couples, with and without children) and two earning levels (67% and 100% of average full-time wages). Unemployment benefits plus cash social assistance.

Source: OECD, *Benefits and Wages Database*; ILO.

StatLink http://dx.doi.org/10.1787/888932999773

The longer UB eligibility for senior workers and in districts with higher unemployment may reduce labour supply, especially given the uniformity of the minimum wage level. Moreover, based on international evidence (RWI, 2005), geographically differentiating the length of the UB period discourages internal migration from high-unemployment areas, although there is no specific study focusing on Poland.

There are strong incentives to register as unemployed despite meagre UB, even if one is not looking for work. While the principle of universal health-care coverage is enshrined in the constitution, the unemployed need to register at the local labour office in order to get health-care coverage for themselves and their families. Registering also allows easier access to social assistance. This creates a situation where some people who are not searching for a job and do not want to work (or might even be working informally) register just to get the insurance. More than 25% of the registered unemployed might be in that situation, according to the Ministry of Labour (PNB, 2013). This feature explains a large proportion of the 3 percentage-point gap between the LFS and the registered unemployment rates. It also implies that some job-search support is bound to fail (because some registered unemployed do not want to find a job), thus discouraging both public employment service (PES) staff and employers posting job offers. Therefore, disconnecting entitlement to health insurance from unemployment registration would help.

The unemployed are theoretically required to accept any suitable job offer – defined as one for which daily commuting time would not exceed three hours – and cannot restrict job search to the occupational field or level of his/her professional qualifications. However, in practice the PES does not refer the unemployed to jobs for which they are distinctly over-qualified. Moreover, monitoring of job-search activity is minimal. While the unemployed must be ready to take up full-time employment and the sanctions in the case of refusal of employment or participation in ALMPs are relatively severe, there are generally no formal job-search requirements apart from being registered as unemployed, reporting to the labour office at designated dates to confirm availability and receive information on employment and training opportunities, and accepting job offers, training or other forms of support (Venn, 2012). OECD *Surveys* of Poland (e.g. OECD, 2008a) have previously recommended tightening work-availability and job-search requirements, but there has been no follow-up action.

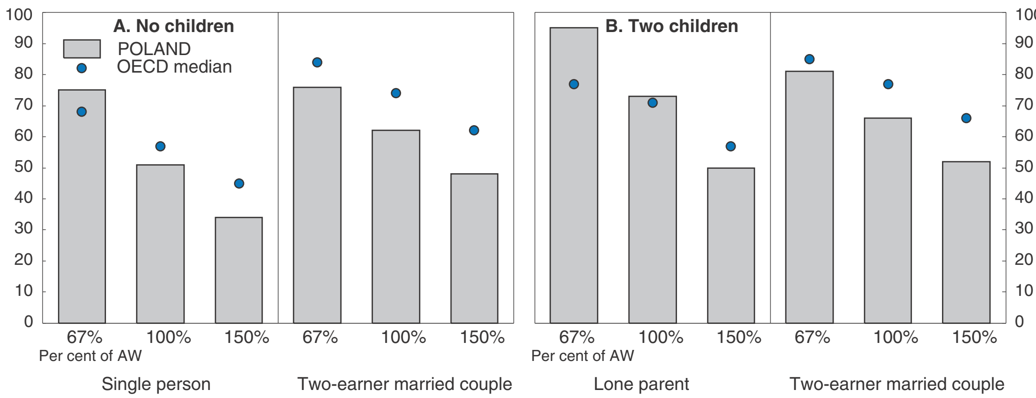
Making work pay

Housing benefits, family benefits and other social assistance (apart from KRUS and old-age, disability and survivors' pensions, which are discussed elsewhere in this chapter) are relatively well targeted. As discussed above, the replacement rates for unemployment benefits alone are low, especially for those with previously high earnings. However, when unemployment benefits are combined with other transfers, situations arise where replacement rates become very high. This is the case for low-wage earners, and especially so for lone parents (Figure 1.12). This nexus can therefore produce strong disincentives to take a job.

The labour tax wedge has been reduced (through lower personal income tax in 2009) toward the OECD average level, though the increase in disability contributions from 6% back to 8% in 2012 (after 13% in 2007) worked the other way. More precisely, the average tax wedge is slightly above the OECD average, while the marginal tax wedge is slightly below it (Figure 1.13). Yet, given that labour taxes are among the least progressive in the OECD, such tax-wedge levels tend to apply also to low wages, thus penalising low-skilled employment significantly, especially in regions where the minimum wage acts as a binding constraint. Overall, making some social-assistance benefits (such as childcare subsidies) conditional on working or on seeking work and introducing a targeted earned-income tax credit would improve work incentives.

Figure 1.12. **Overall net replacement rates are high only for those on low wages**[1]

Families qualifying for social assistance,[2] 2011



1. Initial phase of unemployment but following any waiting period. Any income taxes payable on benefits are determined in relation to annualised benefit values, even if the maximum benefit duration is shorter than 12 months. For married couples, the percentage of average wages (AW) relates to the previous earnings of the unemployed spouse only; the other is assumed to have full-time earnings equal to 67% of AW in a two-earner couple. Where receipt of social assistance or other minimum-income benefits is subject to activity tests (such as active job-search or being available for work), these requirements are assumed to be met. Children are aged four and six, and neither childcare benefits nor childcare costs are considered.
2. After tax and including unemployment and family benefits. Social assistance and other means-tested benefits are assumed to be available subject to relevant income conditions. Housing costs are assumed equal to 20% of AW.

Source: OECD, *Tax-Benefit Models*.

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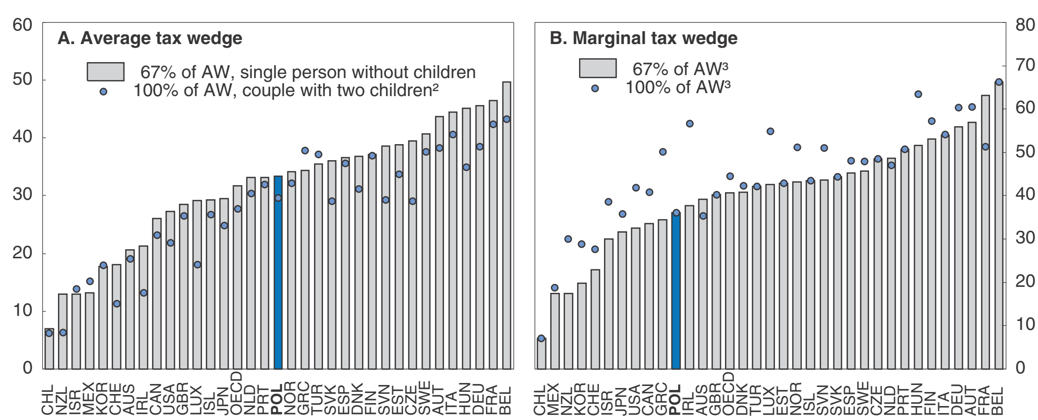
Figure 1.13. **The average tax wedge is slightly above OECD average, while the marginal tax wedge is lower,**[1] **2011**



1. The average tax wedge is measured as the difference between total compensation paid by the employer and net take-home pay, as a ratio of total labour compensation. It includes both employer and employee social contributions. The marginal wedge is measured as the difference between the changes in total labour compensation paid and in net take-home pay, as a result of an extra unit of labour income. The difference is expressed as a percentage of the change in total labour compensation.
2. Couple with two children, at 100% of average worker earnings for the first earner. Average of three situations regarding the wage of the second earner (0%, 33% and 67% of average worker earnings).
3. Single person without children.

Source: OECD (2012), *Taxing Wages Database*.

StatLink http://dx.doi.org/10.1787/888932999811

Enhancing the functioning of public employment services and improving active labour market policies

The public employment service (PES) system is at least in principle largely decentralised. It is run by 340 labour offices operated by the 16 regional and 380 district administrations. The Ministry of Labour and Social Policy sets regulations and co-ordinates the PES across the different actors, but labour offices are autonomous and define programmes in their geographical area. About 80% of PES resources come from the Labour Fund, which is managed by the Ministry and financed by unemployment contributions and to a small degree (about 6%) by EU funds, with the remainder from local governments. The Ministry allocates the Labour Fund's resources to the regions depending on various local unemployment data, and each region in turn allocates resources to the labour offices, which determine detailed eligibility criteria and manage benefit payments.

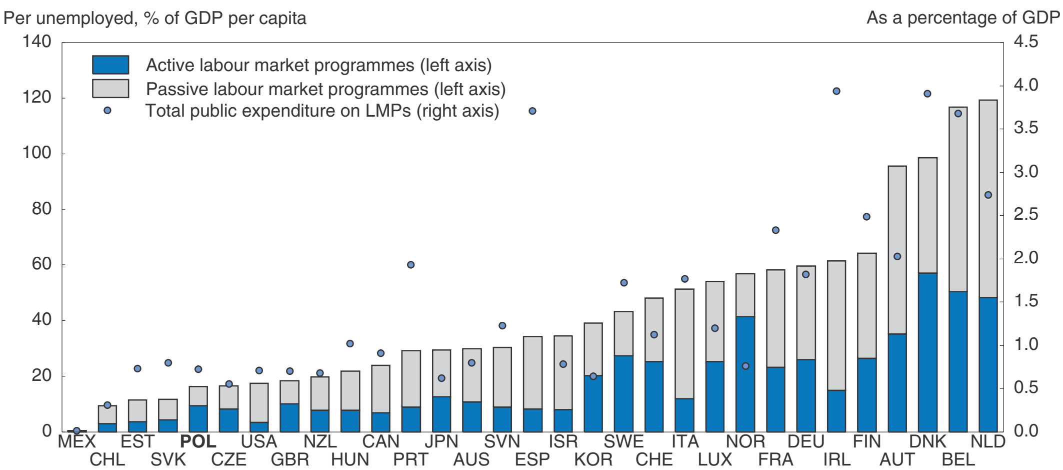
There is a broad consensus that the PES works poorly in Poland (Kaluzna, 2009). First, it lacks resources, suffering in particular from under-staffing. Although the situation has improved, workload indicators still paint a bleak picture. In 2012, each placement officer supervised as many as 595 registered unemployed on average (against 1 132 in 2006 and 1 637 in 2000). Second, although insufficient, available staff resources are not used efficiently: a vast number of them work on back-office administration tasks and even those in the front-line placement functions are burdened by excessive bureaucracy (Kaluzna, 2009). In addition, high staff turnover, driven by unattractive compensation and by the instability of labour market programmes, generates heavy losses in human capital at PES offices. Third, most staff seem to lack the skills required to achieve a good level of job-search support (Grotkowska and Sztanderska, 2008; Trappmann, 2011), in part due to cronyism in the recruitment process (OECD, 2009). The situation might have improved recently, however, given the increase in the share of employees with a higher education level. Nonetheless, local governments' labour offices and social assistance centres seem to have a poor understanding of the overall labour market situation, in part due to the lack of relevant information and their staffs' inadequate analytical skills (Kaluzna, 2009). This is unfortunate, as international evidence suggests that a high standard for PES staff is a crucial ingredient for efficient activation.

As a result, monitoring of job-search efforts is weak (Venn, 2012), and occupational counselling and job-placement services suffer from a poor reputation in the minds of both employers and job-seekers (Trappmann, 2011). Only about half of all firms contact local labour offices when they want to recruit, resulting in high matching costs. There also seem to be large and growing differences in services provision across labour offices. While this might be related to the decentralised organisation of PES functions in a way that does not necessarily reflect inefficiencies, lack of coordination and of automatic exchange of information might also induce persistent and symptomatic heterogeneity in service quality.

PES quality is also affected by serious coordination problems. Grotkowska and Sztanderska (2008) highlight the need for better coordination of PES with firms, the municipalities, especially their social assistance centres, and education institutions, including those involved in professional education. When sanctions are applied to the unemployed, they are often revoked by the Ministry, weakening the authority of labour offices. There is also poor coordination between the PES and the Social Security Institution (ZUS) when job offers are refused for medical reasons. Kaluzna (2009) reports that when labour offices ask for further verification of "strange" medical statements, the ZUS usually refuses, arguing that the unemployed do not fall under their competence.

In recent years the budget allocated to labour market policies has amounted to about 0.6-0.9% of GDP, well below the OECD average of about 1.5% (Figure 1.14). When expenditures are computed per LFS unemployed and expressed as a percentage of GDP per capita, Poland has a low ratio of 16%. That ratio increased until 2010 due to the expansion of resources dedicated to ALMPs in a context of falling unemployment, but ALMP spending was cut after that to cope with overall fiscal tightening. Notwithstanding the question of their efficiency, the pro-cyclicality of ALMPs is unfortunate.

Figure 1.14. **Public expenditures on labour market policies are on the low side, 2011**[1]



1. 2010 for Ireland; 2009 for the United Kingdom and 2007 for Norway.
Source: OECD, *Labour Market Programmes Statistics*.

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Table 1.1 provides a breakdown of labour market expenditures in Poland since 2007. Over the past few years passive labour market policies have amounted to about 0.4% of GDP, two thirds in the form of unemployment benefits and one third of pre-retirement schemes covering about 1% of the labour force in 2012, down from about 3% in 2002. ALMPs consist mainly of: training; subsidised employment targeted at centrally defined disadvantaged groups (so-called "intervention works" in the private sector, and "public works" and "socially useful works" in the public sector and non-governmental organisations); start-up subsidies; and the unusual item "doctors' specialisation courses and internships".

In countries where the UB system is generous, efficient ALMPs could be useful to counteract its work-disincentive effects. However, Poland has both low UB generosity and a low level of ALMP spending, as have English-speaking countries which achieve high employment rates. Australia is a case where ALMP spending is low but very efficient (OECD, 2012b). In sum, while higher ALMP spending might have some merit in Poland to reduce the mismatch between workers' skills and labour market needs, improving their efficiency is the priority, especially in a tight budgetary environment.

Job-search assistance and career guidance should remain the first line of attack, especially for those unemployed who are job-ready (OECD, 2013d). While education and training programmes might have low returns, in a downturn they can prepare the long-term unemployed to take advantage of new job opportunities once the labour market improves. Also, subsidies to non-profit employment may provide a rapid countercyclical response, but they generally do not have a lasting impact on the school-to-work transition (Box 4.1 in

Table 1.1. **Expenditure on labour market policies**

PLN millions

	2007	2008	2009	2010	2011	2012
Total expenditure	5 353	5 756	11 245	12 234	8 744	9 351
Per cent of GDP	*0.46*	*0.45*	*0.84*	*0.86*	*0.57*	*0.59*
Unemployment benefits (including SSC)	2 207	1 833	2 851	3 274	3 047	3 403
Pre-retirement benefits and allowances[1]	0.4	0.1	1 555	1 618	1 625	1 788
ALMPs	2 725	3 363	6 205	6 627	3 340	3 875
Training	27	279	377	897	134	184
Intervention works	213	195	179	215	185	139
Public works	178	249	330	477	155	165
Apprenticeships	691	917	1 350	1 466	836	855
Vocational training	379	535	323	242	299	226
Co-financing of costs to employers of training of adolescents	-	-	254	331	290	303
Refunding cost of workplace equipment	365	385	514	807	181	381
Grants for starting a business	536	701	1 092	1 387	442	708
Doctors' specialisation courses and internships	-	-	568	670	718	755
Other	421	560	634	715	732	285

1. In 2004-08, the financing of pre-retirement allowances and benefits was made from the state budget by the Social Insurance Institution. Since the beginning of 2009, responsibility for this expenditure returned to the Labour Fund. Pre-retirement schemes include pre-retirement benefits and allowances, which are granted to the unemployed under certain conditions of work experience (25-30 years for women, 30-35 for men) or age (55-56 years for women, 60-61 for men) to bridge the gap to retirement.
2. This apprenticeship programme differs from those developed within the Vocational Education and Training system. It refers to specific contracts not exceeding 12 months, supervised by local labour offices and paid 120% of the standard UB level.

Source: Ministry of Labour and Social Policy.

OECD, 2008c). In addition, combining work with a significant training promotes labour market integration, especially for apprenticeship (OECD, 2013d). Finally, start-up subsidies seem to have low efficiency (Dar and Tzannatos, 2009). This evidence suggests that ALMPs in Poland should focus more on improving job-search assistance and apprenticeships.

OECD (2013b) provides additional lessons drawn from in-depth reviews of activation policies in seven OECD countries. First, reforms that have been critical to improve activation strategies have often included mergers or co-location of three main services: job broking, referral to active measures and benefit (UB and social assistance) administration. The objective is not only to create a one-stop shop to access all such services, but more fundamentally to integrate their management. In the United Kingdom, merging the PES and the benefit agency seems to have improved service delivery through better coordination and employment outcomes. In Australia, Centrelink is a single entry point for health, social and welfare payments and services. The main advantages of this type of integration are to enhance the coherence of a broad range of social services and facilitate the enforcement of sanctions. In Germany as well, the success of the Hartz IV reform seems to have resulted from better coordination, lower caseloads for PES employees and the development of performance incentives for local employment agencies (Jacobi and Kluve, 2007).

Second, the effectiveness of the PES and any private counterpart can be improved through performance management, as measured in terms of job placement and longer-term outcomes, especially for harder-to-help groups (OECD, 2012b; OECD, 2013b). Australia and Switzerland, which can be used as benchmarks in this area, have designed sophisticated methods to measure performance of local labour offices in terms of gross outcomes (number of action plans completed, registered vacancies filled, job-placement rates, etc.) adjusted using regression results that account for variation in individual job-seeker and local labour-market characteristics. Strengthening the umbrella function of the Ministry of Labour and Social Policy might be worth considering as regards: the development of capacities to evaluate the local PES in order to identify best practices; the effective use of a nationwide information system connecting job vacancies, registered unemployed and ALMPs caseload; and the setting up of standards to deliver key services (profiling, job-search assistance, assignment to ALMPs, sanctions) (OECD, 2009). The government plans to start benchmarking labour offices in 2014. Third, a quasi-market for employment services can operate, as shown by the Australian experience, but it requires an active management framework, which hinges critically upon rewarding the outcomes of providers in order to ensure that only the best performers remain in the market (OECD, 2013b).

Contracting out PES activities has been permitted in Poland since 2004, but there are currently only a few private job agencies. The government plans to contract out only the most difficult cases. Recent action has included the implementation of a pilot project, "Partnership for Jobs", for outsourcing employment services to private agencies in three regions and a draft law introducing the monitoring of ALMPs and rewarding the best performing labour offices (European Commission, 2013). Moreover, the government intends to improve jobseeker profiling, which is crucial to better tailor support to individual needs, especially for those who are the furthest away from employment. Each jobless person would have a personal case officer and be classified as either active, requiring support or remote from the labour market, and assistance would be provided accordingly (PNB, 2013). Activation could also be based on regular in-person reporting of unemployment status. In Australia, job-search requirements involve reporting 8 to 20 job-search actions by the unemployed person every two weeks (OECD, 2013b).

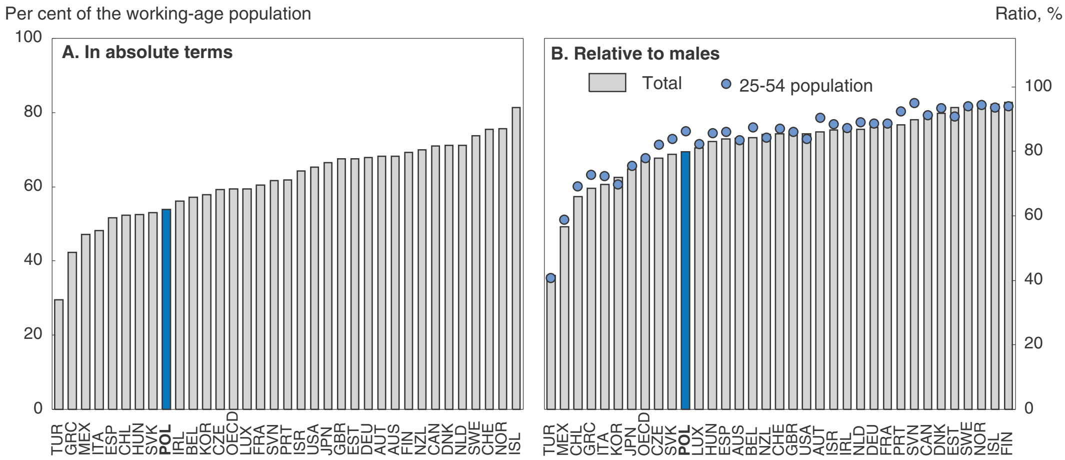
Policies targeted at specific workforce groups

Boosting female participation

The female employment rate is low (Figure 1.15). Even when it is computed relative to its male counterpart, Poland ranks slightly above the OECD average but in the bottom tier of countries, in part due to low participation at older ages. Obstacles to female employment arise from both policies and social norms, which are themselves influenced by policies.

First, old-age pensions are generous for women. The statutory female retirement age of 60 is below its male counterpart of 65, a feature that persists in only a small and diminishing number of OECD countries (OECD, 2012a). Although the incentives built into the pension system imply only a low implicit tax on continued work at older ages (OECD, 2013a), female participation might still be influenced by the legal retirement age of 60, which tends to shape social norms. Following the 2012 reform, the retirement age will be raised to 67 for both genders, phasing in the increase until 2020 for men and 2040 for women. This is welcome, but the pace for women should be accelerated in order to achieve convergence much earlier, for example by 2030. The pension system is all the more generous for women: the gender difference in average life expectancy at 65 was 4.3 years in 2012, well above the OECD average (Figure 1.16, Panel A), and although the pension is inversely proportional to remaining life expectancy at retirement age, unisex mortality tables are used, thus under-estimating women's true average life expectancy.

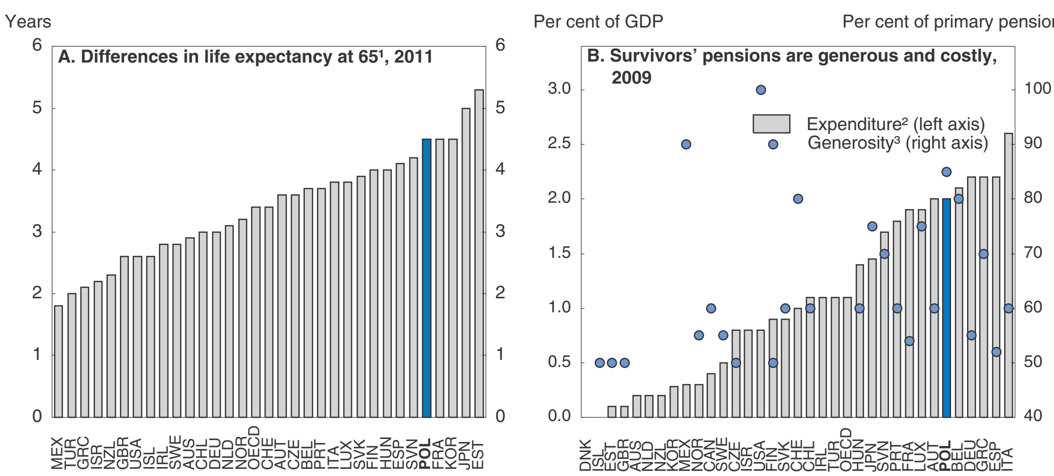
Figure 1.15. **Female employment rate is weak, 2012**



Source: OECD, *Labour Force Statistics 2013 Database.*

StatLink http://dx.doi.org/10.1787/888932999849

Figure 1.16. **The pension system is generous for women**



1. Difference between females and males.
2. Public expenditure on survivors' pensions.
3. Survivors' benefits, as a percentage of individuals' primary pension entitlements.

Source: OECD, *Social Expenditure (SOCX) Database*; for Panel B: E.R. Whitehouse (2013), "Adequacy and Sustainability of Pension Systems: Evidence from Europe," *mimeo* and E. James (2009), "Rethinking Survivor Benefits", World Bank, *Social Protection and Labor Discussion Paper*, No. 928.

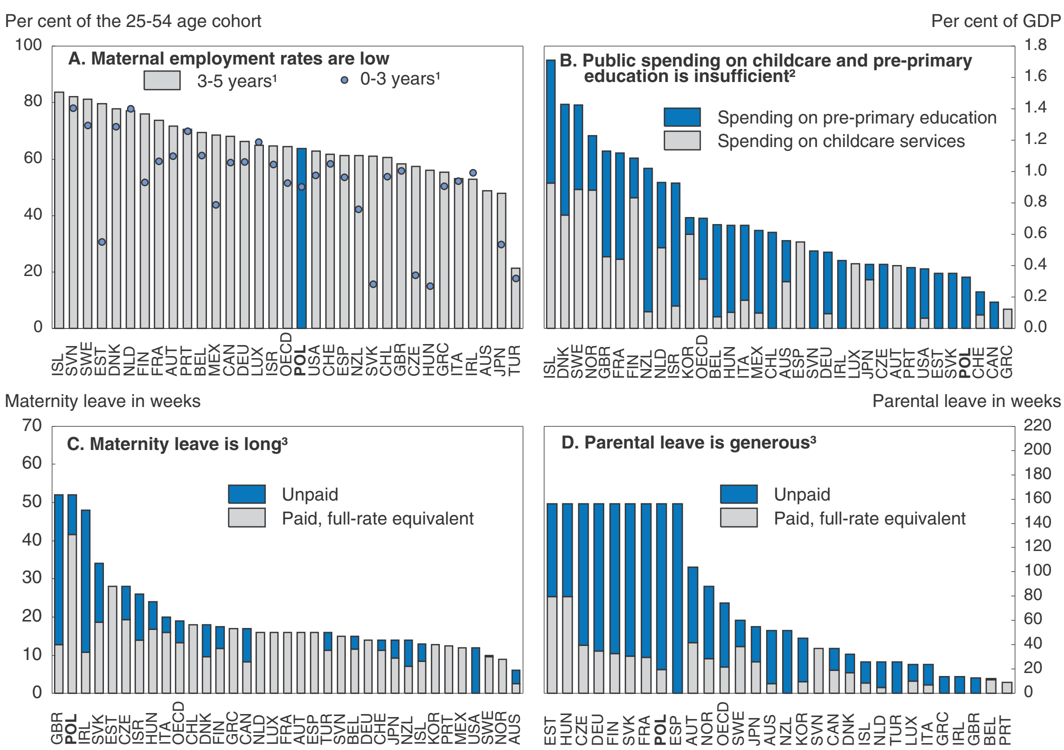
StatLink http://dx.doi.org/10.1787/888932999868

Second, the survivors' pension regime is expensive and undermines work incentives. Spending on the regime, about 90% of whose beneficiaries are women (Whitehouse, 2013), is comparatively high as a share of GDP (Figure 1.16, Panel B). While the primary goal of such pensions is to maintain or protect the survivor's standard of living on bereavement, 85% of their deceased partner's pension is awarded to the survivor, a proportion which tends to increase the survivor's standard of living substantially and one of the highest in the OECD. In Poland, widow(er)s can receive a survivors' pension already at the age of 45. Moreover, the benefit falls if the survivor has earnings, reducing work incentives. Such a system implies redistribution from women who engage in paid work to those who do not and from singles and dual-career couples to single-earner couples (James, 2009). This is because the amount of the pension does not take into account the cost of this type of life insurance at the individual level. Scaling back this programme and reducing the marginal implicit tax involved would increase employment and reduce the overall tax burden.

Third, the tax system features joint taxation of spouses, which boosts the marginal tax rates for second earners if the income gap between spouses is significant. The narrow base of the personal income tax and its relatively low progressivity limit the negative impact in Poland, though. Nevertheless, the government should consider adopting an individual tax system, as many other OECD countries have done (OECD, 2006a), to encourage labour force participation of women, especially those with low educational attainment.

Fourth, the deeply rooted "traditional" family model exerts social constraints on female labour market participation. Long-term care institutions are underdeveloped in Poland (OECD, 2012a), and elderly care is mostly provided by families – typically spouses and children (mainly daughters) (Golinowska and Sowa, 2010). This difficulty is compounded by the poor availability of flexible working-time arrangements, including part-time work. Young mothers and single parents also have low employment rates in Poland, although they are even lower in other CEECs (Figure 1.17, Panel A). While childcare costs are relatively modest (OECD, 2011a), the insufficient development of childcare and

Figure 1.17. **Family policies are detrimental to female employment**



1. Age of the youngest child.
2. Disaggregated spending data are not available for Spain.
3. Child-related leave periods by duration of unpaid leave and the duration of the full-rate equivalent of the leave period; it should be noted that the 52 weeks of Poland's data point are the result of the 2013 reform further extending maternity leave in Poland.

Source: OECD, *Family Database*.

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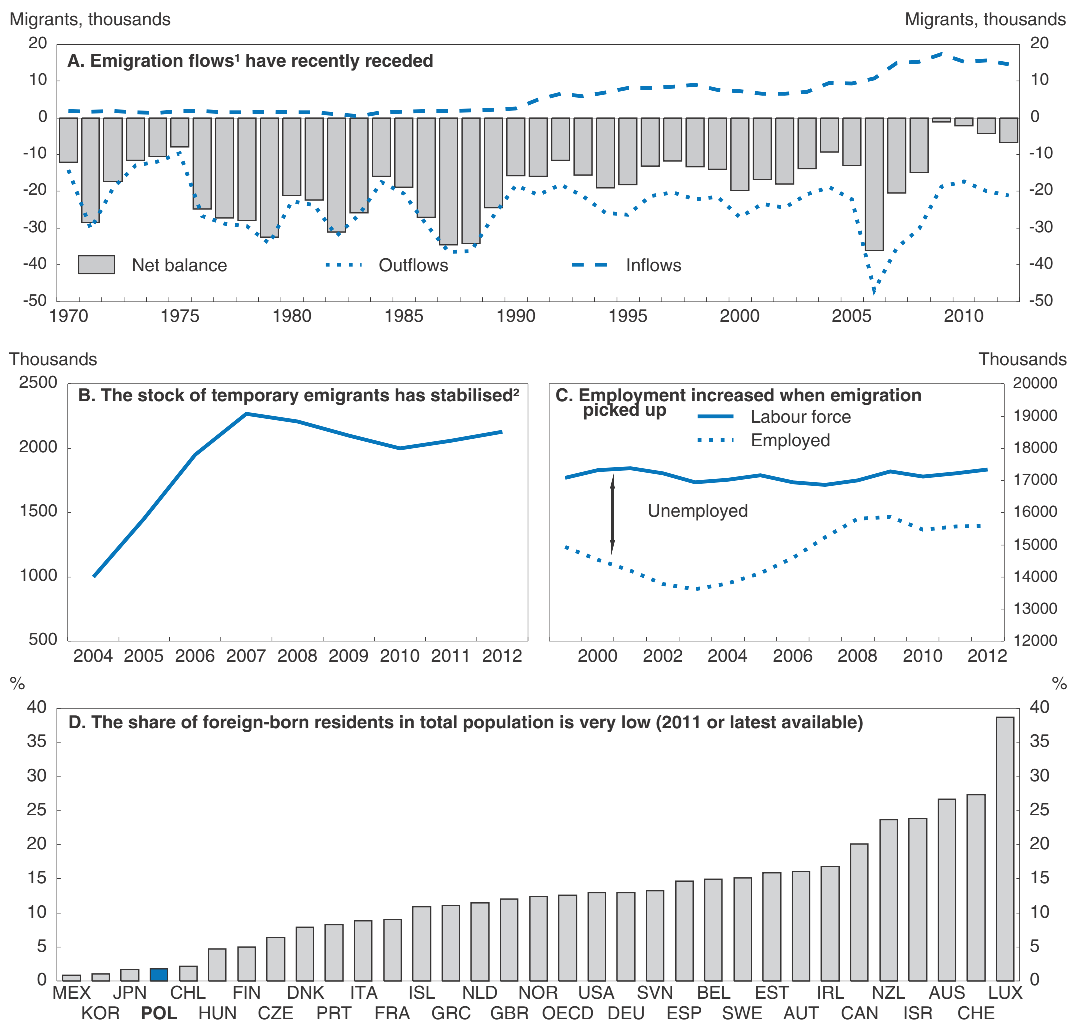
pre-primary-school institutions (Panel B) is persistently cited as a major structural weakness (see OECD, 2013a). The number of places in nurseries almost doubled between 2010 and 2012, but their total capacity remains extremely low (about 50 000 places compared to about 390 000 children born annually in Poland). Yet, important progress has been made recently. Pre-school education became compulsory from the age of five in 2011, and primary education will start at age six (rather than seven) in 2014. In June 2013, the government drastically reduced parents' direct costs of accessing kindergarten. According to a July 2013 regulation, every four year-old will have the right to participate in pre-school education from September 2015 and every three year-old from September 2017. The government intends also to develop a variety of child-care arrangements. A July 2013 law extended beyond municipalities the list of institutions (such as non-public entities or private persons) that will be able to apply for funding from the state budget for the establishment and operation costs of childcare institutions for children under three.

Child-related leave is generous. Fully paid maternity leave was increased from 16 to 18 weeks in 2006 and to 26 weeks in 2012, including 6 optional weeks. It was extended by an additional and optional 26 weeks in June 2013 paid at 60% of salary (Figure 1.17, Panel C), with fathers being entitled to take unused leave (on top of their fully paid 2 weeks of paternity leave). That additional spending might have been better spent on childcare facilities (European Commission, 2013). On top of this, the parental leave of 36 months (entitled until the child is five years old) is also the longest among OECD countries (Panel D). It includes a means-tested monthly benefit of PLN 400 (EUR 95), which is low although beneficiaries' old-age pension contributions are paid by the State. While excessively short parental leave can reduce employment by inducing young mothers to drop out entirely from the labour force, long periods of leave are likely to weaken their attachment to the labour market, generate a loss of human capital and reduce incentives for employers to invest in female workers (OECD, 2012c). About half of entitled women went on childcare leave in the mid-2000s, but the scheme was even more used by mothers with a low level of education, given the low benefit level and means-testing (BERR, 2012). According to BERR (2012), the high level of take-up is due to underdeveloped childcare services, limited availability of part-time work and inflexible work arrangements.

Migration-related issues

Emigration flows picked up very quickly after Poland's accession to the European Union in 2004 and the opening of most EU labour markets to workers from new member states. Keeping in mind that migration numbers are not well measured, in 2007 there were an estimated 2.3 million Polish citizens, or 6% of the total population, staying temporarily abroad, compared to 1.0 million in 2004 (Kaczmarczyk, 2012), when the magnitude of annual net outflows was similar to that in the 1980s (Figure 1.18, Panel A). Overall, the increase in the stock of emigrants since 2004 is equivalent to about 4.1% of the working-age population. With the world economic crisis and Poland's good relative performance, this trend has partly reversed (Panel B). A stronger propensity to migrate abroad has been observed among young people who originate from economically backward areas, giving some credit to the idea that emigration was a response to the oversupply of labour. Yet, emigration since 2004 has fuelled labour shortages in specific occupations, such as construction, retail trade and health care. Between 2004 and 2009, 5.8% of physicians, 2.6% of dentists and 3.4% of nurses were delivered a European certificate of professional qualification, a good proxy of their

Figure 1.18. **Migration indicators**



1. For permanent residence.
2. Estimates of the number of Polish citizens staying abroad for longer than three months (two months in years prior to 2007).

Source: GUS; OECD, *International Migration Outlook 2013*.

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propensities to emigrate (Okolski and Topinska, 2012). The most extreme case was anaesthesiologists, about 19% of whom requested such a certificate.

Although significant, this increase in emigration flows had only a mild short-to-medium-term impact on the Polish labour market (see, among others, Budnik, 2008; Ingham and Ingham, 2011; Kaczmarczyk and Okolski, 2008; and Kaczmarczyk, 2012). It is true that during the 2004-08 period the unemployment rate decreased sharply (Figure 1.1, Panel D). However, the start of the decline preceded the emigration wave. Moreover, to a large extent, the reduction in the number of unemployed since 2004 is accounted for by higher employment than a decrease in the labour force (Figure 1.18, Panel C). Worker outflows are likely to have generated wage pressures, but they seem to have been limited (Budnik, 2008; Kaczmarczyk, 2012). As shown above, at the aggregate level, real wages did not keep pace with labour productivity advances.

Emigration might have two serious adverse consequences over the long term: a brain drain and the amplification of unfavourable demographics. The extent of the former problem is likely to be limited. Only 20% of post-EU-accession emigrants have a tertiary-education level compared to 15% in the overall population (and 15% in the pre-accession period) (Kaczmarczyk, 2012). Hence, while emigration might reinforce skills mismatches, the aggregate quantitative impact is probably small. More serious is the negative impact on long-term GDP and GDP per capita due to a lower working-age population, especially in an emigration country like Poland where the population will soon be ageing quickly, and where, despite the recent increase, immigration flows remain low. The share of immigrants in total employment was the lowest among OECD countries at 0.2%, compared with 12.0% on average in the OECD in 2012. That share was also low in other CEECs, but greater than in Poland: 2.9% in the Czech Republic, 2.2% in Hungary and 0.5% in the Slovak Republic (see also Figure 1.18, Panel D).

The prospects for rapid population ageing and skills shortages, and possibly continuing robust emigration flows, have raised political awareness about the smoothing role of well designed migration policies. To facilitate the return of emigrants, several actions were taken, including information campaigns about administrative procedures and local job markets, but they had only moderate success. Given the still high structural unemployment rate, however, attracting immigrants has not been seen as a pressing issue. Besides, over time the most efficient policy action to limit emigration is to adopt policies that bolster employment opportunities at home and firms' competitiveness, and speed up convergence in standards of living with the most developed countries, thereby reducing the strength of the pull and push emigration forces. This includes removing the obstacles to internal migration discussed above, as internal and external migration are often substitutes. For example, expensive housing in urban areas has restricted internal labour mobility and is often considered to have been an important driver of buoyant post-2004 emigration flows above and beyond greater income prospects.

Although encouraging immigration could be particularly relevant for Poland, its effects on the structure of the population might be mainly temporary (even though they can extend over a generation), as migrants themselves eventually age. Moreover, since the population 15 to 64 is projected to decrease by 27% over 2010-50, immigration alone, while useful, can only attenuate this process to a limited extent, and other policies boosting the labour utilisation of the working-age population will be needed.

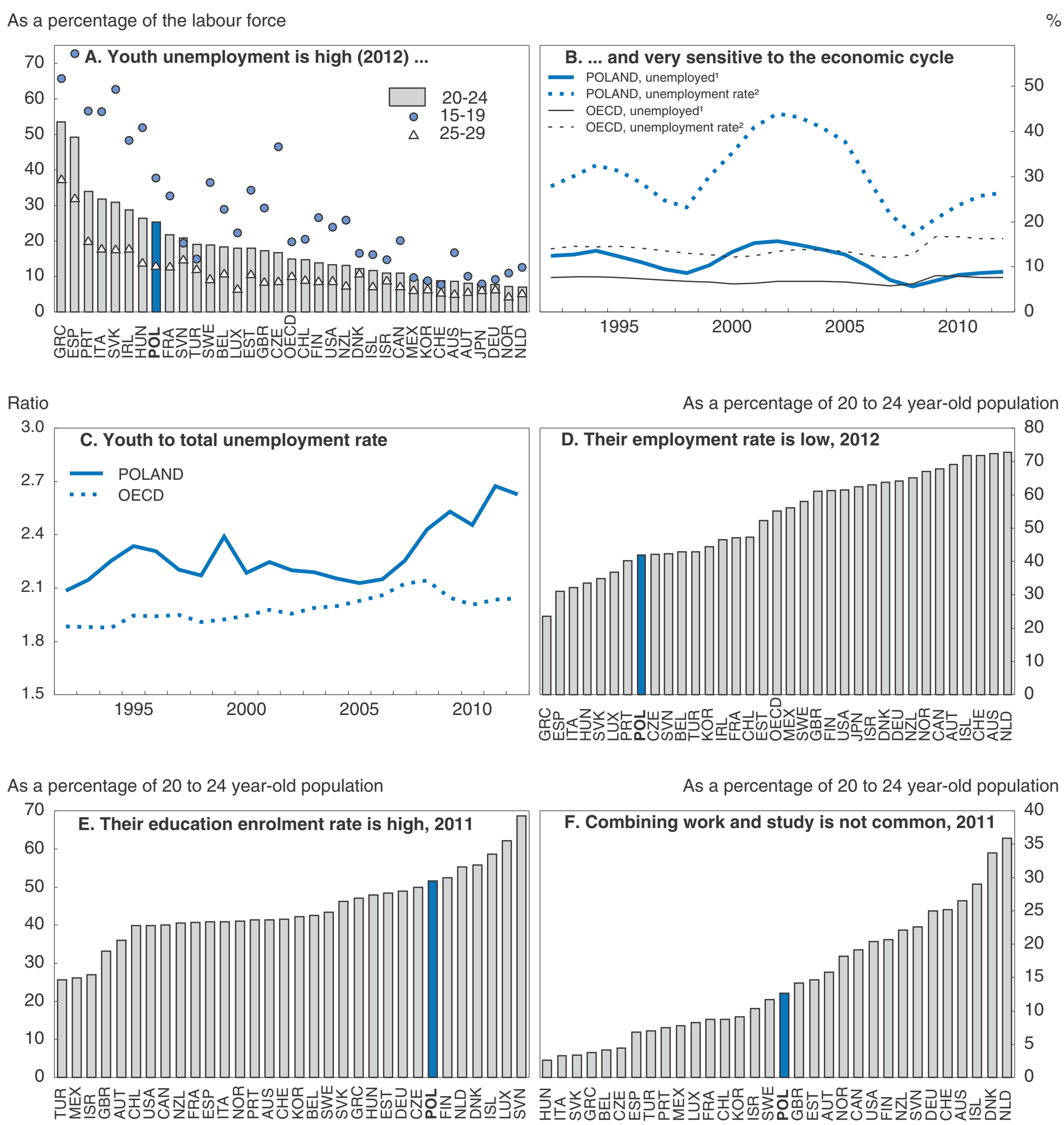
To address short-term labour shortages, in 2006 workers from Ukraine, Belarus and Russia were given the right to work in Poland without permits for three months in any six-month period. In 2008, the scheme was extended to six months of work over a 12-month period, and opened to other Eastern European countries (Moldova, Georgia and recently Armenia) who also gained access to work permits. The procedure that employers must follow was simplified in 2009. However, long-term immigration is restricted: a residence permit can be acquired only after five years of uninterrupted legal residence in Poland, or two years if married to a Polish citizen for at least three years (Iglicka and Ziolek-Skrzypczak, 2010). After public consultation, in July 2012 the Government adopted a document entitled "Migration Policy of Poland – The Current State of Play and Further Actions". Overall, Poland still lags other EU countries in implementing an overarching integration policy and in developing services for immigrants (Iglicka and Ziolek-Skrzypczak, 2010). Some experts consider that, despite the frequently advocated need for it (Okolski and Topinksa, 2012), a single comprehensive strategy to address migration issues has not yet been worked out.

Boosting youth employment prospects

Youth unemployment remains stubbornly high

Despite Poland's good overall economic performance in the recent past, youth unemployment remains stubbornly high (Figure 1.19, Panels A-C). By reducing the labour force participation of the high skilled (a composition effect), high education enrolment combined with a limited share of part-time work while studying contributes to this high

Figure 1.19. **Youth unemployment**



1. As a percentage of the population aged 15 to 24 years.
2. As a percentage of the labour force aged 15 to 24 years.

Source: OECD, *Labour Force Statistics* (2013) and *Education* (2013) *Databases*.

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unemployment rate (Panels D-F). While the rise in educational attainment (OECD, 2013e) has been a major achievement, the increase in the supply of high-skilled workers does not seem to have outpaced the shift in demand towards those with greater skills. Controlling for age and gender effects, the influence of tertiary education attainment on employment rates is one of the largest among OECD countries (Box 1.1). Moreover, the earnings premium of tertiary education has been more or less stable at a high level – between 65 and 80% – since the beginning of the 2000s against an OECD average of 45-60% (OECD, 2013f).

Box 1.1. **Impact of education attainment on employment rates**

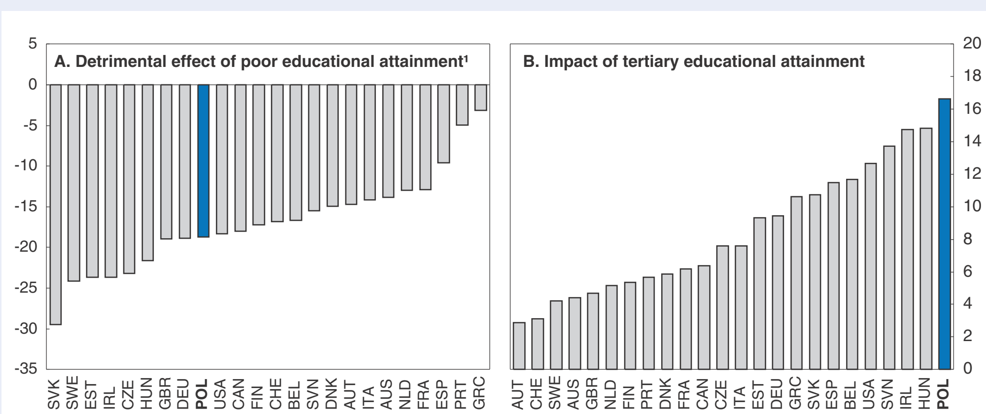
To derive this effect the following specification was estimated for each country for 2011:

$$ER\ (i, j, k) = e\ (i) + f\ (j) + g\ (k) + u\ (i, j, k)$$

where $ER\ (i,j,k)$ is the employment rate for age group i, gender j and education level k, e, f and g are fixed effects controlling for these dimensions, respectively, and u is a residual. Three educational attainment levels are considered: below upper secondary (primary and lower secondary education), upper secondary and tertiary with the upper secondary level used as the reference, i.e. g (k = upper secondary) = 0. Compared with the raw employment rates by education level, the estimated fixed effects $g\ (k)$ enable adjustment for composition effects due to age and gender. Figure 1.20 shows the estimated fixed effects corresponding to the below upper secondary level (Panel A) and the tertiary level (Panel B). For Poland as an example, *controlling for age and gender*, a tertiary education level increases the employment rate by over 16 percentage points, the highest differential within the OECD, while not reaching the upper-secondary level diminished the employment rate by about 19 percentage points, also rather high.

Figure 1.20. **Educational attainment shapes employment prospects relatively heavily**

Coefficient estimates



1. Primary and lower secondary education.
Source: OECD calculations.

StatLink http://dx.doi.org/10.1787/888932999944

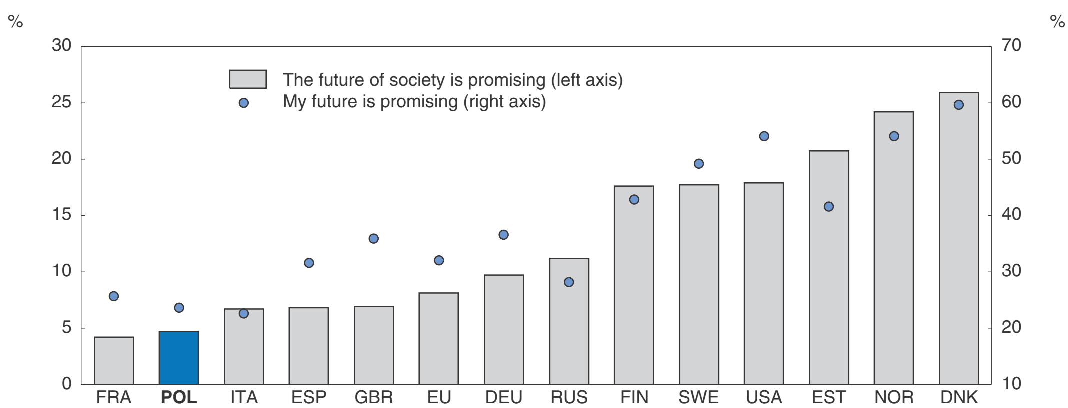
The school-to-work transition is slow. In many countries the first contact with the labour market occurs when students take jobs, but this is not the case in Poland (OECD, 2009). In 2011, only 24% of Polish students aged 20-24 held a job, compared to about 65% in the Netherlands and Australia. Entry-level jobs are not commonly part-time, which is likely to complicate the transition to work (OECD, 2009). Less-educated workers in particular tend to go through an arduous transition.

Precarious forms of employment should be reduced

Temporary contracts are widespread, and precarious employment is pervasive among young workers. With two-thirds of employed youth not having a permanent contract, temporary work is more prevalent among youth than in most OECD countries (Figure 1.8, Panel C). According to Chancellery of the Prime Minister (2011), over 50% of workers between 18 and 32 are employed under a civil-law contract. This situation is tolerated more than chosen: the incidence of involuntary temporary work reached 39% of employed youth in 2011, the third-largest share of OECD countries after Spain and Portugal (OECD, 2013g). That could help explain why, a few years ago, Polish youth seem to have been particularly pessimistic about their society's and their own futures (Figure 1.21), which might in turn fuel emigration.

Figure 1.21. **Young people are pessimistic for the future**

Per cent[1]



1. Percentages agreeing with each statement.

Source: Les jeunesses face à leur avenir: une enquête internationale, Fondation pour l'Innovation Politique, 2008.

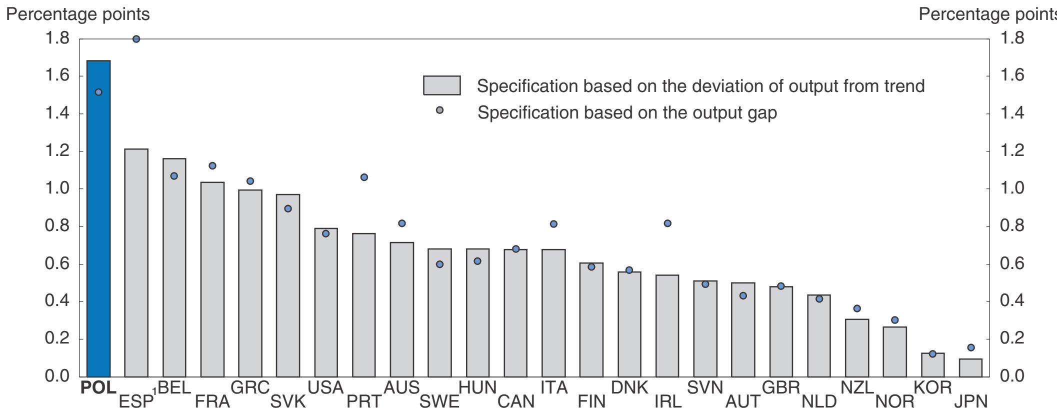
StatLink http://dx.doi.org/10.1787/888932999963

While the possibility of civil-law contracts, weak protection provided by fixed-term contracts (FTCs) and low costs of dismissing limited-tenure employees might promote the hiring of new entrants, young Polish workers, and especially the unskilled, bear a disproportionate share of the social costs generated by the deep segmentation of the labour market (Figure 1.8). Poland is the OECD country where the sensitivity of youth unemployment to the business cycle is the strongest (Figure 1.22). Such labour-market duality might be detrimental to economic performance, as it generates erratic pathways towards stable employment and may result in underinvestment in human capital. Temporary contracts do not seem to serve as a springboard to stable employment in Poland (OECD, 2009; Polakowski, 2012), but rather as a screening device (Baranowska et al., 2011).

A worker taking up his/her first job can be paid 80% of the minimum wage for the first year. While this provision has no age limit, it effectively increases demand for younger workers. Such a scheme is useful. However, a potential wage increase of 25% after the first year might be too sharp, inducing substitution effects, which might generate work

Figure 1.22. **Youth unemployment rates are deeply affected by cyclical developments**

Total change in unemployment rate due to a permanent shock of 1 percentage point of GDP



1. Reported estimated changes in the youth unemployment rate have been capped at 1.8 points to improve the readability of the graph, the true value being 2.4 for Spain (based on the output gap).

Source: Boulhol and Sicari (2013a), "Labour Market Performance by Age Groups: A Focus on France", *OECD Economics Department Working Papers,* No. 1027.

StatLink http://dx.doi.org/10.1787/888932999982

instability. Hence, smoothing the transition by allowing a pay floor of, say, 90% of the minimum wage for the second year might be worth considering. In addition, the scheme could also be extended to the long-term unemployed.

Fostering a better school-to-work transition

Whereas youths tend *de facto* to be excluded from unemployment benefit (UB), given strict eligibility rules, they have incentives to register with the PES. Indeed, registering opens up to them, on top of the usual range of PES services (information about job vacancy, internship, on-the-job training, subsidised jobs), a scholarship of 50% of the basic UB level (for young people under 26 without qualification, means-tested) and public health insurance coverage (OECD, 2009). In terms of ALMPs, the largest youth programme (although since 2009 it has been open to all unemployed, irrespective of age) is the apprenticeship system (different from that developed within Vocational Education and Training, VET). These are specific contracts not exceeding 12 months, supervised by local labour offices and paid 120% of the standard UB level. Another programme, Intervention Works, based on wage subsidies for private employers seems *prima facie* to be giving good results in terms of employment after completion, but one should be cautious about extending such schemes as they are subject to large deadweight losses when they are not well targeted (Martin and Grubb, 2001). Given their short labour-market experience, unemployed youths need to have access to a well functioning PES (see above), and OECD (2009) emphasised that too few of them benefit from ALMPs in Poland.

Integrating youths who leave the school system without completing their studies, and the less-skilled more generally, is a difficult task. Intervening after the student has left school is very costly and the results often disappointing, so it is important to wage this battle earlier, at school (see below). For dropouts, early action is particularly important, and job-search strategies that are based on reciprocal obligations are often found to be the most cost-effective (Quintini et al., 2007). One challenge is to detect early signs of loss of contact with the world of work and to intervene rapidly, because course corrections become complicated when a young person is socially marginalised. Training, which is generally less effective in the case of dropouts, must be tailored and calibrated to labour market needs as much as possible. In this area, social-partner involvement may prove beneficial (Quintini et al., 2007). Co-ordination between the PES and educational authorities is crucial to rapid intervention with youths who are in danger of losing their bearings. The Netherlands, Norway and the United Kingdom have recently bolstered this co-ordination in order to more quickly identify and offer a solution to youths quitting school prematurely (OECD, 2011b).

Important mismatches persist, despite human-capital deepening

It is generally perceived that there remains in Poland a wide gap between the skills produced by the education system and those that are required by firms. Beyond the recent cyclical contraction in labour demand, a lack of skills is indeed often viewed by Polish employers as the most important constraint on firm activity. Rutkowski (2011) documents the shift of labour demand away from less skilled manual to more skilled white-collar labour following the economic transition. The current skills shortages, resulting from this needed job-reallocation process, would apply to both "hard" skills, such as technical qualifications and competences, and "soft" skills, such as the capacity to work in a team, job attitudes and behavioural skills. Moreover, innovative firms tend to be the most affected by skill shortages. While shortages and hiring difficulties of high-skilled white-collar workers are the most obvious, despite human-capital deepening, employers also find it difficult to hire skilled blue-collar workers, notwithstanding the excess supply (and high unemployment) of blue-collar workers more generally (Rutkowski, 2011). The poor employment prospects of workers with secondary general education points to weak labour demand for general skills that are not accompanied by technical or vocational skills. Education has unfortunately been more oriented towards theory than practice, and the link between the two in curricula has been very weak (Chancellery of the Prime Minister, 2011).

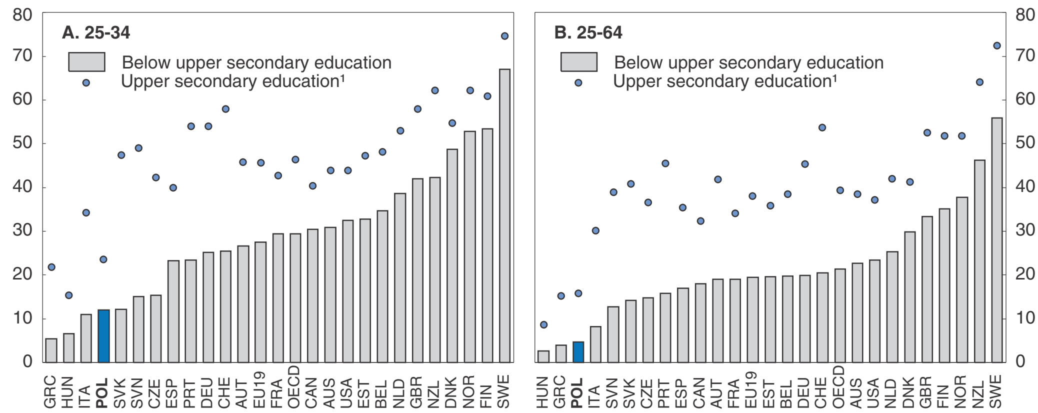
Tackling mismatches requires a wide array of policy actions. The most far-reaching reform would involve greater responsiveness by the education system to labour market needs. On-the-job training and lifelong learning can also play a great role in adapting workers' skills to a rapidly changing technological environment and thereby in preventing the entrenchment of under-skilling. For example, the participation of low-skilled youth in non-formal education is very low (Figure 1.23). In as much as skill shortages might have been amplified by emigration, encouraging well targeted immigration could help to fill skills gaps. Enhancing job-matching services, including through better job-market information, and fostering labour mobility would also help to reduce mismatches. In addition, the prevalence of FTCs for youth is likely to hinder the development of such "soft" skills as commitment, reliability, responsibility and motivation.

Further improving education outcomes

Following the reforms undertaken after transition, the improvement in education performance has been impressive. Average PISA scores rose between 2000 and 2012, when Poland ranked slightly above the OECD average. This achievement came mostly from progress recorded by the poorest performing children, which has reduced inequality of education levels markedly (Boulhol and Sicari, 2013b). Between 1989 and 2011, the number of tertiary education students also grew fivefold. Despite these impressive advances, some important challenges remain.

Figure 1.23. **Participation in non-formal education is minimal**

Participation rate of the 25-34 and 25-64 year-old age groups, 2008 or latest year available



1. Including post-secondary non-tertiary education.

Source: OECD, *Education at a Glance 2012 Database*.

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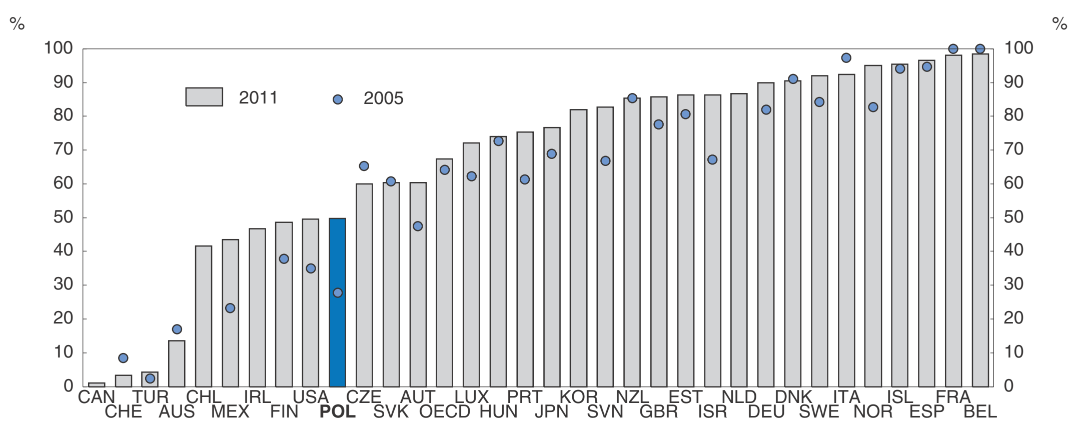
First, while pre-school enrolment rates have increased substantially recently, they remain low (Figure 1.24 and OECD, 2013d), especially in rural areas. Yet, investment at an early stage yields the highest returns, especially for children from disadvantaged backgrounds where the development of interpersonal skills and discipline gets little encouragement (Heckman, 2008). This is because learning is a cumulative process: actions taken during early childhood have long-lasting effects that can enhance social skills and learning abilities (Heckman and Carneiro, 2003). Developing pre-school facilities therefore remains a top priority. As discussed above, recent changes go clearly in the right direction.

Figure 1.24. **Enrolment rate in pre-primary education is rising but remains low**

At the age of 3



Source: OECD, *Education at a Glance 2013 Database*.

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Second, the VET system, which enrols about one third of upper-secondary students, needs to be improved. Since the mid-1990s there has been a large outflow from vocational education towards general education (Polakowski, 2012). Yet, although Poland has one of the lowest dropout rates in the OECD, graduates who have completed just general secondary education or basic vocational schooling are often ill-prepared for the labour market because of a lack of practical training (OECD, 2008a). VET has lost some of its attractiveness due to the failure of most schools to modernise their programmes and equipment sufficiently rapidly. Moreover, as shown by the German example, one key aspect lies in the involvement of social partners in VET policy and provision, and in the quality of social dialogue (Quintini et al., 2007). It is critical that VET programmes retain strong elements of work-based learning (OECD, 2013f), but Polish VET relies mostly on school-based programmes, with only a small share of VET students (about 17%) combining school and work (OECD, 2010b).

The government recognises the need to enhance the VET system and introduced changes in 2012. The aim is to foster employers' involvement in the curriculum and in conducting courses and examinations, and to create more flexible courses. It is too early to assess the scope and impact of the implemented changes. However, more could be done. For example, firms' managers could be appointed to school boards. Also, the European Commission (2013) pointed out that more forceful action is needed involving greater public money to reimburse employers' training costs and to expand the enrolment capacity of VET schools, and raising the quality of teaching.

Third, the *OECD Review of Polish Tertiary Education* (OECD, 2007) highlighted vocational tertiary education as an area of serious weakness. Although the tertiary education system includes vocational Higher Education Institutions (HEIs), their specific role in meeting labour demand is not fully exploited, although the 2011 higher education reform brought significant progress. It introduced an obligation by HEIs to choose between academic curricula emphasising theoretical modules and practice-oriented curricula based on practical modules and strengthened participation of employers' representatives. HEIs were granted more autonomy, as they are now entitled to create their own study programmes based on the National Qualifications Framework for Higher Education. This framework improves the HEI evaluation process carried out by the Polish Accreditation Committee.

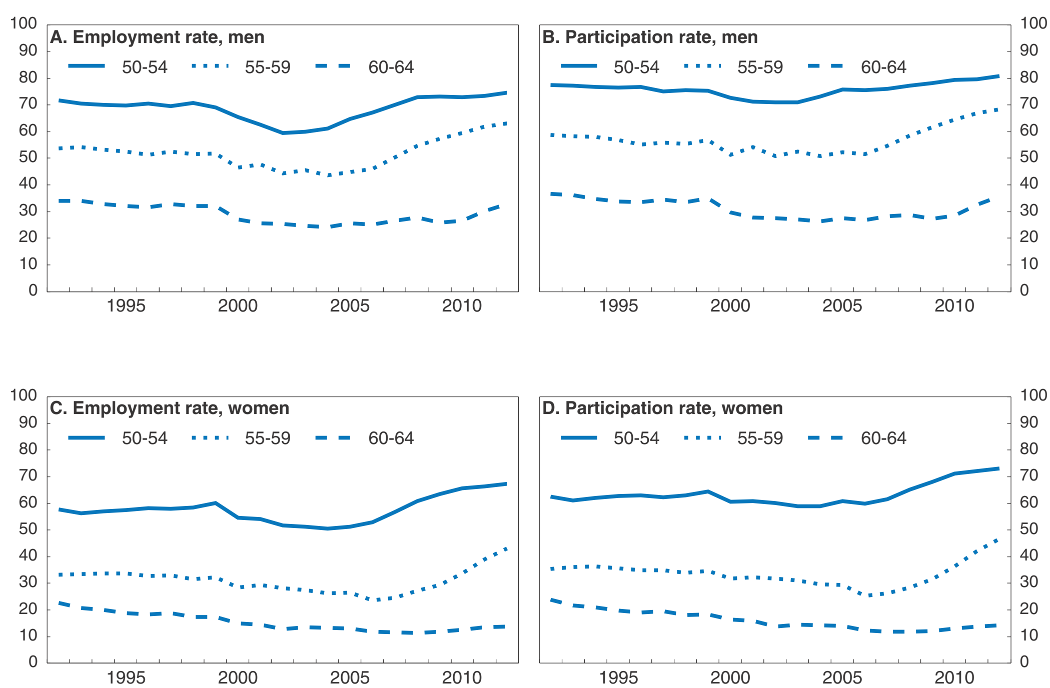
Moreover, graduates' early careers must be monitored by HEIs. A system of quality-based financing was introduced, amounting to about 2% of tertiary education spending, and HEIs are required to fill research and teaching vacancies competitively. The reform also includes measures to strengthen the links between HEIs and businesses, and a programme has been launched to attract students to economy-relevant areas, including information technology, chemistry, mathematics, construction and biotechnology, given that students often choose courses in social science, humanities, law and economics irrespective of often disappointing job prospects. A 2013 draft amendment to the Higher Education Law would, if implemented, enhance employers' involvement in both the design of the curricula and the teaching process, introduce a three-month obligatory internship for students opting for the practice-oriented curricula, create a central system to track graduates' employment outcomes and allow the validation of learning outcomes achieved outside the formal system. With Germany and Finland providing useful examples of well functioning vocational tertiary education (OECD, 2007), the authorities should make further efforts to promote a distinct vocational sector, as intended by the 2013 draft amendment, which would introduce a clear distinction between academic and vocational HEIs.

Fourth, with about 440 higher education institutions, tertiary education is very fragmented. The split between fee-based private universities (accounting for about a third of students) and public universities that charge no tuition fees is unfair and distorts competition. Beyond the funding advantage, public universities enjoy a much better reputation as well as greater physical capital and better human resources inherited from the past. They can therefore select the best students. Moreover, they also provide fee-based programmes that are not called full-time daily studies, as those have to be free of charge according to the constitution. Past *Surveys* of Poland (OECD, 2006b; O'Brien and Paczynski, 2006; OECD, 2008a) recommended that the authorities: put the financing of public and private HEIs on an equal footing; introduce cost-related tuition fees in the public sector; simplify access to the dysfunctional student-loans system, whose repayment should be income-contingent; allocate academic positions based on transparent and competitive procedures; and systematically assess HEI quality. In October 2012, mandatory payments for the second and additional degrees were introduced at public HEIs.

Continuing to enhance the supply of senior workers

The employment and participation rates of older workers have both risen strongly since the mid-2000s (Figure 1.25). For the 50-54 and 55-59 age groups, employment rates increased by 13-19 percentage points between 2004 and 2012 for both men and women. For 60-64 year-olds, the improvement is only half as large for men, while it is virtually nil for women, who still face attractive public pension provisions. Yet, the current levels remain well below OECD averages (Table 1.2). Figure 1.4 (Panel D) shows that even within the poorly performing group of countries with a similar age structure of employment rates, Poland's drop-off starts from the 45-49 age group, and its decline is steeper. The OECD is carrying out a new review of Polish policies to encourage greater labour market participation at older ages by fostering employability, job mobility and labour demand; it is set to be published at the end of 2014 (OECD, 2014).

Figure 1.25. **Employment and participation rates for older workers have increased from low levels**



Source: OECD, *Labour Force Statistics 2013 Database.*

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Table 1.2. **Older workers scoreboard, 2002, 2007 and 2012**

	Poland			OECD[1]		
	2002	2007	2012	2002	2007	2012
Employment						
Employment rate, 50-64 (% of the age group)	40.3	43.4	49.4	56.3	60.2	62.0
Of which: 55-69	22.4	24.1	32.2	37.1	41.4	43.7
60-64	18.6	18.4	22.6	33.5	37.8	41.0
Gender gap in employment, 55-64 (ratio men/women)	1.7	2.1	1.7	1.8	1.6	1.4
Employment rate, 65-69 (% of the age group)	10.8	8.5	9.5	15.6	17.2	19.3
Job quality						
Incidence of part-time work, 55-64 (% of total employment)	22.1	18.5	11.6	17.1	17.7	18.4
Incidence of temporary work, 55-64 (% employees)	11.6	19.9	21.8	9.3	9.4	8.9
Incidence of self-employment, 55-64 (% of total employment)	42.0	36.4	30.1	30.2	27.1	26.1
Full-time[2] earnings, 55-59 relative to 25-29 (ratio)	1.39	1.61	-	1.32	1.34	1.34
Effective labour force exit age[3] (years)						
Men	61.1	61.4	62.3	63.3	63.7	64.2
Women	59.0	57.7	60.2	61.3	62.3	63.1
Unemployment						
Unemployment rate, 55-64 (% of the labour force)	10.5	6.8	7.4	4.7	4.0	6.0
Incidence of long-term[4] unemployment, 55+ (% of total unemployment)	57.7	57.0	43.9	43.6	45.9	46.9
Employability						
Share of 55-84 with tertiary education[5] (% of the age group)	12.7	12.3	12.8	20.0	21.1	23.8
Participation in training,[6] 55-64						
Absolute (% of all employed in the age group)	1.5	2.1	1.8	6.3	8.1	9.4
Relative to employed persons aged 25-54 (ratio)	0.23	0.31	0.31	0.43	0.54	0.57

1. Unweighted averages for 34 OECD countries.
2. Mean gross hourly earnings, 1998 and 2004.
3. Effective exit age over the five-year periods 1997-2002, 2002-07 and 2007-12.
4. Unemployed for more than one year.
5. 2005, 2007, 2011.
6. Job-related training during the last month in 2001, 2007, 2011.

Source: OECD estimates from national labour force surveys, EU-LFS and *OECD Education Database*.

Eliminating special old-age pension regimes

The sharp tightening of early-retirement conditions in 2008 has boosted the labour supply of older workers (OECD, 2010a). As a result the average effective retirement age increased from 57.1 years in 2007 to 59.8 in 2011. Nevertheless, it remains too low due to the low statutory female retirement age, the slow phase-in of the 2008 reform tackling early retirement and the existence of special regimes. In 2011 almost 80% of old-age pensions were managed by ZUS, 17% by KRUS and the remainder by the Ministries of Internal Affairs, Defence and Justice (Martinez-Fernandez et al., 2013). Out of the people beginning to receive an old-age pension from ZUS in 2011, the average effective retirement age was 60.1 years for men (against a legal age of 65) and 59.5 for women (against 60) (Table 1.3). This is because about 12% of men who retired were miners with an effective retirement age of 47.9 years. Also, those who had worked for 20-25 years before 1999 in specific work conditions remain entitled to early retirement. That scheme will vanish gradually, but a hefty 60% or so of new male retirees in ZUS, excluding miners, fall under it. As a result, in 2011, only about one quarter of new male retirees were at least 65, the statutory retirement age.

Table 1.3. **Pensions granted in 2011 – Social Insurance Fund**

Age	Total	Male	Female
Total	102 466	56 653	45 813
49 and less	5 296	5 175	121
50	2 024	1 938	86
51	432	285	147
52	375	161	214
53	407	122	285
54	479	128	351
55	8 052	475	7 577
56	1 642	205	1 437
57	1 501	152	1 349
58	956	116	840
59	1 152	106	1 046
60	53 344	25 746	27 598
61	5 152	2 952	2 200
62	3 144	1 990	1 154
63	1 657	1 219	438
64	1 621	1 325	296
65 and more	15 232	14 558	674
Average age in years	59.8	60.1	59.5

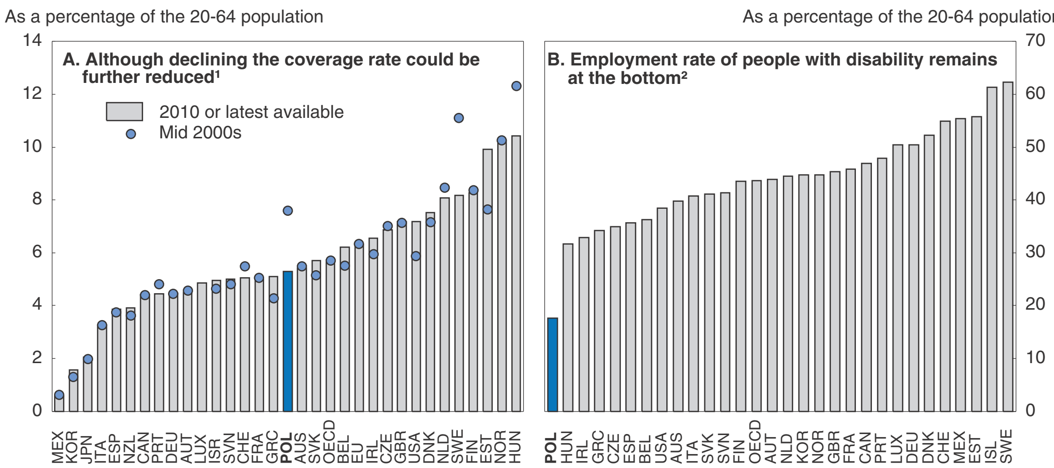
Source: Social Insurance Fund Database.

The main special retirement regimes cover farmers, miners, railway workers, uniformed services and judges. Miners can retire after 25 years of work. Until the 2012 reform, soldiers and police officers could retire after 15 years, but now uniformed officers will be able to retire only at age 55 and only provided that they have worked for at least 25 years. Moreover, the pension will depend on earnings for 10 consecutive years instead of the final salary as at present. The reform will apply to those who start their service after 1 January 2013, hence a very long phase in. As discussed above, the changes to the farmers' regime have been very limited.

Continuing to tighten disability pension schemes and better activate disabled workers

Since the early-2000s the number of disability benefit recipients, among whom older workers are over-represented, has been divided by three from a very high level (Figure 1.26, Panel A). Farmers remain also over-represented, accounting for about 30% of beneficiaries. The eligibility criteria have been steadily tightened, the health status of the beneficiaries better verified and the benefit made temporary, with a maximum period of three years. These changes are also notable, since early-retirement schemes were also tightened during the same period, which could have led to a shift into disability support, as observed in other countries. They might be short-lived, however, since disability benefits will become more attractive. Indeed, under the 1999 old-age pension reform, replacement rates will be reduced, since, for a given retirement age, the old-age pension automatically decreases with improvements in life expectancy. As a result, the ratio of average disability to old-age pensions will increase significantly, boosting incentives to retire early under the former regime when possible (IMF, 2013). Therefore, the formula used to calculate disability pensions should be revised in line with that used for old-age or minimum pensions in order to account for life expectancy gains. The generosity of the benefits on the other hand

Figure 1.26. **Disability pensions**



1. 2010 or latest available. Poland's data point refers to 2012 and is constructed assuming the number of disability benefit recipients in the KRUS changed in the same proportion as the total number of beneficiaries in ZUS since 2007, the latest year for which data for the KRUS are available.
2. Late 2000s.

Source: OECD, *Going for Growth 2013*; *OECD SOCX Database* and OECD (2010), *Sickness, Disability and Work, Breaking the Barriers*.

StatLink http://dx.doi.org/10.1787/888933000058

is slightly below average: Poland spends about 1.1% of GDP on public disability pensions (against a hefty 4.2% in the mid-1990s), compared with an OECD average of 1.2%.

Poland has the OECD's lowest employment rate of people with disabilities (Figure 1.26, Panel B). Moreover, about one-third of those employed work part-time, one of the OECD's highest shares (see Figure 2.3 in OECD, 2010c), even though part-time employment is low overall in Poland. Employers often prefer not to fulfil the 6% subsidised employment quota for disability benefit recipients and pay a fine (about 40% of the average wage for each worker below the quota). This suggests that, while the quota level could be reduced, there is some room to raise that penalty (in a budget-neutral way), which should also be differentiated to take into account the degree of disability of employed workers. With little vocational rehabilitation and training, and the emphasis put on employment by Sheltered Work Enterprises, which account for about two-thirds of subsidised employment of disabled people, benefit from overly generous tax breaks and help perpetuate the segregation of disabled workers, Poland's policy has traditionally been passive (OECD, 2006c). Better activating people with disability is rightfully a priority, as is recognised by the government.

Little or no progress has been achieved on the recommendations made following the OECD's 2006 in-depth review of work obstacles confronting people with disabilities in Poland (OECD, 2006c). First, the supply of well targeted and individualised high-quality services of vocational rehabilitation and training should be increased, and local labour offices should place greater emphasis on early intervention. Second, the structure of employment support should be overhauled by streamlining administrative structures and responsibilities in order to provide the disabled with timely and adequate support. Too many players are involved (ZUS, the PES, the State Fund for the Employment and Rehabilitation of Disabled People, or PFRON, and local governments), each with unclear responsibilities. PFRON and the PES are perceived as rather passive institutions in terms of dealing with disabled people, failing to combat their high level of inactivity (OECD, 2006c).

The 2006 review recommended improving coordination regarding vocational training and re-qualification programmes between ZUS and the PES, placing the governance of PFRON under local governments' responsibility and having ZUS in charge of the entire disability assessment; currently they do so for income-support purposes only, and local governments perform them for labour-market purposes. Third, KRUS rules should be aligned with those in the general social insurance scheme: in the KRUS, disability is narrowly defined as the inability to continue to work on one's own farm. Even in the ZUS, the definition of partial disability is related to the inability to continue working in one's own profession and should be abandoned. Fourth, financial incentives to work should be improved by smoothing the phasing-out of disability benefits with higher earnings. Finally, special employment conditions for disabled workers, such as shorter working hours and longer annual leave entitlements, should be eliminated, as they represent employment obstacles for employers, are probably ineffective in boosting labour supply and reinforce stereotypes and prejudices (OECD, 2006c).

Removing some specific limitations to the demand and supply of older workers

On the demand side, employers generally point at a disconnect between higher wages for seniors and lower productivity, due to illness, difficulties in adapting to technological changes, especially those induced by information technologies, and insufficient training. In 2011, labour costs were reduced, as the number of days of sick-leave benefits paid by employers was lowered from 33 to 14 (from the 15th day sickness benefit is paid by ZUS). Also, older workers on open-ended contracts are subject to a stricter employment protection, as they cannot be fired less than four years before their retirement age. This feature is a source of uncertainty and costs for firms and ends up limiting the recruitment of older workers. France, for example, had a similar albeit less strict regulation and did well in eliminating it in 2008.

On the supply side, the longer unemployment benefit (UB) entitlement for over-50 workers, discussed previously, should be eliminated. Beyond issues related to early retirement and disability, the government launched the "Generational Solidarity 50+" programme in 2008 to raise seniors' participation rate. The programme aims to improve working conditions, upgrade skills and qualifications, enhance activation policies targeted at the disabled and unemployed, and reduce labour costs of women aged above 55 and men above 60 through exemptions from unemployment insurance contributions (this also applies to hiring all unemployed over 50 for the first 12 months). The results of that programme have been somewhat disappointing, in part due to ALMP budget cuts since 2011 (IMF, 2012; Martinez-Fernandez et al., 2013).

Implementing a broad and flexible system of lifelong learning

Professional training and lifelong learning are critical to adapt skills to technological progress and the fast pace of on-going globalisation and to deliver the general competencies that might be needed over a person's career. Yet, despite generous EU funding, less than 5% of Polish adults aged 25 to 64 participated in non-formal education and training in 2011, one of the lowest shares in Europe, with an even lower share for older or less educated workers (Figure 1.23, Panel B). Based on a report from the Ministry of Labour and Social Policy, the majority of employers do not invest in their workers' training: while in 2010 about 90% of large firms had prepared a training plan, this was the case for only about a third of micro and small firms (EWCO, 2010). This might result from a lack of SME resources and from time and credit constraints facing employers. It could also be due to SMEs' reluctance to invest in transferable human capital. All these explanations might signal a sub-optimal level of training, which would call for government intervention. However, even though training policies differ importantly across OECD countries, no consensus has emerged yet about best practice in this area.

Currently, several measures help low qualified and older workers to upgrade their qualifications or change occupations. Employers can receive government reimbursement for up to 50% of training costs and 80% for workers aged over 45. The government is also considering the creation of a national training fund to provide for a greater share of training costs. Also, an amendment to the School Education Act passed in 2011 allows vocational schools to be integrated into the continuous education system, which will make it easier to obtain qualifications outside the school-based system. The New Core Curriculum at schools emphasises core competencies development, including mathematics, science, technology and the use of ICT. According to a 2013 draft law, universities would be able to validate the learning outcomes achieved in non-formal learning, thus facilitating access to higher education for people with at least five years of work experience. However, the elaboration of a broad and flexible system of lifelong learning that the OECD has recommended in recent *Surveys* (e.g. OECD, 2010a and 2012a), as part of an overarching strategy for a more competitive economy, is still missing. A strategic document on the "Prospects for Lifelong Learning" was published in March 2011, but, according to European Commission (2013), the responsibility for the strategy has continuously been shifted between ministries. In September 2013, the strategic document was adopted by the Council of Ministers.

Recommendations to boost employment

Policies other than labour market policies

- Continue to develop transport infrastructure, in particular by upgrading the quality of the rail network. Reform housing policies by: making the release of zoning plans by municipalities mandatory; and replacing transaction taxes by *ad valorem* property taxes.
- Accelerate the reduction of government subsidies to the farmers' social insurance system.
- Downsize the informal economy by: simplifying tax regulations; reinforcing the monitoring and enforcement of the tax system; and eliminating the preferential regimes for the self-employed.
- Enhance product-market competition (Chapter 2).

Labour market policies

- Reduce labour market dualism by: making all contracts for labour services subject to the same tax and social contribution regime as Labour-Code contracts; extending the maximum length of trial-period contracts; streamlining legal dismissal procedures; setting a maximum duration for temporary contracts with the same firm; and easing regulation on temporary work agencies.
- Scale back survivors' pensions to reduce the labour tax wedge. Reduce wage rigidities by bringing the effects of age and education on public-sector wages closer to private-sector standards.

Recommendations to boost employment *(cont.)*

- Eliminate regional and age-related differences in the length of unemployment benefits. Disconnect health-insurance entitlement from unemployment registration. Tighten job-search requirements. Enforce the provision that a suitable job offer is not restricted to the occupational field of the unemployed person. Smooth pay increases by allowing a floor of 90% for the second year of people in their first job.
- Consider merging local labour offices with unemployment benefits and social assistance administration to create a one-stop shop and more fundamentally to integrate the management of those activities. Enhance coordination and automatic exchange of information between local labour offices, firms, assistance centres and education institutions. Expand the resources of public employment services to hire more high-skilled staff, and ensure that overall resources are better allocated to front-line placement tasks. Strengthen the umbrella function of the Ministry of Labour and Social Policy, including by promoting the adoption of best practices through performance management and the introduction of benchmarking of employment-service providers.
- Rationalise ALMPs by focusing more on job-search assistance, career guidance and work schemes having a high training content. Improve job-seeker profiling. Reduce passive social assistance by making more transfers (such as childcare subsidies) conditional in part on being employed or seeking work. Expand the scope of private employment services.

Policies to deal with specific workforce groups

- Develop child-care and long-term care facilities and pre-school education. Monitor closely the impact of the long maternity leave on the employment of mothers. Introduce an individual taxation system. Increase the female retirement age at a faster pace, e.g. to reach 67 by 2030 instead of 2040 as currently scheduled.
- Enhance work-based learning in VET programmes, and boost social partners' involvement. Expand subsidies to cover employers' VET costs. Elaborate a broad and flexible system of lifelong learning.
- Phase out all special occupational regimes, remove pre-retirement schemes, and avoid that disability pensions become attractive relative to old-age pensions. Promote the employment of people with disability by: reducing the employment quota of 6% and raising the penalty for firms failing to reach the revised level; and better training and activating workers with disability.
- Remove the prohibition to lay off a worker less than four years before retirement age.

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Chapter 2

Strengthening competition

Poland's productivity has grown strongly over the past decade, and efforts to reduce the regulatory burden have been significant. Despite impressive progress, product market regulation remains more burdensome than in most OECD countries, partly due to the importance of red tape and the level of state involvement in the economy. Further reduction in red tape and pursuing privatisation in competitive markets would increase competitive pressures and ensure neutrality, notably in public procurement processes. Economic rents in many sectors seem high, as stringent entry regulations, regulatory barriers and inefficient bankruptcy procedures induce significant resource misallocation. A welcome deregulation of professional services is ongoing, and the government plans to further ease firm registrations and reform bankruptcy procedures. The independence of the sector regulators in network industries and the powers of the Competition Authority can still be enhanced, as the reform efforts in these sectors remain patchy. The dominant positions of the incumbents and the failure of network sector regulators to introduce a level playing field in order to secure third-party access to the sectoral infrastructure and allow new entry in the competitive segments are another main issue. The advantages of being considered a farmer are also slowing the consolidation process in the agricultural sector.

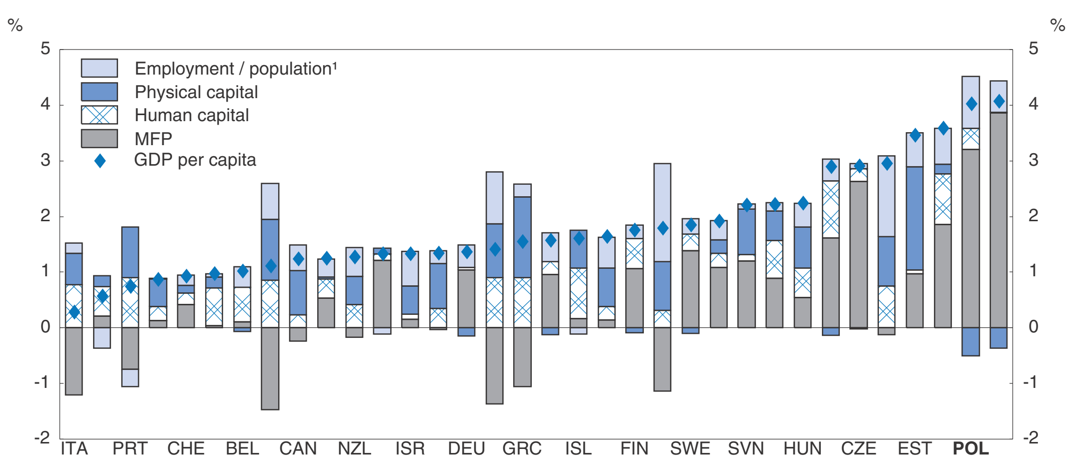
Strengthening competition to boost long-term growth

Poland's recent economic performance has been remarkable

Economic growth has been strong in Poland since the beginning of the transition process. It is the only OECD economy that did not shrink during the global economic crisis of 2007-09. Per capita real GDP growth averaged around 3.8% between 2000 and 2012, against an OECD average of about 1.6%. Among Central and Eastern European countries (CEECs), only the Slovak Republic and Estonia achieved a similar performance.

Productivity gains explain the major part of the recent growth performance (Figure 2.1). Per capita income growth can be broken down into the effects of labour utilisation (total hours worked per person), physical capital intensity, human capital and technological progress, so-called multi-factor productivity (MFP) growth (Johansson et al., 2013). While enhanced human capital and better labour utilisation have helped increase per capita income growth, it has been largely impressive MFP outcomes that have driven improved standards of living. Among its OECD peers, only the Slovak Republic recorded stronger productivity growth during this period. Sustained productivity growth is the result of the country's transition from central planning to a market economy and technology transfers from abroad, in part due to Poland's increasing trade openness and integration in global value chains (OECD, 2010a; IMF, 2013a). At the same time, low capital intensity has acted as a severe drag on per capita incomes. By contrast, several other CEECs have benefited from an increase in capital intensity. The negative contribution of physical capital intensity to MFP

Figure 2.1. **Average annual GDP per capita growth in OECD countries, 2000-11**



1. To ensure that the percentage gap in the components of GDP add up to GDP per capita the decomposition is done in log differences since the decomposition is multiplicative. GDP per capita is equal to the product of the components MFP, Human capital, (Physical capital/GDP)$^{1/2}$ and employment/population.

Source: Johansson et al. (2013), "Long-Term Growth Scenarios", *OECD Economics Department Working Paper*, No. 1000.

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growth partly reflects the modest level of foreign direct investment (FDI) and the high overall regulatory burden on businesses and investment (Égert and Kierzenkowski, 2013).

Nevertheless, per capita income was still almost 40% lower than the OECD average in 2012, mainly because of a shortfall in labour productivity, which was 39% lower than the OECD average in purchasing power parity terms (OECD, 2013a). Furthermore, over the medium term, the productivity catch-up process could be mechanically slowed by the fast population ageing associated with low fertility rates and a steady rise in life expectancy.

Pro-competitive structural reforms could boost long-term growth and competitiveness

Speeding up pro-competitive structural reforms could have large long-term beneficial effects on growth and competitiveness. Poland is catching up with the productivity frontier in many sectors, and increasing the level of competition may have especially large productivity payoffs in such a context (Acemoglu et al., 2006). Indeed, sound pro-competition policies and institutions may boost productivity growth and competitiveness through three main channels.

First, stronger competitive pressures would incentivise firms to continuously improve their performance and drive the least efficient firms out of the market. For example, stronger import competition has been shown to increase the productivity of Polish firms through reallocation effects (Goh and Javorcik, 2007). The danger of losing market share to competitors may also increase managers' (and workers') efforts and push firms to adopt better management practices, while allowing owners to better compare and monitor managers (Nickell, 1996; Bloom et al., 2013).

Second, innovation could benefit from stronger competitive pressures, as competition appears weak in most sectors (see below). Rising competition from initially low levels puts pressure on firms to upgrade their technologies and innovate (Aghion et al., 2005; Hashmi, 2013). New entrants may compete by bringing in the latest technologies and push incumbents to invest in human and physical capital, and the pure threat of entry may give incentives to approach the technological frontier (Alesina et al., 2005). Openness to foreign competition through trade and FDI also increases technology transfers within multinational companies and spill-overs to local firms (Nicoletti and Scarpetta, 2005).

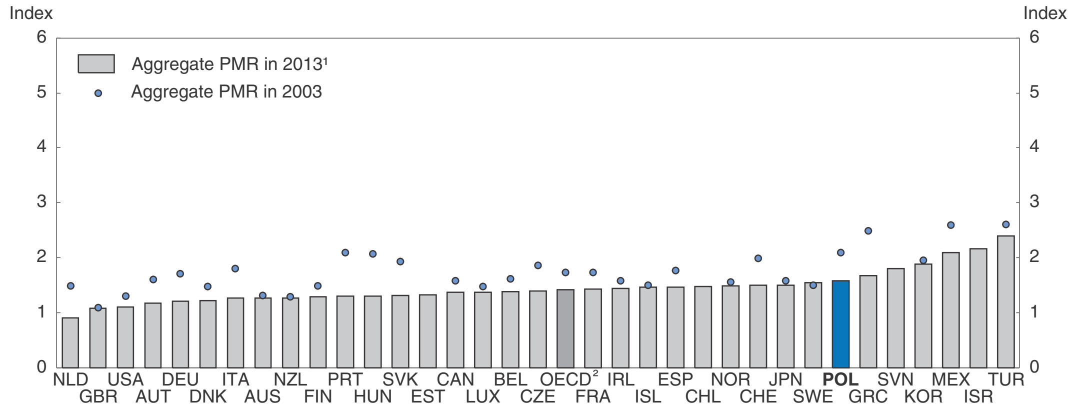
Finally, Poland's productivity may increase via strong spill-over effects across sectors. Product market reforms in upstream industries not only help raise their productivity but also that in those sectors using their outputs (Javorcik, 2004; Goldberg et al., 2010). Recent OECD work showed that Poland has the largest potential in the OECD to increase productivity by aligning product market regulations in network industries, retail distribution and professional services with the average of the three best performing OECD countries (Bourlès et al., 2010; Bouis and Duval, 2011). Though the precise magnitude of this estimate must be interpreted with caution (OECD, 2013b), pro-competitive reforms could lead to a 14% increase in Polish productivity over a 10-year period in a fast-implementation scenario.

Product market indicators reveal considerable room for progress

Poland substantially reduced the burden of Product Market Regulation (PMR) on the economy between 2003 and 2013, according to the OECD's aggregated PMR indicator (Koske et al., 2014). However, product market regulations still appear much more burdensome than in the OECD average country and, in 2013, Greece and Slovenia were the only EU countries having more stringent PMRs (Figure 2.2).

Figure 2.2. **Product market regulation in OECD countries, 2003 and 2013**

Index scale from 0 to 6, from least to most restrictive



1. 2008 for the United States.
2. The OECD average excludes Chile, Estonia, Israel and Slovenia for which 2003 data are missing.

Source: OECD (2014), preliminary *Product Market Regulation Database*.

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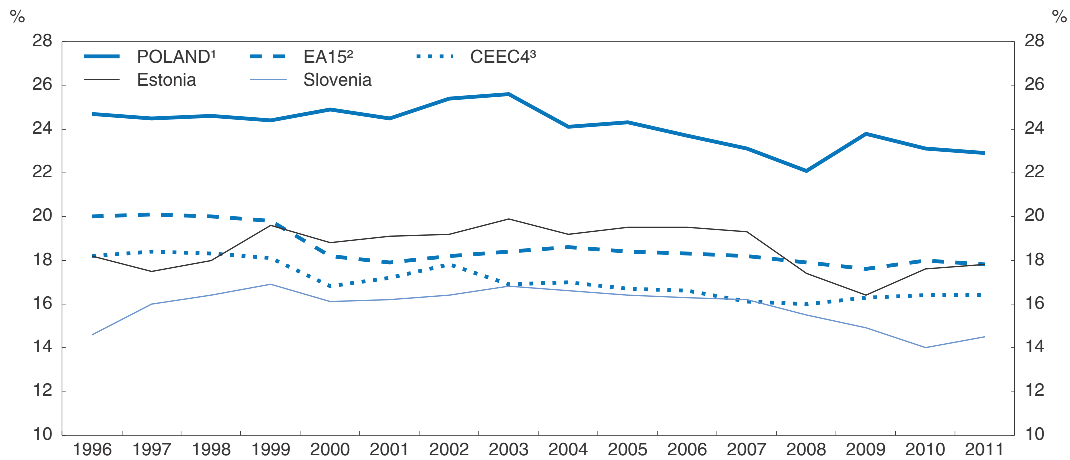
Progress has been significant but fairly unevenly distributed across different areas. According to the PMR sub-indicators, Poland's competition policy framework (legal barriers, antitrust exemptions, barriers to competition in network sectors and services) was the second least conducive to competition in 2003 but ranked better than the OECD average in 2013. Similarly, government involvement in business operations, such as through command and control regulations, decreased significantly between 2003 and 2013. Reductions in explicit and implicit barriers to trade and investment have also been impressive, but they remained among the largest in the OECD in 2013. By contrast, progress has been moderate for barriers to entrepreneurship, and Poland still ranks among the worst OECD countries as regards red tape, as measured by the administrative burden on start-ups and regulatory and administrative opacity. Moreover, the government's grip on the economy remains one of the tightest in the OECD. The public ownership sub-indicator was the OECD's highest in 2013, although the privatisation programme, launched in 2008, has continued to reduce public ownership in the economy (see below).

Other indicators of business conditions also highlight that the regulatory burden remains heavy, notwithstanding significant improvements. According to the World Bank's "Doing Business" survey, in 2012 Poland improved the most in the ease of doing business through four reforms: making it easier to register property, pay taxes, enforce contracts and resolve insolvency (World Bank, 2012). However, the survey confirms that administrative costs imposed by regulations still weigh significantly on firms: only nine OECD countries had a lower ranking than Poland in 2013 (World Bank, 2013). Starting a business appears particularly lengthy. According to the survey, there are four procedures to go through, and the process takes nearly a month. A reform of the procedure, approved by the government in early 2014, should reduce the registration time to seven days (Ministry of Justice, 2014). By contrast, it takes only one day to register a new business in New Zealand. Furthermore, Poland still lags behind most OECD countries according to the complexity of the tax system, the difficulties to resolve insolvency or to obtain an electricity connection for a new business (World Bank, 2013).

Market outcomes confirm the existence of severe obstacles to competition and scope for improving economic performance via stronger market discipline. The level of price-cost margins (PCMs, or the Lerner index), a common proxy for the mark-up over marginal costs and the extent of product market competition (Nickell, 1996; Aghion et al., 2005 and 2012; Boulhol, 2010), highlights the importance of competition-restraining regulations in Poland. Indeed, the average PCM of 23 percentage points is 5 to 7 percentage points higher in Poland than elsewhere in the region (Figure 2.3). PCMs have fallen slightly in Poland since 2003, but their average level in 2011 remained 5 percentage points above the average of the original 15 countries in the euro area (EA15).

Figure 2.3. **Price-cost margins in the whole economy over the 1996-2011 period**



1. Price-cost margins (PCMs) are adjusted for self-employment: self-employed are assumed to earn the average wage in the sector except in the agricultural sector. For each country, the formula used is: $PCM = [VA - \Sigma_i (LABR_i - LABR_i/EMP_i \times SELF_i) - LABR_a]/OUTPUT$, where *i* is the sector (excluding agriculture), *VA* is value added, *LABR* is labour costs, $LABR_a$ is labour costs in agriculture, *EMP* is employment, *SELF* is self-employment, and *OUTPUT* is output. Labour costs are not imputed for the large share of self-employed in agriculture (more than 90% in Poland), which suggests that the contract-based average labour costs would be a poor proxy for the labour costs of the self-employed.
2. EA15 excludes Ireland for which data are missing.
3. CEEC4 excludes Poland.

Source: *Eurostat National Accounts Database* and OECD calculations.

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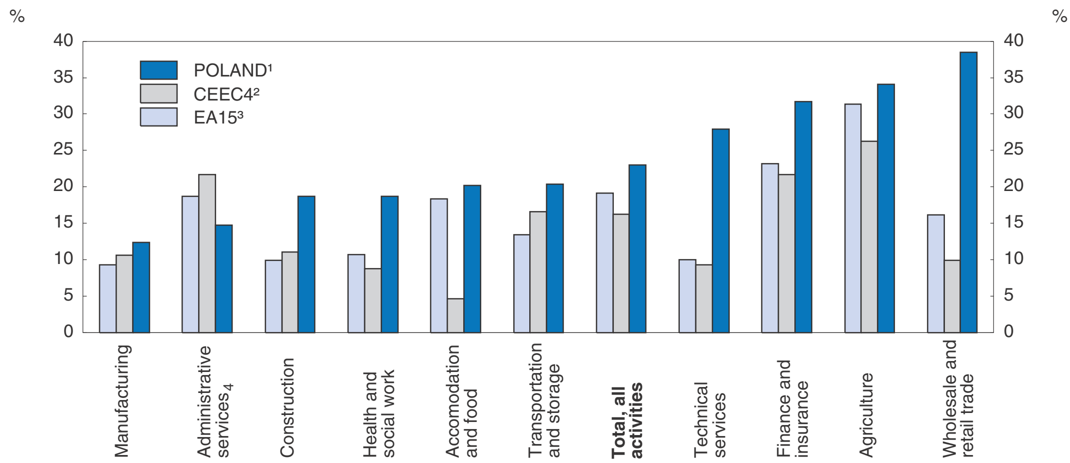
The inter-sectoral structure of PCMs in Poland is similar to other CEEC4s (Hungary and the Czech and Slovak Republics) and the EA15's, but their level is higher in all sectors except administrative services (Figure 2.4). The ratio of price to average costs is determined by competitive pressures and sector-specific production technologies, as described, for instance, by returns to scale and fixed costs. As expected, PCMs are low in manufacturing, as foreign competition tends to squeeze margins. By contrast, margins are particularly large in domestically oriented and sheltered sectors.

Poland has recently implemented a broad deregulation of professional services, which should increase competition in this sector (see below). However, competitive pressures are likely to remain weak in other sheltered sectors. In particular, the average mark-up in wholesale and retail distribution is 29 percentage points above the average in the other CEEC4s and 22 percentage points above the EA15 outcome. This indicates that, despite the increasing penetration of chain stores and e-commerce, competition in wholesale and retail activities remains weak. Indeed, retail regulations are as restrictive as in Denmark

Figure 2.4. **Price-cost margins in Poland and comparator countries in 2008-11**



1. The self-employed are assumed to earn the sectoral average wage except in agriculture. Sectors which comprise less than 2% of Polish employment – mostly public activities (education, public administration and defence) – are not displayed.
2. CEEC4 excludes Poland.
3. EA15 excludes Ireland for which data are missing.
4. Include human resources' activities, office administration, security activities, services to buildings, travel agency services and rental and leasing of motor vehicles, personal and household goods, machinery and equipment, and intellectual property.

Source: *Eurostat National Account Database* and OECD calculations.

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and France. The most stringent regulation applies to the licensing of new outlets, suggesting that current regulation serves to protect incumbents.

Policies to improve the regulatory framework and product market competition

Given the high level of regulations and the low level of competition measured by policy indicators and price-cost margins, further increasing market discipline could have large long-term benefits for productivity growth. While public ownership remains widespread, simplifying and rationalising state aids and strengthening the competencies and independence of the Competition Authority could boost competition. Empowering consumers in competition law enforcement, reducing red tape, reforming inefficient bankruptcy procedures and increasing transparency and capacities in public procurement would also increase competitive pressures and improve resource allocation.

Extensive state ownership distorts competition

There is broad consensus among economists that shifting from public to private ownership tends to increase efficiency and profitability, especially in areas where competitive pressures can be strong (Megginson and Netter, 2001). Privatisation is likely to improve productive efficiency and resource allocation across the economy. First, private ownership facilitates and enhances incentives for monitoring managerial performance, based, for instance, on stock and bond prices, because owners can extract the returns to better outcomes, while in state-owned enterprises (SOEs), higher profits belong to taxpayers, who have no direct control over public businesses. The danger of hostile takeovers and bankruptcies and the competitive market for private managers may further push managers to seek to satisfy the profit-maximising objectives set by the owners of privatised firms, rather than to inflate costs through so-called "X-inefficiencies". By contrast, state ownership may provide implicit state guaranties leading to soft budget constraints.

Second, private ownership limits the ability of politicians and pressure groups to distort resource allocation. Polish labour unions wield a non-trivial political influence in mining and transport SOEs, leading to potential cronyism (Capobianco and Christiansen, 2011). Some SOEs have also been shown to have competitive advantages just because of their close ties to local governments (OECD, 2009a). They may receive direct or hidden subsidies incorporated into laws and administrative procedures or public procurement processes (see below). These subsidies are likely to impact on the cost of capital of private firms, possible takeovers and the likelihood of bankruptcies, and ultimately the overall tax burden.

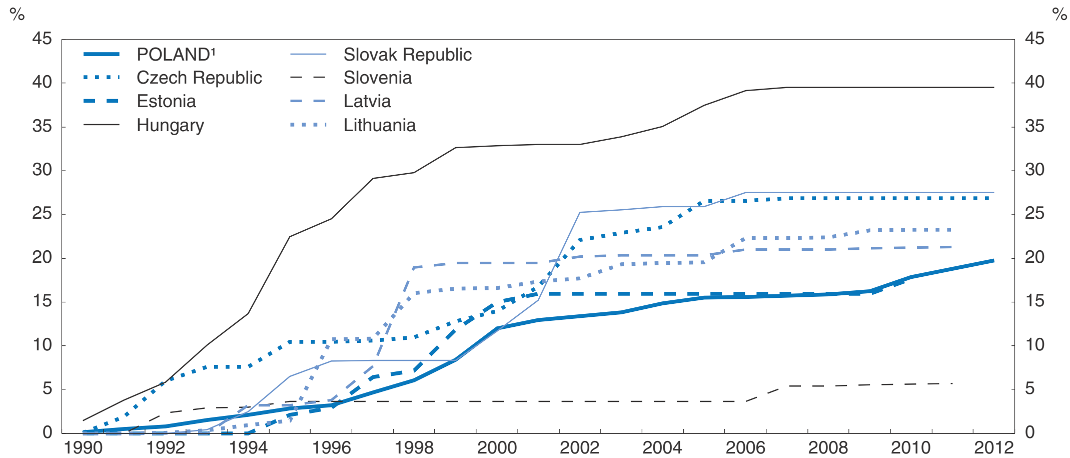
However, privatisation is not always a panacea. For example, network industries have substantial natural monopoly elements, and regulating powerful privatised monopolies poses significant challenges, notably the risk of regulatory capture. Political influence may also persist if the sector regulator is not independent from the government. Furthermore, vertical separation between the potentially competitive parts and the natural monopoly segment, followed by the privatisation of competitive parts, may lead to agency problems. On the one hand, the sector regulator may set access prices that do not cover network costs and discourage investment; on the other hand, prices may also be set too high and lead to overcapacity. Strengthening the independence of the sector regulator and its capacities can reduce the risks of regulatory capture, political influence and agency problems (Nicoletti and Scarpetta, 2003 and 2005).

State ownership remains widespread

Poland lags behind other CEECs in terms of cumulated privatisation since transition got underway (Figure 2.5). As a result, public ownership remains one of the most prevalent in the OECD area according to the OECD's PMR indicator (Figure 2.6). A precondition for a level playing field between SOEs and private firms is that SOEs should at least be corporatised, so that competition, procurement and general bankruptcy laws apply equally to both public and private companies (OECD, 2009a and 2012a). The restructuring of the corporate sector and the privatisation process started very modestly after 1992 and accelerated towards the end of the 1990s with the launch of the mass privatisation programme in late 1994 (OECD, 2010a). In 1990, there were about 8 500 state-owned enterprises. By 2012, 2 300 of them had been privatised, 1 900 liquidated and some 1 800 corporatised and commercialised, while less than 400 active enterprises remain in state hands (Ministry of Treasury, 2013a; OECD, 2013c).

The Polish government plays an important role in many potentially competitive sectors of the economy. Indeed, Poland took the 6th position among OECD countries in terms of the share of SOE employees in total employment in 2008 (Christiansen, 2011). The largest Polish SOEs, which make it to the Forbes Global list, generate sales equivalent to more than 12% of GNI, their profits reach 1.3% of GNI, and their market value is around 15% of GNI (Kowalski et al., 2013). Norway is the only OECD country displaying higher figures, because of its large oil sector (Table 2.1). Moreover, public ownership concerns not only specific, mostly network, industries, as in many other OECD countries. In 2008, there were indeed over 200 SOEs in manufacturing, employing a total of around 80 000 people, more than 100 publicly owned mining companies and almost 30 publicly owned real estate companies (Christiansen, 2011).

Figure 2.5. **Cumulated privatisation revenues as a share of GDP**



1. Privatisation revenues are computed as a share of GDP of the relevant year and are then cumulated over the years.

Source: *World Bank Privatisation Database 1990-2008*, *World Development Indicators*, IMF Article IV reports and *CESIFO DICE Database*.

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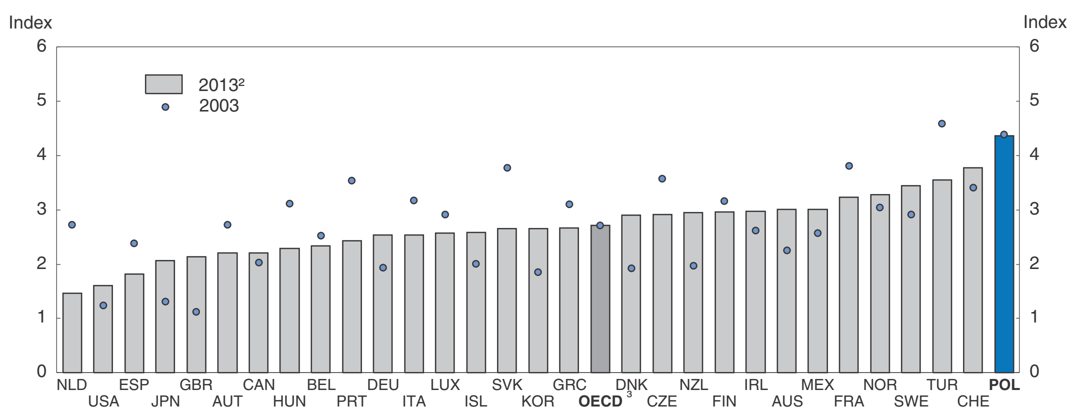
Figure 2.6. **Public ownership in the economy, PMR indicators, 2003 and 2013**

Index scale of 0 to 6, from least to most restrictive[1]



1. The OECD public ownership indicator measures the scope of public ownership in 30 sectors, the extent of state ownership in network industries and the level of public control in enterprises where the state owns shares. The indicator is based on qualitative information, for example the presence or absence of SOEs in a given sector. It measures the scope of public ownership across sectors rather than the quantitative scale of public ownership in the economy.
2. 2008 for the United States.
3. The OECD average excludes Chile, Estonia, Israel and Slovenia for which 2003 data are missing.

Source: OECD (2014), preliminary *Product Market Regulation Database*.

StatLink http://dx.doi.org/10.1787/888933000172

Partial privatisation of SOEs raises further challenges for competition in Poland, where the government has often opted to list them on the stock exchange while selling minority or majority stakes in a dispersed way. The method of privatisation has important implications for efficiency improvements, as it gives managers different incentives to restructure the firms (Djankov, 1999). While the overall effect of privatisation on productivity is generally found to be positive in CEECs, a concentrated private ownership structure appears to produce superior economic outcomes compared to dispersed private ownership, presumably

Table 2.1. **Forbes Global 2000 SOE sales, profits, market value and assets as a % GNI, 2011**

	Sales	Profits	Market value
Norway	25.0	2.1	25.9
Poland	**12.4**	**1.3**	**14.8**
France	7.9	0.4	7.1
Korea	6.8	0.2	4.0
Ireland	6.5	-1.9	0.3
Greece	5.8	0.4	3.8
Czech Republic	5.6	1.3	13.1
Sweden	3.4	0.7	8.1
Finland	3.3	0.7	10.6
Switzerland	3.1	0.6	7.1
United Kingdom	2.8	-0.1	3.2
United States	2.7	-0.1	0.4
Belgium	2.6	0.9	2.9
Austria	1.1	0.1	3.1
Turkey	0.7	0.1	0.4
Japan	0.5	0.0	0.8
Italy	0.4	0.0	0.2
Germany	0.1	0.0	0.2

Source: Kowalski et al. (2013), "State-Owned Enterprises: Trade Effects and Policy Implications", *OECD Trade Policy Papers*, No. 147.

because it prevents the state from retaining close control of the firm even if it remains a minority owner (Estrin et al., 2009). In Poland, the "golden veto" legislation of 2005, by which the Treasury was allowed to maintain a privileged position in strategic state-controlled enterprises for public-interest reasons, was abrogated in 2010, as it was viewed by the European Commission as incompatible with EU law (OECD, 2010a). However, the Polish state has kept a controlling stake in many companies by remaining a majority owner or a large minority owner. This form of state-controlled privatisation may result in much lower efficiency improvements than full privatisations. Indeed, state-controlled firms may benefit from the same competition distortions as SOEs relative to private firms.

Government involvement in the economy is likely to remain high

The government launched ambitious privatisation plans in 2008-11, targeting the sale of around 800 companies, and 2012-13, and the process is still on-going. The privatisation process accelerated in 2010-11, as proceeds increased from 0.2% of GDP in 2008 to 1.0% in 2011, and additional revenues of about 0.2% of GDP per year were expected by the government in 2013 and 2014. However, the government classified almost 50 SOEs as strategically important and intends to keep them under majority state ownership, or to sell tranches in such a way that it can maintain control due to dispersed ownership (Ministry of Treasury, 2013b). These SOEs operate mostly in the energy, financial and mining sectors. Table 2.2 gives a selected list. The government also wants to maintain control over companies in the chemicals and mining industries, which are not deemed as strategically important.

In late 2012, the Prime Minister announced the creation of the Polish Investment Programme, which will use future privatisation revenues (and also government assets, including SOE holdings) to co-finance investments in infrastructure, estimated at about 30% of GDP, and in chemicals, energy, transport and telecommunications industries (Ministry of Treasury, 2013). If such a programme may be justified by the need to remedy

Table 2.2. **The State intends to retain control of some SOEs even in the long term**

Selected list of state-owned enterprises in which the State wants to keep a controlling stake

Percentage

Company	Sector	State ownership 2013	Targeted state ownership
Strategic companies			
PGE	Energy	62	50
Tauron	Energy	30	25
PKO BP	Banking	31	25
PZU	Insurance	35	25
KGHM	Metals mining	32	32
PGNiG	Oil and gas	72	72
PKN Orlen	Oil and gas	28	28
Grupa Lotos	Oil and gas	53	53
Keeping control over non-strategic companies			
Grupa Azoty	Chemicals	33	33
JSW	Mining – coal	56	34
Komnpania Weglowa – NL	Mining – coal	100	50
Katowicki holding Weglowy – NL	Mining – coal	100	50
Disengagement from non-strategic companies			
Ciech	Chemicals	39	0
ENEA	Energy	52	0
WSE	Financial sector	35	0
PHN S.A.	Real estate	75	0
Energa – NL	Energy	84	0
Weglokoks – NL	Trading – coal	100	0

Source: Ministry of Treasury (2013b), Poland: Privatisation plan and investment opportunities, June.

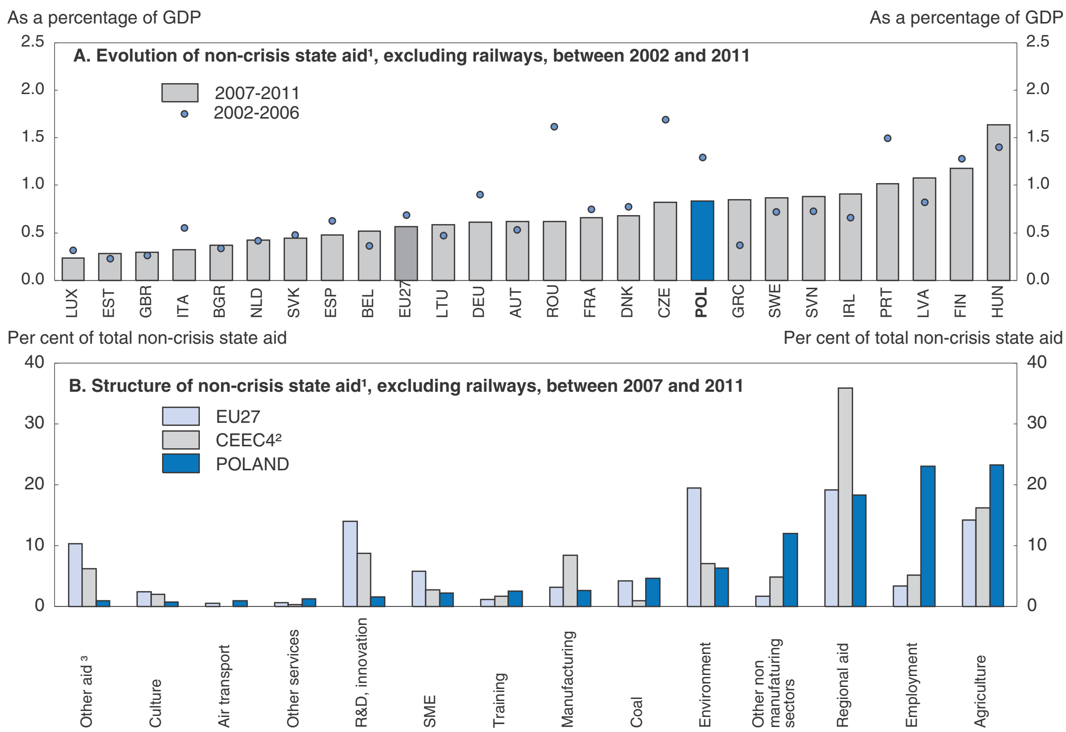
market failures in terms of the weak market availability of long-term finance for infrastructure projects, which would therefore stimulate economic growth, it could also mean further state involvement in some competitive sectors of the economy.

The maintenance of majority state ownership in some companies in competitive segments of the economy may limit the potential benefits of the 2008-11 and 2012-13 privatisation plans. While the government wishes to improve the efficiency of these companies through enhancing corporate governance standards rather than via privatisation, changes in the government's priorities may make such advances easily reversible and may question the independence of the managing board. For example, the Treasury recently expressed its desire to tighten its control over a number of SOEs through their supervisory boards (*Polish News Bulletin*, 2013b). In sum, the government should significantly reduce state ownership in competitive markets, such as financial institutions, mining and chemical companies, while ensuring sound governance of the remaining SOEs.

State aids should be better targeted and regularly evaluated

State aid, including subsidies and tax expenditures aimed at specific sectors and firms, could also contribute to competition distortions. The most frequent forms of state aid are tax concessions and grants, which represented around 97% of aid in 2011 (UOKIK, 2012). State aid, as recorded by the European Commission, appears high by European standards, though its share as a percentage of GDP decreased between 2002 and 2011 (Figure 2.7, Panel A). State aid regulation in Poland is consistent with EU law. Competition-distorting aids are banned, but exceptions for rescuing firms, restructuring distressed sectors and regions, promoting SME growth, and fostering employment and lifelong

Figure 2.7. **Non-crisis state aid is high by European standards and targeted at agriculture and employment**



1. Non-crisis state aid excludes financial crisis aid and temporary framework aid granted from 2008 to 2011. It refers to measures authorised by the European Commission decisions or being implemented by member states under block exemption. It excludes measures that do not favour certain enterprises or sectors, and public subsidies that do not affect trade or distort competition.
2. CEEC4 is the unweighted average of Hungary and the Czech and Slovak Republics.
3. Other aid regroups residual forms of aid, which represent less than 1% of granted aid in Poland.

Source: European Commission (2012c), "Facts and Figures on State aid in the EU Member States", *Commission Staff Working Paper*, No. 778.

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training are permitted. To ensure equal competition, state aid schemes or changes to the conditions for its use require notification to the European Commission. The only exceptions are aid granted under the so-called block exemptions and *de minimis* aid. Block exemptions aim to foster job creation, competitiveness and SMEs, which are considered to be compatible with state aid rules without requiring prior notification. Cumulated *de minimis* aid per firm must not exceed EUR 200 000 gross value (or EUR 100 000 in the case of road transport) over three consecutive calendar years.

State aid may help correct market failures and enhance economic growth and efficiency, but it may also be influenced by pressure groups and lead to resource misallocation (OECD, 2010b; Aghion et al., 2012). At the aggregate level, it appears aimed at sustaining the agricultural sector and maintaining employment, notably for disabled persons, while support to research and development and innovation and environmental aid play lesser roles than in the EU27 and the other CEEC4s (Figure 2.7, Panel B). At the microeconomic level, state aid also appears dispersed across granting institutions and recipients. Indeed, a large number of organisations are responsible for state aid attributions. In 2011, 831 organisations, including ministries, public bodies and local governments (389), granted state aid to around 81 000 beneficiaries (UOKIK, 2012). Though the Competition Authority records granted aids, the dispersion of aid suggests that reducing the number of granting institutions could increase its cost effectiveness and ease its monitoring and economic evaluation.

Another main issue with state aid in Poland is the lack of assessment of its economic effects, which may include competition distortions. The impact of existing state aids should be carefully analysed, and any additional aids should address specific market failures, minimise moral hazard and adverse selection risks, and avoid distorting competition or crowding out private financing. One important example is the Special Enterprise Zone (SEZ) programme. In Poland, investors have benefited from incentives to locate their activities in 14 SEZs since 1994 as part of regional policies to fight high structural unemployment in some peripheral areas. Benefits consist of tax reductions, assistance in handling formalities, availability of land at below-market prices and real estate tax exemptions (OECD, 2010a). The SEZ programme's expiry was recently extended from 2020 to 2026. However, their economic effects have yet to be evaluated, and the programme has been criticised by the Ministry of Finance for its inability to improve regional growth (Ministry of Finance, 2013). Even though the programme may have been partly successful at attracting FDI and motivated by tax competition with Hungary and the Czech and Slovak Republics, it may generate large deadweight losses through competition distortions (OECD, 2010a). Indeed, empirical evidence regarding the effects of such economic zones in France and the United Kingdom is mixed. It suggests that they may in some cases be cost effective, while in others large displacement effects – without economic gains – may occur through competition distortions involving domestic firms located nearby (Criscuolo et al., 2012; Mayneris et al., 2012).

The Competition Authority needs greater independence and further strengthening

Poland has gone a long way in setting up well designed competition policies and ranks above the OECD average according to the 2013 OECD indicators of Competition, Law and Policy (CLP). After the start of transition, competition policy focused on monitoring market dominance of traditional state monopolies including infrastructure providers. Over the years, monitoring anti-competitive state aid also became a priority (Wise, 2003). The Competition and Consumer Protection Law of 2007 represented an important upgrade of the framework, unifying competition rules on antitrust (vertical and horizontal agreements and abuse of dominant position) and mergers. As a result, the scope of competition law activities, the processing of alleged anticompetitive behaviour and the capacity to advocate competition at different levels of government appear above the OECD average according to the 2013 CLP indicators. Nevertheless, information regarding the way in which alleged anticompetitive behaviour is tackled by the Competition Authority could be further developed, as there are no official publications explaining the assessment of alleged anti-competitive behaviour, such as abuse of dominance and horizontal and vertical agreements (Alemani et al., 2013).

Overall, the Competition Authority is perceived as an efficient competition enforcer, despite the weak competitive pressures in the economy (see above) and its limited budget. According to the 2013 edition of the Rating Enforcement of the Global Competition Review (Global Competition Review, 2013), which is based on a survey sent to antitrust lawyers, academics and journalists, the Polish Competition Authority received a three-star rating (out of a maximum of five). The enforcement of competition policy in Poland is considered similar to that in the Czech Republic, Finland or Sweden but significantly below that in France, Germany, the United Kingdom or the United States (Table 2.3). The Review points out that the size of a competition authority and its budget are correlated with its rating. The Polish Authority is not particularly big, and its budget is also not large: with about 130 people working on competition, its staff is small in absolute terms and represents a smaller share of total employment than in many other countries. Taken at face value, this indicates that allocating more resources to the agency could improve competition enforcement in Poland.

Table 2.3. **Rating competition authorities**

	Elite (5 stars)		Very good (4 stars)
European Commission	DG Competition	Japan	Fair Trade Commission (4½ stars)
France	Competition Authority	Australia	Competition and Consumer Commission
Germany	Federal Cartel Office	Brazil	CADE
United Kingdom	Competition Commission	Netherland	Competition Authority
United States	Department of Justice's antitrust division	Spain	National Competition Commission
United States	Federal Trade Commission	United Kingdom	Office of Fair Trading
	Good (3 stars)		**Fair (2 stars)**
Canada	Competition Bureau (3½ stars)	Belgium	Competition Authority (2½ stars)
Italy	Competition Authority (3½ stars)	Chile	National Economic Prosecutor's Office (2½ stars)
Korea	Fair Trade Commission (3½ stars)	Denmark	Competition and Consumer Authority (2½ stars)
New Zealand	Commerce Commission (3½ stars)	Mexico	Federal Competition Commission (2½ stars)
Austria	Competition Authority (3½ stars)	Pakistan	Competition Commission (2½ stars)
The Czech Republic	Office for the Protection of Competition	Turkey	Competition Authority (new entrant) (2½ stars)
Finland	Competition Authority	Lithuania	Competition Authority
Greece	Competition Commission		
Hungary	Competition Authority		
Ireland	Competition Authority		
Israel	Antitrust Authority		
Norway	Competition Authority		
Poland	**Office of competition and consumer protection**		
Portugal	Competition Authority		
Russia	Federal Antimonopoly Service		
South Africa	Competition Commission		
Sweden	Competition Authority		
Switzerland	Competition Commission		

Source: Global Competition Review (2013), *Rating Enforcement 2013*.

Besides the Authority's limited resources, competition enforcement in Poland faces four serious challenges. The first concerns the current legal framework which offers little power to the Competition Authority as regards the enforcement of structural remedies. The Competition Authority can start a market study and publish its conclusions, but it cannot, for instance, split up dominant firms. This is an important issue in some sectors, such as telecommunications, energy, railways, air transport and airports, in which market concentration is high and firms are mostly state owned. For example, the Authority cannot force the vertical separation of companies if they abuse their monopoly power in terms of third-party access to their network infrastructure (such as the gas and electricity transmission and distribution networks). This stands in contrast with countries like Austria, Canada, Germany, Ireland, Japan the United Kingdom and the United States, where structural separation remedies are available under national competition law (OECD, 2012b). A welcome draft amendment would give the Authority more power to reduce market power and SOE monopoly rents through structural remedies.

A second challenge relates to cartel cases and inefficiencies in the legal system. Concerned parties can appeal the Competition Authority's decisions first in a court specialised in competition issues and then, in a second instance, in a "normal" court. The time lapse between a first decision and a final court ruling can thus be very long. While this is certainly not a major problem for mergers, as they are not allowed to take place before the final ruling, the long delay may have important economic consequences in the case of cartels, given that cartels can continue operating throughout the period up to the final ruling. For instance, no final legal decision has been made thus far in the case of an alleged cement industry cartel reported by the Competition Authority in 2009. Developing information and communication technology use would help to reduce the length of court procedures (Palumbo et al., 2013).

A third challenge is that the political independence of the president of the Competition Authority is not fully guaranteed, despite important improvements. While the Competition Authority has shown considerable independence in its decisions in individual cases (Wise, 2003), an amendment to the 2007 Competition Act transformed the five-year mandate of the President into an open-ended contract. The incoming Prime Minister in 2008 used this opportunity to nominate a new head who was in turn dismissed in February 2014. The open-ended contract and the fact that its President can be recalled without justification potentially expose the Competition Authority to political pressures. It would be useful for the President to have a non-renewable fixed-term tenure of five or six years, straddling electoral cycles, and a contract ensuring he or she cannot be dismissed without fault. At the same time, it needs to be acknowledged that a formal competitive recruitment process for the nomination of a new President and eligibility criteria, such as professional experience and education, have been put in place to ensure high professional competence and transparency. The Prime Minister can choose only from three candidates short-listed by a group of experts who are nominated under his/her authority. The group of experts has to justify the non-selection of candidates for the short list in writing, with the names of the short-listed candidates being published in an official government journal.

Finally, the leniency programme implemented in 2004 to fight cartels could provide greater incentives. Leniency, which gives immunity or reduced fines for cartel participants for disclosing information, is an important tool in the fight against cartels. Between 2004 and 2011 the Competition Authority received only 30 applications for leniency, but 16 firms applied to the programme in 2012 (UOKIK, 2013). A recent draft amendment to the Competition Act prepared by the Authority would enhance the functioning of the leniency programme by increasing rewards to cartel participants who report them. The Polish "leniency plus" programme, inspired by US legislation, would offer a reduction in fines for those cartel participants who were the second or third to report the existence of a cartel, and thus do not qualify for the initial leniency, if they report another cartel agreement. The amendment would also increase the incentives of natural persons including managers and sales representatives to provide evidence of cartels. While under the current legislation the liability of natural persons, such as executives and managers of cartel members, is limited to procedural violations, the draft amendment would expand their liability to anti-competitive conduct, allowing the Authority to impose fines on them of up to PLN 2 million (about half a million euros) but also to grant them leniency.

The draft amendment also comprises other important improvements: the simplification and shortening of antitrust procedures and the inclusion of a list of possible remedies the Competition Authority may enforce to remove barriers to competition. In particular, it would introduce structural remedies to enforce competition policy (see above). A further improvement proposed is the simplification and acceleration of the merger-review process, which would make it easier to concentrate on the potentially most harmful deals.

Private enforcement of competition laws remains limited

Private enforcement involves actions brought by private individuals before the ordinary courts seeking compensation for losses incurred as a result of breaches of competition law. Public enforcement has historically been dominant in Poland, and consumers rely heavily on the Authority to control anti-competitive behaviour. When it was first established in 1990, the main task of the Competition Authority was to enforce competition law; it became responsible for the protection of consumer interests only in 1996. Indeed, there is substantial empirical evidence that strengthening consumers' rights, protection and information increases competition (OECD, 2008b). The enforcement of both policies under one roof provides for a high level of co-ordination of enforcement activities. The antitrust act on the basis of which the Authority has been operating since April 2007 enables it, *inter alia*, to impose financial penalties amounting to 10% of violators' net income from the previous year on undertakings applying practices infringing consumers' collective interests.

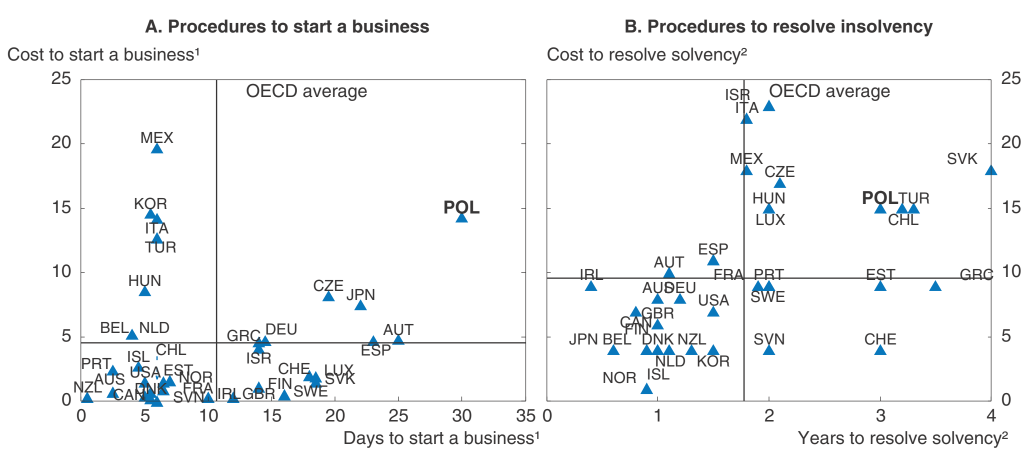
As gathering evidence is rather difficult and the proceedings are costly in competition cases, private enforcement of competition law is bound to be limited in most countries. Consumer organisations and class actions can encourage private claimants to undertake legal actions (OECD, 2011a). The notion of class actions was introduced into Polish law in July 2010 in accordance with the Act of December 2009 on collective redress (OECD, 2011b). Consumers and entrepreneurs can seek such redress for common damage. The Act does not limit consumer claims as to their object, and they could result from antitrust infringements and competition law violations. For example, in July 2013, the court found that BRE Bank unlawfully collected portions of loan instalments from a group of 1 247 consumers and awarded refunds with statutory interest. It is one of the first class-action lawsuits filed in Poland and the largest in terms of the number of claimants. However, competition infringements remain scarce, with only one class action filed for misleading advertising among the over 40 class actions undertaken in 2010-11 (Piscz, 2012; Tulibacka and Goral, 2013). The small number of judges qualified to examine competition law cases, potential plaintiffs' limited knowledge of the relevant procedures and the absence of punitive damages partly explain the overall limited development of private enforcement (European Commission, 2008).

Red tape and inefficient bankruptcy procedures slow entrepreneurship

Competition and entrepreneurship suffer from a number of barriers to the entry and exit of firms. Indeed, empirical cross-country evidence suggests that red tape acts as a drag on firm and job creation (Ciccone and Papaioannou, 2007). The government estimates the administrative burden imposed upon business by regulation at more than 5% of GDP per year (OECD, 2012c). Red tape and cumbersome registration processes are likely to weigh particularly on foreign companies' penetration by FDI or otherwise. Attracting more internationally mobile investors will require improving the business environment. In particular, some regulations applying to professional services may hinder foreign competition. For example, the European Commission (2012a) argues that Poland's poor transposition of the single-market legislation negatively affects the business environment, in particular for foreign companies. Although Poland transposed the Services Directive, the effect of the resulting horizontal law on a number of sectoral acts remains uncertain, especially with respect to the cross-border provision of services such as education and tourism (for example, establishment, registration requirements and obligation to possess a special identity document).

The government has launched a programme aimed at reducing red tape (OECD, 2012c). In 2011, several significant improvements to economic law and business registration procedures were implemented. They aim to cut red tape for setting up and running businesses by replacing around 200 administrative certificates by self-certifications and by reducing the number of documents needed for starting a business. The information obligations required to run a business have also been cut. However, the registration time for companies to be allowed to operate is still long. While new firms have been able to register on the Internet since mid-2011 and the time needed for the registration of limited liability companies is now one day, the usual cost and time required to start a business measured by the World Bank Doing Business survey remain high by OECD standards (Figure 2.8, Panel A). The government plans to further ease the administrative burden by implementing new streamlining measures and by reducing the paperwork related to the collection of taxes and

Figure 2.8. **Procedures to start a business and resolve insolvency remain long and costly**



Note: Vertical and horizontal lines represent the OECD average process length and costs, respectively.

1. The cost to start a business is recorded as a percentage of the economy's annual income per capita. It includes all official fees and fees for legal or professional services if such services are required by law. Time to start a business captures the median duration that incorporation lawyers indicate is necessary in practice to complete a procedure with minimum follow-up with government agencies and no extra payments.
2. The cost of the insolvency proceedings is recorded as a percentage of the value of the debtor's estate. Time to resolve insolvency represents the time for creditors to recover their credit in calendar years. The period of time measured by *Doing Business* is from the company's default until the payment of some or all of the money owed.

Source: World Bank (2013), *Doing Business, 2014*.

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social security contributions. For example, welcome e-procedures would allow new entrepreneurs to submit a unique application for the business register, the revenue office, the social security agency and the statistical agency (*Polish News Bulletin*, 2014).

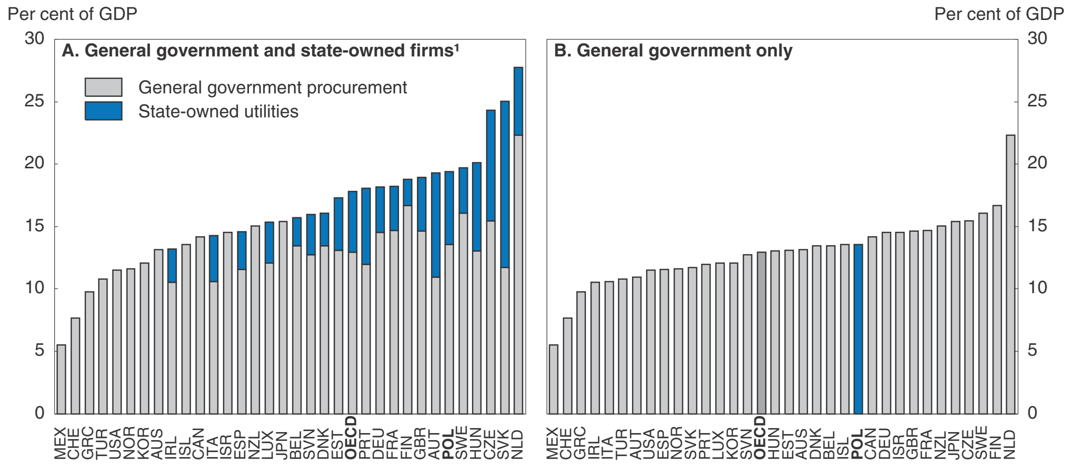
Time-consuming and costly bankruptcy proceedings also deter entrepreneurship and limit the ability to save viable businesses, especially during economic downturns. They may also hamper the exit of inefficient businesses, limiting resource reallocation. The most important feature of a good bankruptcy regime is that it deals with problems clearly, fairly and expeditiously. If it is also lenient toward indebted companies, that has advantages for entrepreneurship in that it reduces the costs of failure and hence the downside risks, while allowing debtors to recover and undertake new initiatives. This, however, must be weighed against the disadvantages in terms of availability of capital due to weaker creditors' rights (Bravo-Biosca et al., 2013). Poland does not compare favourably here (Figure 2.8, Panel B). The World Bank *Doing Business* survey suggests that the bankruptcy process takes about a year more than in the average OECD country and that the cost is also far higher. The bankruptcy proceedings remain open as long as valid creditor claims are outstanding, and hence the process can be lengthy. Only when it is completed, and assuming there are no issues of bad faith, can the bankrupt party start a new business. The result of these arrangements is that relatively few bankruptcies occur. In 2012, 4 313 entrepreneurs filed for bankruptcy, but only 916 were declared. Encouragingly, the stigma of bankruptcy seems to have been reduced, and Polish society appears increasingly inclined to allow a "second chance" for entrepreneurs who have previously gone bankrupt (European Commission, 2012b). Furthermore, in 2014, a planned reform of bankruptcy procedures would allow companies to undertake early restructuring procedures, introduce simplified arrangements and develop second-chance policies.

Natural persons operating a business in sole proprietorship may file for bankruptcy only under business law as personal bankruptcy law does not apply to entrepreneurs (OECD, 2010b; Ministry of Economy, 2012). As lenders to small businesses often require that the owner provide a personal guarantee for the loan, such as a second mortgage on his/her house, the personal guarantee of a firm's owner and the level of outstanding debt in case of business failure may effectively prevent entrepreneurs from creating a new firm and discourage firm entry (Polish Agency for Enterprise Development, 2011).

Improving public procurement capabilities would increase competition

The design and implementation of public procurement policies have important implications for product market competition, public finances and long-term growth. In Poland, general government public procurement is estimated to have accounted for more than 13% of GDP in 2011; if public procurement by SOEs is also taken into account, it would have been around 19% of GDP (Figure 2.9). The amounts involved in public procurement contracts are substantial: contracts awarded according to Polish public procurement law amounted to 9.5% of GDP in 2011 (Public Procurement Office, 2012). If public procurement does not ensure competitive neutrality, i.e. the selection of suppliers with the best combination of prices and quality, incentives for firms to compete are significantly reduced. Moreover, distorted public procurement policies have a detrimental indirect impact on long-term growth, as they often concern physical infrastructure that has a great impact on international competitiveness (OECD, 2011c). In addition to getting the general competition policy framework right, including criminal justice provision, the OECD recommends a set of rules on the optimal design of public procurement to reduce

Figure 2.9. **Public procurement as a share of GDP in OECD countries, 2011**



1. Data for public procurement of state-owned enterprises refer to 2008. Estimations of the public procurement transactions of state-owned utilities are available only for some OECD countries that are also members of the EU. The missing countries are not included in the OECD average for this calculation.

Source: OECD (2011d and 2013d), *Government at a Glance*.

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anticompetitive behaviour (collusion) and corruption. Generally, these should be accompanied by national market opening to international competition, increased e-procurement, expanded education of public officials, a systematic review of public-contract awards and the auditing of public-procurement procedures (OECD, 2011c). In Poland, public procurement is open to international competition, and the Public Procurement Office controls contract awards and procedures, but some specific factors hinder the efficiency of public procurement practices.

The large degree of state ownership in potentially competitive segments of the Polish economy threatens competitive neutrality between public procurement bidders. Although public procurement rules are the same for private and public companies (special provisions apply to in-house procurement under some special circumstances defined by the European Commission's jurisprudence (OECD, 2012a) and the gas, water and electricity sectors), governments may be tempted to favour state-owned firms during bidding processes. These anti-competitive pressures may be particularly intense in sectors dominated by local governments where personal relations may be more important. Though decentralised local governments may be better at eliciting people's preferences and providing population-specific services than is central government, local public resources may easily be captured by local elites and politically powerful groups. In Poland, sub-central governments have often tried to shield local SOEs from competition. For example, municipalities have sought to prevent entry by funeral services companies in municipal cemeteries, and in many cases there is little competition for local water services and public transportation (OECD, 2009a). Similarly, municipalities have been shown to protect local monopolies in waste collection markets by requiring the use of municipal waste-storage sites even if cheaper alternatives exist nearby. The law that transferred waste-management responsibilities to local governments in June 2013, requiring them to establish public procurement processes, also implies a need to build sufficient public procurement capacities at the local level. Alternatively, local governments could set up a joint public agency in charge of waste management contracts to achieve scale economies in human resources and ensure fair competition in the bidding processes.

There is a heavy reliance on price for awarding public contracts in Poland: the lowest bid is almost always chosen. In about 90% of the awarded contracts in 2011, price was the only contract award criterion (Public Procurement Office, 2012). The main explanation is that civil servants are afraid of being accused of corruption. For simple tasks, the price of an offer may be the most important factor for decision makers. But for more complicated projects, technical details and methodologies, timing, execution, organisation, guarantees and references should also be taken into account both in contract specifications and the assessments of offers. In particular, environmental impact should be explicitly considered. Since the public sector is a major buyer of a wide range of products, its purchases can promote technological developments that enhance output quality, public health and ultimately citizen well-being (OECD, 2011c). By contrast, the excessive reliance on the lowest bidders could generate unfair competition, lower quality and increase the risks of leaving projects unfinished if contractors go bankrupt. A well known case is COVEC, a Chinese company, which was supposed to build a stretch of the A2 highway but which pulled out because the final costs would have been twice the amount of its initial offer.

Overall, contracting authorities should seek to build up capacities to better judge technical aspects of offers. For particularly complex projects, developing competitive dialogues, used for instance in the United Kingdom, could help civil servants appreciate technical details. In such procedures, competitors interact with each other on the specification in an open way, and bid prices relate to very similar specifications. A more stable public procurement framework would also help reduce uncertainty and lower bidding costs (OECD, 2013e). Better information during public tenders, focusing specifications on functional performance and appropriate sanctions for anti-competitive behaviour, could improve fairness, transparency and value for money in public procurement (OECD, 2009b). According to the amended Public Procurement Law proposed by the Public Procurement Office in August 2013, bidders in public tenders offering exceptionally low prices would be requested to provide evidence in support of the possibility of successful completion of the contract within the specified cost limit (*Polish News Bulletin*, 2013c). The proposed amendment also specifies dissuasive sanctions in case of infringements. Bidders may be excluded from future tenders and have their bid bonds retained by the ordering party if no satisfactory evidence is provided.

Heterogeneous progress across sectors

Polish regulatory policies for private service sectors vary in scope. *First*, network industries are characterised by natural monopoly segments, into which competition is difficult (or even impossible) to introduce. In such cases, the regulatory framework should be directed to securing non-discriminatory third-party access to the networks and opening potentially competitive segments to competition. *Second*, some sectors, such as professional services, retail distribution, financial services and agriculture, are inherently competitive, but the intensity of competition appears affected by distortionary regulations and the extent of state ownership. For example, self-regulation by professional service associations tends to strengthen incumbents' positions. Some regulations also favour local monopolies in the retail sector and reduce entry and exit in agriculture. *Last*, state ownership in financial services may also reduce competitive pressures.

Competition remains weak in most network industries

In network industries such as electricity and gas, if a company owning and managing the natural monopoly segment of the sector (the transmission and distribution systems) is also present in the potentially competitive part (production and supply), it may be tempted to shelter its activities in the competitive segment by barring or complicating access for (potential) competitors to the natural monopoly infrastructure segment. Therefore, separating vertically integrated utilities into different entities for the network infrastructure and competitive parts may enhance third-party access. Such a separation can take the form of accounting separation within the same company, legal and functional separation when the company is split into two legal, functionally unbundled entities under the supervision of the same owner, or ownership separation. Ownership separation tends to wipe out any bias of the infrastructure owner and operator in terms of third-party access. Though it is often claimed that vertical separation may result in under-investment in physical infrastructure, a vertically integrated firm can also engage in strategic under-investment to keep out new entrants from its competitive segments. Therefore, increasing competition in the competitive segments triggered by vertical separation is likely to generate significant investments by new entrants (OECD, 2012b). Indeed, empirical evidence for OECD countries suggests that incentive regulation in the natural monopoly segment coupled with an independent sector regulator increases investment (Égert, 2009).

State-ownership distorts competition in the electricity and gas sectors

Vertical separation started in Poland's gas and electricity sectors in 2004 under the influence of EU regulations. The first steps to open up the wholesale gas market to competition were taken that year when the gas transmission network system operator, Gaz-System, was carved out from the state-controlled historical operator, PGNiG. The Treasury has a controlling stake in both companies, but a third-party access rule to the network was introduced. The amendment to the Energy Law of September 2013 contains a further improvement. The transmission system operator is now supervised by the Ministry of Economy, while PGNiG remains under the control of the Ministry of Treasury. However, the two Ministries remain ultimately under the supervision of the Prime Minister. The legal and functional unbundling of gas distributors occurred in 2007 when six regional distribution system operators were created in the PGNiG group (OECD, 2012b). In 2013, these six system operators were consolidated into one distribution operator, which remains separated from the gas supplier (PGNiG S.A.) in the PGNiG group.

The liberalisation of the gas market is ongoing. However, despite legal and functional unbundling, improved third-party access and increasing interconnection capacities to neighbouring countries, PGNiG still controlled 95% of the gas sector in 2012, including production, imports, storage, wholesale and retail sales, and distribution (ERO, 2012). At the end of 2012, a gas exchange was created, and 97 entities were entitled to trade. The government introduced obligations for PGNiG and other important gas trading companies to sell 30%, 40% and 55% of the gas entering the Polish network on the exchange in 2013, 2014 and 2015, respectively. In July 2013, an amendment to the Energy Law also eased the entry of small distribution companies by giving them the right not to unbundle their supply and distribution activities as long as they do not distort competition. While these new developments go in the right direction and should ensure more transparent rules of trading in natural gas, there is room for further increasing competition. The current low share of alternative gas suppliers implies that third-party access is not working well, and it is unclear to what extent the creation of a gas exchange will increase competition, given PGNiG's dominant position. Indeed, the Competition Authority recently found that PGNiG has been applying contractual terms and conditions that are disadvantageous for entrepreneurs making wholesale or retail purchases of natural gas (UOKIK, 2014). The government should consider encouraging more entry into gas production and distribution, potentially by fully separating the ownership of: i) gas production from transmission, because both activities are owned by SOEs; ii) gas production and wholesale sales from distribution; and iii) distribution system operators from gas suppliers. Full ownership separation, which would involve the privatisation of the gas-supplying part of PGNiG, would ease the entry of new firms and limit possible political interference via the sector regulator.

Electricity production is also dominated by a few, mostly state-owned utilities. The largest majority state-owned electricity producer, PGE, generates almost 40% of Poland's electricity, and the top four generators account for almost 70% (ERO, 2013); three of those are directly controlled by the government. A power exchange for electricity producers was set up in 2010 and a legal obligation introduced for producers to sell at least 15% of their production on the exchange. At the same time, producers entitled to receive compensation covering their stranded costs under long-term power purchase agreements were obliged to sell all generated electricity on the exchange. The electricity transmission system operator, PSE, is legally unbundled from the large state-owned producers but is also 100% state owned. As in the gas sector, in September 2013, the government shifted the control of PSE from the Treasury to the Ministry of Economy, while the Treasury remains in charge of generators. Though this is encouraging, full ownership separation should remain an objective, and the Competition Authority should be given the power to reduce dominant market positions in case of competition infringements.

The Treasury is a major shareholder in four of the five main electricity distributors. These four capital groups are indirectly government owned and vertically integrated by ownership with major generators. They are also heavily involved in supplying businesses and households. The sector regulator reckons this to be a regulatory challenge (ERO, 2012). Third-party access to the distribution grid, supervised and enforced by the Energy Regulatory Office (ERO), was strengthened in 2013, as it turned out that, while switching suppliers was simple on paper, some distributors and suppliers made it difficult by delaying the switching procedure, misinforming customers and threatening to suspend electricity supply if buyers did not sign up again (ERO, 2012). About 35% of electricity supplied through the five large distribution grids in 2012 was provided by alternative suppliers (mostly the other incumbents). Nevertheless, there is a natural potential bias for distribution system operators to favour suppliers belonging to the same holding company over alternative operators; only full ownership separation – implying the privatisation of the state-owned generators – would fully eliminate this potential bias.

The National Renewable Energy Action Plan sets a 2020 target of 15% for the share of renewable energies. However, renewable forms of electricity remain underdeveloped. Since 2005, mandatory quotas for power companies and a green certificate market have pushed many state-owned coal-fired power plants to co-fire with biomass, but the development of other technologies has been limited. A better pricing of externalities could make other renewables more competitive, but grid capacity and management would also need to improve. Planned extensions of the interconnection capacity with neighbouring countries would foster competition between renewables producers and facilitate balancing of demand and supply, which is particularly challenging with intermittent supply typical of wind- and solar-powered generation (OECD, 2012c).

The natural-monopoly parts of the sector (the transmission and distribution grids) need to be overseen by an independent sector regulator that would simulate a competitive environment via incentive regulation with a view to forcing the incumbent operator to reduce inefficiencies. In Poland, the sectoral regulator, ERO, sets the regulatory framework for the distributors and the transmission system operator. This includes an RPI-X price-setting formula for these companies imposed over a period of four years (2012-15), which is long enough for them to reap the benefits of efficiency improvements. Nevertheless, imposing tough efficiency targets may be a tricky task for the regulator, given that almost all operators are government controlled. Therefore, it is vital to strengthen its political independence. In September 2013, the open-ended contract of the ERO President was transformed into a five year fixed-term contract that can be renewed only once. Ideally, the contract should also be made non-renewable and prevent the President from immediately taking a position in the energy sector at the end of his/her mandate to avoid revolving-door opportunities.

The liberalisation of the telecommunications market has increased competition

Liberalisation of the telecommunications market is fairly advanced. As a result, the market is increasingly competitive, especially in mobile services. One important change was the reinforcement of the independence of the sector regulator (UKE), which came in 2009 after the European Commission opened proceedings against Poland. The UKE's President now has a five-year fixed-term contract, and the conditions for dismissal are also clearly spelled out, contrary to other sector regulators and the Competition Authority. The President cannot take up a job in the telecommunications industry during the year following departure from the UKE, a safeguard aimed at minimising conflicts of interest. UKE enforces telecommunication regulations by monitoring access charges using tests for predatory pricing (based on audited costs) and oversees how quickly customers can change providers. From 2006 to 2013, UKE made some 400 decisions regarding complaints over third-party access. However, UKE's decisions are frequently appealed before administrative and general courts, which make their implementation lengthy, and a mobile termination rates case triggered extraordinary action by the European Commission (European Commission, 2012c).

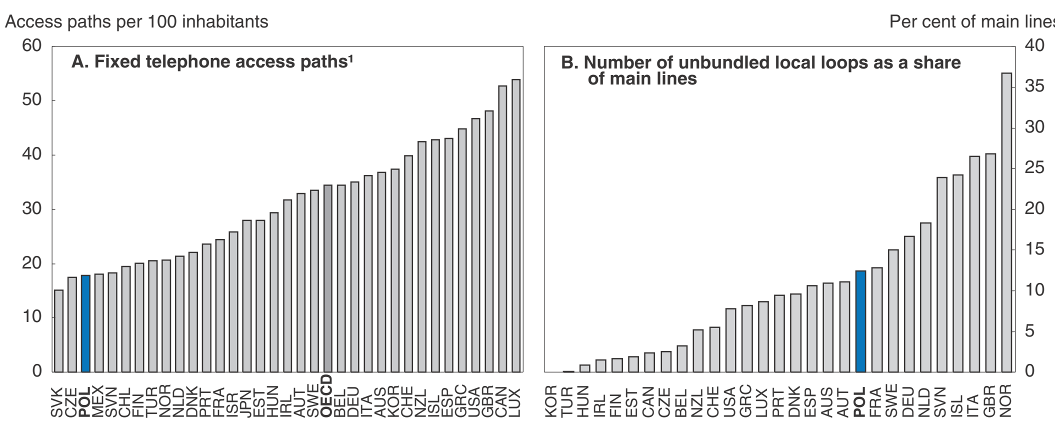
The sector also differs from other network industries due to its comparatively low level of government ownership. The incumbent firm, Telekomunikacja Polska (TPSA), was fully privatised in 2010. Switching barriers have been lowered in recent years, shown by the shorter time needed to change operators for fixed-line phones while keeping the same number ("portability") from 23 days in 2009 to an average of 7 days in 2013 (one day for the applications directly submitted by customers and 14 days for others). However, TPSA still dominates both landline telephones and, to a lesser extent, fixed-line broadband. A new entrant in the mobile market has recently boosted competition, lowering prices to levels considerably below the EU average, while mobile termination rates have been declining (OECD, 2012d).

Despite these competitive pressures, the telecommunications sector still faces some important challenges. *First*, TPSA's privatisation also suspended the separation of its wholesale and retail activities. Given TPSA's record of delaying tactics regarding third-party access, this still requires close vigilance by UKE. Notwithstanding the 2009 agreement between UKE and TPSA on third-party access to the physical infrastructure, in 2011 the European Commission fined TPSA for abusing its dominant market position in broadband. Indeed, TPSA "proposed unreasonable conditions, delayed the negotiation processes, rejected orders in an unjustifiable manner and refused to provide reliable and accurate information to alternative operators" (OECD, 2012b, p. 81).

Second, the fixed-line network remains underdeveloped and outdated. Landline telephony is fairly limited, and prices are above the OECD average for most bundles (OECD, 2013f). In 2011, the number of telephone lines per capita was among the OECD's lowest (Figure 2.10, Panel A). In addition to TPSA, other SOEs own and operate backbone infrastructure (TK Telekom – owned by public railway and power companies – and Exatel, controlled by the state-owned gas firm). Mobile and internet use has been growing rapidly in recent years but is reliant on upgraded backhaul networks to provide broadband connectivity services. The backbone infrastructure is patchy, and extending the network may be costly, especially in rural areas with low population density. Delivering a well functioning broadband network, using either fixed or mobile wireless networks requires the roll out of these networks into these areas. If rolling out fixed broadband in the last mile is deemed to be expensive, expanding wireless networks may be appropriate. However, this still requires the fibre backbone to be rolled out to the antenna sites.

Figure 2.10. **Fixed-line infrastructure is underdeveloped**

2011 or latest year available



1. Fixed telephone access paths include analogue and ISDN lines.

Source: OECD (2013f), *Communications Outlook 2013* (Panel A) and OECD (2011d and 2013f), *Communications Outlooks 2011 and 2013* (Panel B).

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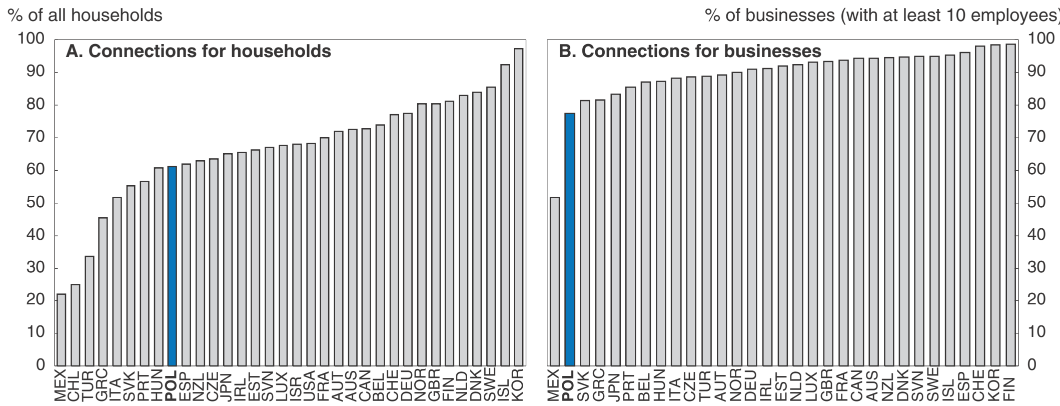
Third, the underdevelopment of the fixed-line network may create competition problems at the local level for Internet service providers, where there could be limited choice for consumers. Local loop unbundling (LLU) may not yet be fully functional, in view of the concerns about third-party access raised by the European Commission in 2011 (OECD, 2012b). Progress in LLU has been fast but from a low level (Figure 2.10, Panel B): the share of unbundled local loops in total main lines increased from 5.3% in 2009 to 12.4% in 2011, and substantial investment would be needed for further upgrading (OECD, 2011d and 2013f).

Finally, the low Internet and broadband penetration rates can impede the rapid distribution of ideas and information and act as a drag on competition and economic growth (OECD, 2011e). The number of households with Internet connections is low in international comparison (at some 72% in 2013), in sharp contrast with almost 100% in Korea (Figure 2.11). Furthermore, Poland is the second-worst OECD performer in terms of business access to broadband. More than 20% of firms with 10 or more employees still did not have broadband connections in 2011.

Figure 2.11. **Internet access is still low by international standards**

Broadband connections, 2011 or latest available year



Source: OECD, *Key ICT Indicators*, 2012.

StatLink http://dx.doi.org/10.1787/888933000248

Postal services are being liberalised

Domestic postal services have been progressively liberalised in Poland since 2006 for parcel delivery and partly for letters. The incumbent operator, Polish Post, is considered highly inefficient (Cienski, 2013), implying that increased competition would generate large productivity gains and lower prices. In November 2012, the new Postal Law designated Polish Post as a universal service provider for a transitional period of three years to fulfil the requirements of the 2008 EU Postal Directive, and the market for letters less than 50 grammes in weight was opened to alternative providers in January 2013. After the three-year transition period, a new national operator will be selected for 10 years through a competition organised by the sector regulator (UKE). Potential bidders at the tender to be held in 2016 are complaining that the requirement of having a national postal infrastructure is very difficult to meet within three years and that the incumbent enjoys a considerable advantage from the start. Other sources of unfair competition are the fact that the incumbent operator may be able to keep its privileged position for postal money orders and that the definition of mass sender in the law provides VAT exemption for universal postal services that are currently provided by Polish Post. Finally, only proof of registered letters posted at a post office is considered as official, and alternative service providers do not have full third-party access to the incumbent's postal infrastructure (Integer, 2012; WIK-Consult, 2013).

The water industry should be supervised by a nation-wide regulator

The water sector is dominated by municipally owned water and wastewater utilities, which are mostly not corporatised. Out of the 50 largest companies, only one is not majority-owned by local governments (Saur Group in Gdansk, controlled by a French state-owned firm). The water industry landscape is very fragmented: there are about 1 600 water companies, compared with slightly fewer than 2 500 municipalities. There is no national sectoral regulator, and the mayor of each municipality is in charge of supervising the local water company. Water companies propose tariffs, which have to be approved by municipal councils. Overall, it seems that they are not very efficient, as they suffer from overstaffing, a lack of automation and low wages (OECD, 2011e), and, in 2008, water and sanitation bills as a share of disposable income were the highest among the 22 OECD countries surveyed (OECD, 2010c).

The creation of an independent national sector regulator could help increase efficiency. In the recent past the Competition Authority has had to handle a number of cases of abusive contract clauses faced by small businesses and consumers. A national regulator could set some sector-wide standards for invoicing and other procedures relating to suppliers' monopolistic positions. It could set productivity targets for each company using international benchmarking and yardstick regulation, which would simulate a competitive environment. Such regulation could push water companies to merge to reap the benefits of scale economies. Waste water collection and treatment services could also be included under the responsibilities of this national water regulator. More efficient operations could leave more room to finance badly needed investment in the water supply and sewage infrastructure. Poland is one of the few OECD countries where a non-trivial share of the population, 13%, was not connected to water supplies in 2009. Also, compliance with EU regulations in terms of water sanitation implies a need for substantial investment.

Competition in railways remains limited

Increasing competition in the rail sector is likely to link prices more closely to service quality, which might help to enhance intermodal competition, increase the share of rail in overall traffic and lower greenhouse gas emissions and air pollution. The special chapter on transport and infrastructure in the 2008 *Survey* suggested that the Polish rail sector was very inefficient (OECD, 2008a; Kierzenkowski, 2008). Although some progress has been made, the quality of railroad infrastructure is still perceived by world executives to be the worst in the OECD (World Economic Forum, 2013). Several restructuring programmes have been carried out to improve the efficiency of the state railway company (PKP). It was split into a holding company, owning freight, national and regional passenger transportation and infrastructure-management entities. In 2007, the government launched a strategic plan called "Strategy for railway transport until 2013". At the heart of the programme was the preparation of the cargo and transnational passenger parts of PKP for privatisation. While the cargo part of the company (PKP Cargo) was partly privatised in October 2013, the government still controls a majority of its shares, and the privatisation of the passenger part (PKP Intercity) has not yet started.

SOEs dominate the passenger transportation segment through PKP Intercity and a number of regional operators. The five largest operators accounted for more than 90% of the market in terms of passengers in 2011 (UTK, 2012). Only one company is not controlled by the state or local governments – Arriva RP, belonging to Deutsche Bahn, which has a market share of 1%. More competition could be expected to result in substantial productivity gains. The 2008 *Survey* (OECD, 2008a) suggested that competition could be encouraged via competitive bidding for the provision of services in specific regions. But it is also important that the organisation of passenger transport on a regional basis does not lead to anti-competitive behaviour by operators restricting inter-regional traffic.

The liberalisation of rail freight transportation started in 2003, and a large number of licenses were soon issued by the sector regulator (UTK) for both freight transport and rolling stock leasing. Accordingly, the prices of rail freight services have declined sharply, new services have been developed, and the market share of the incumbent (PKP Cargo) has fallen. Yet, in 2012 PKP Cargo still had a market share of 60% (down from 80% in 2006), and other SOEs, including PKP LHS, which is specialised in heavy industry, and Lotos Kolej, transporting the products of the state-owned oil company Lotos, played an important but declining role in the freight market. The fact that the management of the rail infrastructure is dominated by the state-owned company PKP PLK S.A., part of the PKP group, is a serious impediment to competition. Indeed, PKP Cargo had a privileged position regarding the allotment of routes by PKP PLK S.A. (OECD, 2008a). Moreover, 6 out of the 28 operating transshipment terminals (including the most important one – Malaszewicze – at the Eastern border) are owned by PKP Cargo or its subsidiary, Cargosped Sp. z o.o. The 2008 *Survey* recommended vertical separation, preferably based on ownership, rather than legal or accounting separation, of the main state-owned infrastructure manager (PKP PLK S.A.) from the PKP Group, which would help increase competitive neutrality between the public and alternative carriers and improve the transparency of access pricing by eliminating the possibility of cross-subsidies within the PKP Group.

The independence of UTK could be improved. As in other network industries with strong public ownership, the President of UTK is appointed for an indefinite period and can be recalled by the Prime Minister at his own discretion (Krol, 2010). In fact, the Prime Minister used his prerogative in 2012 and dismissed the last UTK's President. Enhanced political independence could be insured through a fixed-term non-renewable mandate defining clear dismissal conditions, coupled with the vertical separation of the infrastructure manager from the state carrier. This would help guarantee third-party access to the network, including non-discriminatory access pricing. Indeed, UTK may have tended to approve prices put forward by the infrastructure manager, PKP PLK S.A., with little discussion (OECD, 2008a), resulting in inflated charges that have led to significant claims by rail network users. In May 2013, the EU Court of Justice found that charges for accessing the infrastructure were excessive (Court of Justice of the European Union, 2013). Recently, UTK has displayed more scrutiny about proposed access charges: in April 2013 it refused to approve the access charges initially proposed by PKP PLK S.A. until some significant amendments were made.

State-ownership is important in aviation and seaports

Poland has 13 airports. The stakeholders are the Polish Airports' State Enterprise (PPL) (supervised by the Ministry of Infrastructure and Development), municipalities and regions. Warsaw and Zielona Góra airports are managed by PPL, and the other 11 airports run their businesses as separated commercial law companies, though PPL still owns substantial shares in many of them. This ownership structure is not conducive to competition among airports. A solution would be to fully insure the independence of the infrastructure manager from the airport operators to allow more competitive and transparent pricing policies. Airport owners could issue long-term concession agreements for different airports. The key, of course, is that the auctions and concessions be properly designed and executed to prevent collusion and attract entry, while avoiding opportunistic renegotiations and providing sufficient incentives for long-term investments (OECD, 2007). The government currently aims to corporatise PPL to increase its efficiency and financing opportunities. This could be a first step towards privatisation, as recommended in the 2008 *Survey*.

Polish airports have some degree of regional monopoly power, but their overlapping catchment areas and the high share of low-cost airlines, which shift easily between airports, put downward pressure on airport charges. Since January 2014, the Civil Aviation Authority (CAA) monitors airport charges based on forecasted costs. CAA is relatively independent as the rights and duties of its President are defined in Aviation Law Act. Its President has an open-ended contract and is appointed by the Prime Minister. Though the recruitment process is open and competitive, awarding CAA's President a fixed-term non-renewable contract ensuring that he or she cannot be dismissed without fault would guarantee further independence. For airports above 5 million passengers, CAA can accept or reject charges proposed by airport managers, while for smaller airports it can require modification of the established charges. However, it can do so only based on whether the procedures followed the legal fee-setting framework but cannot verify economically the costs behind the fee proposals (Wolszczak, 2009). Allowing the regulator to verify the economic costs covered by airport fees would likely increase competitive pressures.

Air transport has been developing at a rapid pace, as domestic and international flights were liberalised following Poland's EU accession and the entry of a number of low-cost airlines. Yet, the state-owned airline company (LOT) has a 28% market share in terms of passengers transported (similar to Ryanair's but above Wizz Air's 20%, according to *Warsaw Business Journal*, 2013). The government has made several failed attempts to privatise LOT. It needs urgent restructuring, having incurred losses for a number of years, requiring public subsidies, currently under investigation by the European Commission. A large, subsidised state-owned airline and the presence of state-owned airports may challenge competitive neutrality. Though Polish Aviation Law ensures some independence of landing slot allocation from airport owners and airlines, state-owned airports may be tempted to shelter LOT from its competitors through access prices.

According to the World Economic Forum (2013), the quality of Poland's seaport infrastructure is perceived as poor, ranking 97th out of 148 countries. One reason for this is that the major seaports are state-owned and poorly managed. But they have started upgrading their outdated capital stock, as advocated in the 2008 *Survey*. While they are still in public hands, private investors have created companies operating in existing ports, contributing to their revival. At the same time, geographically close ports, such as Gdansk and Gdynia, have started competing with each other. More widespread privatisation could further enhance competition and efficiency. However, ports enjoy favourable tax treatment, which may distort intermodal competition, and such tax breaks should be phased out (OECD, 2008a).

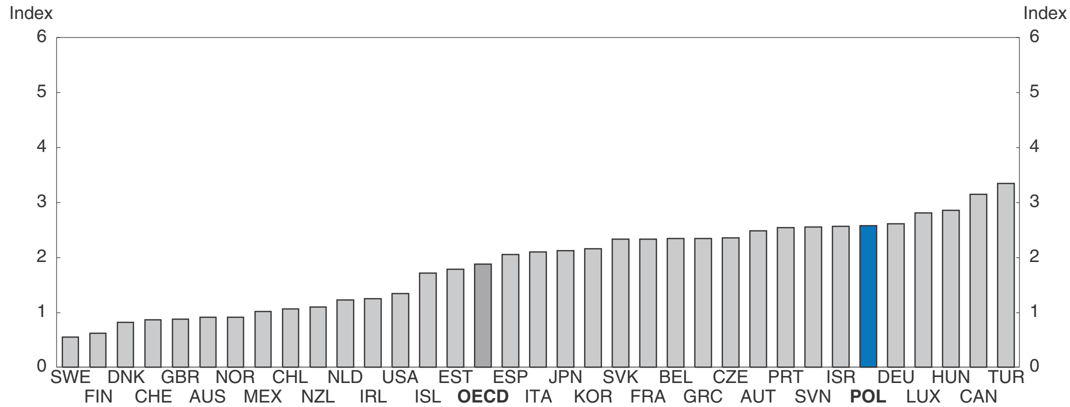
Professional services have been partly deregulated

Self-regulation (or similar rules embodied in legal statutes) in professional services is relatively common in OECD countries, but it may restrict competition unnecessarily. Indeed, Poland had about 350 regulated professions in 2011 (Rojek, 2013). Its average level of regulation of finance and legal professionals and for architects and engineers was above the OECD average in 2013 and substantially above the lowest levels observed in countries such as Finland, Sweden or the United Kingdom (Figure 2.12). Low-level indicators show that heavy regulation mostly took the form of strict entry barriers (licencing and education requirements), whereas conduct regulations are lax. This indicates that lighter entry regulations would probably foster competition, without being detrimental to the quality of services.

Against this background, the government recently launched a large deregulation programme. In 2011, about 70% of the currently regulated professions were identified for full or partial deregulation. While this would align Poland only with the EU average, it would still be a very important step towards reducing entry barriers and exposing those occupations to more competition. It is likely to reduce prices and thus monopoly rents and create additional jobs in the economy, especially for young people. Productivity will probably rise in the deregulated professions, and reduced red tape and lower input costs would also increase competitiveness in other sectors using these professional services.

Figure 2.12. **The OECD's indicator of the severity of professional services regulation in 2013**[1]

Index scale from 0 to 6, from least to most restrictive



1. 2008 for the United States.

Source: OECD (2014), preliminary *Product Market Regulation Database*.

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The deregulation programme concerns some 250 professions accounting for 6% of the labour force (about 1 million people), including 3% of the labour force in the sectors subject to complete deregulation. It will be conducted in three waves. The first, adopted by the Parliament in June 2013, comprises 51 professions, notably legal professions. It aimed to speed up and lighten entry examinations and to extend eligibility for attorneys and bailiffs, scrap the nationality requirements for notaries, phase out the university degree requirement for court and prosecutor staff, real estate brokers and managers and driving instructors, and shorten the duration of the compulsory apprenticeship for a number of professions. Although professional interest groups are opposed to deregulation and argue that it may go too far and will reduce quality, there is general public backing for it, as shown in recent opinion polls and by the approval of the first bill by both government and opposition Members of Parliament (Rojek, 2013).

The second wave of deregulation launched in the second half of 2013, is aimed at 91 professions. It is expected to be passed in the first half of 2014. The professions concerned include engineers in various sectors, accountants and tax advisors, car diagnostic technicians, commercial pilots, railway professionals and insurance brokers. For example, special examinations will no longer be necessary to become a stockbroker for those who hold an appropriate degree and have at least three years of experience with a stockbroking firm (*Polish News Bulletin*, 2013a). Some double examinations in selected professions will also be eliminated. A university degree would henceforth be enough to enter these professions; the related profession-specific exams, which overlap to some degree with what is taught in the education system, will be eliminated.

The third wave was also launched in 2013, a public inter-ministerial consultation was carried out in the summer, and the draft act was accepted by the Permanent Committee of the Council of Ministers in December 2013. The deregulations would concern more than 100 remaining occupations, mostly in finance, mining and some crafts. Further professions, including medical professions and jobs concerned with safety at work, may be added to the list. This may eventually lead to a fourth wave of deregulation.

This impressive programme will be accompanied by an *ex post* impact assessment of the deregulation process for the most important cases, which will examine its effects on prices, incomes and employment. The results may trigger corrective measures with regard to access conditions. Indeed, a careful balance needs to be struck between easing access requirements and maintaining quality, and *ex post* evaluations will help to assess whether it has been. On the one hand, there is a risk that unnecessary regulations will remain in place; on the other, some regulations may indeed lead to higher quality.

The government also intends to further reduce the extent of double examinations in some professions, conditional on the ongoing restructuring of the tertiary education system. In concert with the ongoing deregulation of professions, two further changes are being considered by the government. First, it would like to ensure that implementing EU directives in Poland will not be coupled with additional regulations at the national level. The second concerns the review of professional self-governing bodies required by law. For example, as a result of the review of the obligatory professional chamber of city planners, the government proposed the liquidation of this chamber in the second wave of deregulation.

Competitive pressures appear low in retail trade

Even though regulation in retail distribution was reduced to some extent between 1996 and 2008, Poland stood out in 2008 as one of the OECD countries with the most stringent regulation in this sector (Figure 2.13, Panel A). Disaggregated indicators show that licencing requirements are extremely burdensome, with little change over time (Panel B). Regulations concerning large outlets have been eased to some extent over time, and the protection of existing firms has remained stable at moderately high levels. By contrast, the lenient regulation for shop-opening hours was toughened between 1996 and 2003: municipalities have the right to set limits on retail opening hours, but it is rare that they impose strict opening hours. Shops can open on Sundays. Nevertheless, since 2007, they must close on most national holidays, except fuel stations and small owner-operated outlets. Large stores are allowed to have month-long sales twice a year at the end of the summer and winter seasons. However, large retailers can reduce prices if this is economically reasonable (e.g. due to high stocks) and if this is not meant to make access to market by smaller retailers more difficult. There are no restrictions regarding the extent of price reduction.

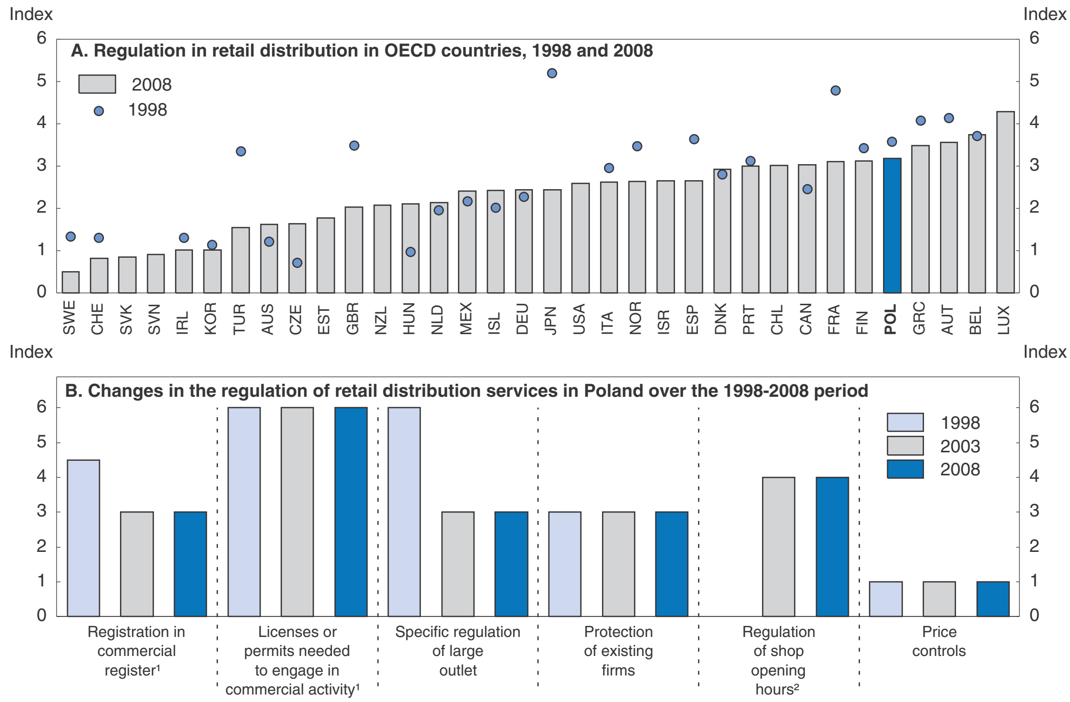
Despite the recent expansion of some of the major international retail groups and e-commerce in Poland, retail trade is to a large extent dominated by very small shops, which, in 2007, contributed to almost half of the sector's total turnover, the third highest share after Italy and Greece (Figure 2.14). This suggests that current regulations protect local incumbents from new entry. The sector's structure is also reflected in high price-cost margins (Figure 2.4) and apparent limited efficiency gains: between 2004 and 2011, average annual sectoral labour productivity growth was slightly above 1%, while Bulgaria and Latvia reached gains of around 6% per annum. These developments suggest that reducing barriers to entry could foster further competition in the retail sector, though they may also be partly explained by the preference of Polish consumers for small shops.

The agricultural sector is very fragmented

The agricultural sector appears fragmented and leaves little scope for contract-based employment. In 2010, average farm acreage was still only half the EA15 average (Figure 2.15, Panel A). Farms with less than 20 hectares represented 92% of the holdings and 85% of agricultural employment, but only 55% of total farm output (Eurostat, 2010). At

Figure 2.13. **Regulation in retail distribution services**

Index scale from 0 to 6, from least to most restrictive

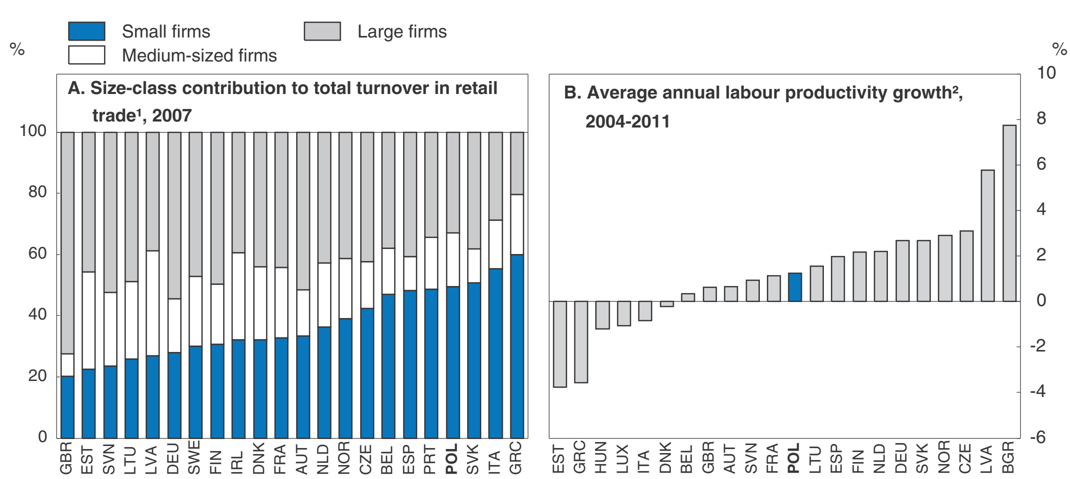


1. Refers to licenses and permits needed for food outlets.
2. The sub-indicator for regulation of shop opening hours was 0 in 1998.

Source: Update of Conway et al. (2006), "Regulation, Competition and Productivity Convergence", *OECD Economics Department Working Papers*, No. 509, OECD Publishing.

StatLink http://dx.doi.org/10.1787/888933000286

Figure 2.14. **The wholesale and retail trade sectors**

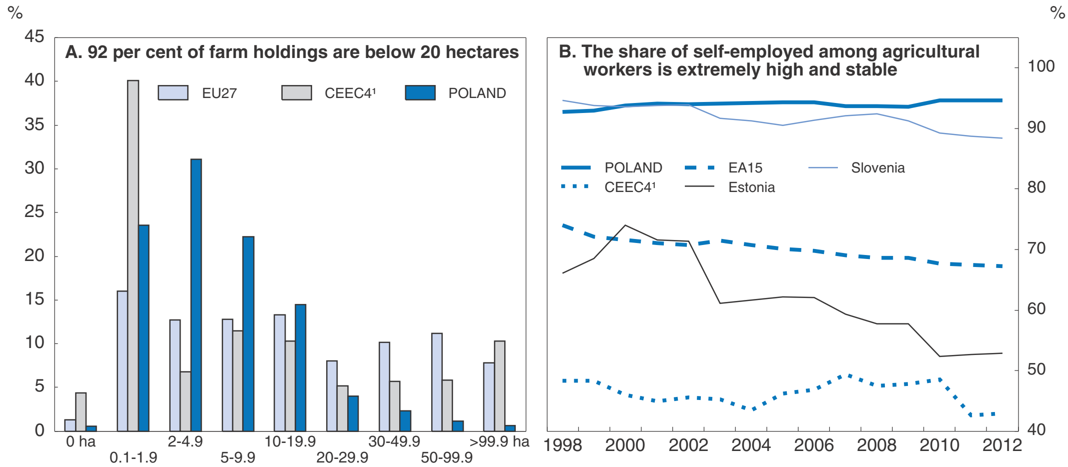


1. Small firms are those with 1 to 19 employees, medium-sized firms between 20 and 249 and large firms 250 and more.
2. Labour productivity is computed as follows: gross value added in constant prices divided by total employment in wholesale and retail trade, repair of motor vehicles and motorcycles. Data are drawn from a 10-sector decomposition.

Source: OECD's *Structural Business Statistics Database* for Panel A; OECD calculations based on data from *Eurostat's National Accounts Database* for Panel B.

StatLink http://dx.doi.org/10.1787/888933000305

Figure 2.15. **Competition distortions contribute to a heavily fragmented agricultural sector**



1. In both panels, CEEC4 is the unweighted average of Hungary and the Czech and Slovak Republics.

Source: Eurostat Farm Structure Survey 2010 (Panel A) and Eurostat Agriculture Labour Input Statistics 2012 (Panel B).

StatLink *http://dx.doi.org/10.1787/888933000324*

the same time, the share of agricultural workers in 2012 who were self-employed, 95%, was much higher than in the EA15 or the rest of CEEC4 and has been stable since 1998 (Figure 2.15, Panel B). Among comparator countries, only Slovenia displays a similar share of self-employed farm workers, albeit declining.

Some subsidies to the agricultural sector constrain an efficient consolidation of the sector and distort competition among farmers. An advantageous social security system, the KRUS, and specific tax expenditures support individual farmers. The high level of subsidy to farmers and their dependants under the KRUS weaken incentives to leave the sector, a process which may be reinforced by the support of some measures under the Common Agricultural Policy (OECD, 2008c). The significant difference in contribution rates – for pensions and social security – combined with similar benefits encourages individual workers to hold on to small plots of land to ensure eligibility for KRUS, despite their extremely low productivity (OECD, 2004 and 2006; Tompson, 2009). By contrast, farmers employing agricultural workers, co-operatives and corporate farms have to insure their workers in the state welfare system, ZUS, and pay higher contributions for their employees' pensions than those of individual farmers (European Commission, 2003). Furthermore, since 2009, the level of pension contributions of Polish individual farmers to the KRUS has been dependent on farm size, but higher contributions do not lead to higher benefits, creating further distortions between farms of different sizes.

Specific tax expenditures also slow the consolidation of the agricultural sector and reduce competition between individual farm holdings and farm companies by increasing the cost of entry. Individual farmers are exempt from personal income tax and are liable instead for an agricultural tax. The calculation of that tax depends on farm area, the type of arable land, the class and the location of the farm. However, agricultural company shareholders are taxed in the same way as non-agricultural companies. The current government had planned to harmonise farmers' social contribution and taxation on the general system (Tusk, 2012). However, implementation has so far been lagging, though small health-care contributions for KRUS beneficiaries were introduced in 2012. Indeed, health insurance for individual farmers with less than six hectares of land (around 60% of all farms) remains totally covered by the state budget.

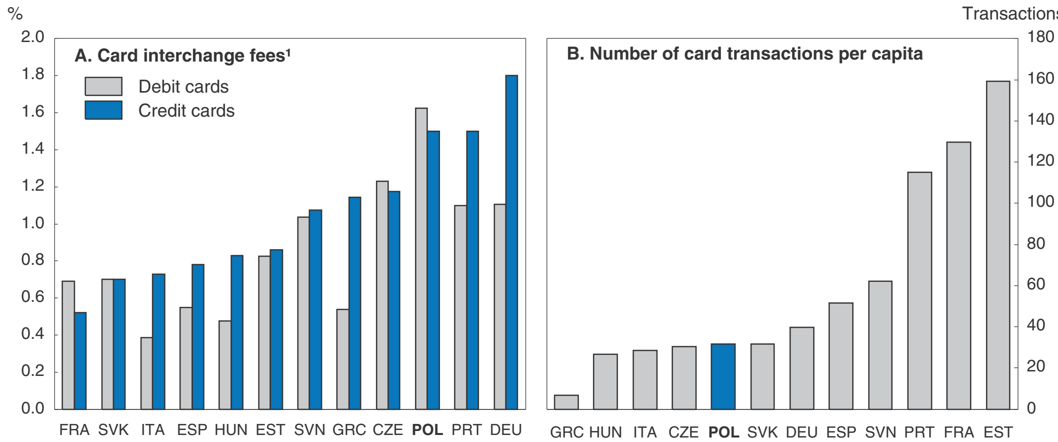
Financial services are generally competitive

Financial services seem generally competitive in Poland, and any increase in competition among financial institutions should be weighed against the increased potential risk of financial and macroeconomic instability (OECD, 2011f; Ratnovski, 2013). The Treasury continues to control the largest commercial bank and two others, representing around one fifth of the total assets of the banking sector, in addition to the state investment bank, BGK. Foreign financial institutions owned 37 banks and 19 branches of credit institutions, which together held 65% of the sector's total assets. The foreign ownership structure appears relatively diversified according to country of origin of the primary dominant entities: Italy, Germany, the Netherlands and Spain owning comparable shares. The six private banks with majority Polish ownership accounted for 6.7% and the 572 co-operative banks for 6.1% of total assets. The position of the 10 largest banks has a crucial impact on the sector as a whole – at the end of 2011 their assets accounted for 62.1% of the total banking assets, but sectoral proxies for competitive conditions, such as price-cost margins, net interest margins, and indices of concentration, generally tend to show an increasingly competitive environment (Pawlowska, 2012). The Financial Supervision Authority (KNF) supervises the banking, insurance, pension fund and securities sectors, and oversees payment institutions. It is also responsible for competition (as a means of achieving financial stability), conduct of business and development issues, while the Competition Authority is in charge of competition and consumer protection. The KNF has been praised for its governance and independence (Kowalski and Rybinski, 2011).

Though competitive pressures appear significant, state ownership may threaten competitive neutrality among financial institutions, and, given the inherently competitive nature of retail banking, the government should consider fully privatising state-owned commercial banks over the medium term. Furthermore, Polish co-operative banks, which are particularly important for the agricultural sector, appear operationally less efficient than commercial banks (IMF, 2013b). This may result from the fact that voting rules are independent of the number of shares an individual member holds, which reduces the probability of take-over of inefficient institutions. Co-operative banks may also reduce local competitive pressures in retail banking. Indeed, three elements can potentially increase their market power: i) regulations may discriminate in favour of co-operative banks; ii) network co-operation practices may restrict competition; and iii) connections with local politicians may create entry barriers (European Commission, 2007; Fonteyne, 2007). However, in the medium term competition from commercial banks is likely to increase, as they are beginning to encroach on co-operative banks' traditional small-town and rural territory.

Interbank fees for card transactions are very high in Poland, suggesting competition issues (Figure 2.16, Panel A). Indeed, the two main firms, Visa and MasterCard, control 99% of the Polish market, as in many other European countries (European Commission, 2013). The high prices caused by interchange fees are harmful to consumers, who tend to be unaware of the fees paid by merchants for such payment instruments. At the same time, a series of incentivising practices applied by providers (such as travel vouchers, bonuses, rebates, etc.) steer consumers towards the use of payment instruments generating high fees. Against this background, in 2006 the Polish Competition Authority issued a decision that agreements between banks on the level of interchange fees were in breach of

Figure 2.16. **Card fees are high by European standards, 2012**



1. Average weighted domestic interchange fees from Visa and MasterCard for consumer cards.
Source: European Commission (Panel A) and European Central Bank (Panel B).

StatLink http://dx.doi.org/10.1787/888933000343

competition law. However, the case is still in the courts. More recently, the Parliament decided to cap interchange fees at 0.5% of the transactions from July 2014. Polish regulations would interact with the recent European proposals, which would introduce a ceiling of 0.2% for debit card rates and 0.3% for credit cards on interchange fees (European Commission, 2013). Such a reduction in card fees is likely to lead to a higher acceptance and usage of cards in Poland (Panel B).

Recommendations for invigorating product market competition

Barriers to entrepreneurship and state ownership

- Lower further the costs of entry and exit, such as red tape. Reduce the length and costs of bankruptcy procedures.
- Pursue privatisation, and substantially reduce government ownership in competitive segments of the economy while ensuring sound governance of remaining state-owned enterprises. At a minimum, regulations and implicit subsidies distorting competition between public and private firms should be removed.

Competition law and policy

- Introduce fixed-term non-renewable mandates for the President of the Competition Authority and all sectoral regulators, during which they cannot be dismissed without fault, and prevent revolving-door opportunities.
- Give the Competition Authority more power including to split up companies so as to reduce dominant market positions and impose vertical separation as a remedy for third-party access problems in network industries.
- Accelerate the functioning of the judicial system to shorten the time between the Competition Authority's decisions and a final court decision in antitrust cases by, for example, developing the use of information and communication technologies.

Recommendations for invigorating product market competition *(cont.)*

- Modify public procurement practices to select contractors offering the best value for money rather than the lowest prices. Focus procurement decisions on a mix of prices and technical bid details. This will require enhancing staff skills to deal with complex selection criteria.
- Make the judicial environment friendlier to class actions in cases of competition breaches.

Regulatory policies in network industries

- Reduce further public ownership in competitive segments of the energy and water sectors.
- Create an independent sector regulator for water and sanitation services.
- Increase competition in rail transportation. Insure total independence of the main public infrastructure manager from the operators. Reduce anti-competitive pressures resulting from the participation of Polish Airports State Enterprise (PPL) in many airport entities, and consider long-term concession agreements or privatisation for airport entities. Privatise the national air carrier (LOT).

Regulatory policies in competitive industries

- Fully implement the second and third stages of the liberalisation of professional services.
- Substantially reduce the current level of government subsidies to individual farmers compared to farm companies. Progressively align farmers' social security contributions and personal income tax on the general system.
- Set a cap on interbank fees for credit card transactions to reduce the effects of market concentration in line with the 2013 EU proposal.

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