

### 3.5 Privatisation of municipal services, outsourcing and in-sourcing efforts and their employment impacts in the European Union countries and Hungary\*

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In December 2012 some unusual news appeared in daily newspapers regarding a “strike” at the public transportation company of a Hungarian town. At dawn on a Monday morning one third of the bus drivers refused to start work, therefore many bus lines were not operating during the morning peak hours. The director of the company alluded to a coup attempt, suggesting that although bus drivers were citing the technical condition of buses, their refusing to work was in fact due to their wage claims. The trade union leader’s statement, of course, immediately rebutted this assumption. By the end of January 2013, the news reported that the trade union leader, who had long been protesting because of the condition of the buses, was laid off, the company justifying it through a loss of trust. The trade union took legal action against the unlawful dismissal. A report in mid-February 2013 revealed that a police investigation was underway for “disturbing the operation of works of public interest”. In his statement the town’s mayor promised full support to the company director who had gone to the police, calling it unacceptable that the town’s life should be paralyzed by a wildcat strike that no one could prepare for.<sup>1</sup>

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1 The news reports appeared in the local media, national newspapers and at the Hungarian News Agency. Unfortunately we have to omit the exact references and verbatim quotations for the sake of anonymity which we must ensure for every interviewee who participated in the research.

2 The research project “Public sector pay and social dialogue during the fiscal crisis” covered five countries (France, Germany, Hungary, Sweden and the United Kingdom) and was funded by the European Commission (VS/2011/0141), Research coordinator: Damian Grimshaw, Manchester Business School (Grimshaw, Rubery and Mariano, 2012). This chapter builds greatly on the results of the research gained both in Hungary and internationally.

The case gained nationwide publicity and exposes, to some extent, a field of industrial relations which has so far received little attention in studies: the specificities of the municipality-owned enterprises sector. Coincidentally, half a year before the above-mentioned case we had actually conducted interviews at the company in question in the framework of an international research project<sup>2</sup> and could not detect any signs of the coming conflict. Therefore we will return to the case at the end of the present sub-chapter and attempt to give an explanation as to the developments that ensued in the meantime.

The original field research, conducted in the framework of an international research project, took place in two country towns that provide a wide range of public services, involving the private sector and church institutions in different ways (Berki *et al.*, 2012). The two towns, differing in size, were indebted to different degrees and party politics appeared differently in their lives. In both towns we conducted interviews with the heads of the municipality and its institutions/companies, as well as interest representation organisations – wherever they existed. In both places we focused on five service areas: public transportation, geriatric care, provision of school meals, cleaning and waste management. Hereby we would like to thank our interviewees for their cooperation.

In line with the practice of New Public Management (NPM), described in Chapter 3.3 of the current volume, an increasing part of municipal public services are provided – in various structures – by private or non-profit organisations, and the disintegration of sharp divisions between sectors can be seen. The first part of the sub-chapter provides a brief overview of the motives behind outsourcing and in-sourcing, (public) procurement, its prevalence and regulation, as well as its impact on the labour market in some of the EU member states. The second part attempts to map the relevant Hungarian experience – the starting point being the specificities of management, service provision and interest reconciliation in the Hungarian municipal system –, giving a description of interests and counter-interests that are behind organisational changes. Finally, we will take two case studies to illustrate the employment impact of outsourcing and re-municipalisation, as well as the involvement of the church in service provision. Our article focuses mainly on labour market segmentation and the transition between various employment statuses, so many other parts of the topic will have to be covered in outline only.

### **Municipalities' crisis reactions and outsourcing in some EU member states**

a) *The impact of austerity measures at the level of municipalities.* An ILO study (Vaughan-Whitehead, 2012) exploring European crisis reactions, and more closely the adjustment of the public sector, between 2008–2010, distinguishes between quantitative measures (redundancies, wage freeze and wage cuts) and structural reforms. Differences among countries in this respect are significant: while in Greece or Portugal it was necessary to significantly reduce the size of the public sector, other countries – such as the UK or the Netherlands – chose a combination of two adjustment approaches: in the case of some public services the responsibility of provision was decentralized and delegated to the municipalities. In many countries the direction of structural changes was privatisation, outsourcing, purchasing services from the private sector – that is processes that began with the New Public Management (NPM) (see sub-chapter 3.3) have been bolstered. According to OECD data, calculated on the basis of the national accounts, the total volume of buying services from the private sector between 2007 and 2010 increased on average from 12% of the GDP to 13%. In Holland, Finland and Canada particularly significant increases were registered. Hungarian figures are close to the average but show an approximately 1% decrease (OECD, 2013).

Research on the reactions to the crisis focused initially on national responses (see sub-chapter 3.4) and only the most recent studies have come to study the level of municipalities. This is despite the fact that a considerable element of public services are provided in the framework of municipalities, therefore budgetary constraints introduced after the onset of the crisis appeared most-

ly at this level. Our topic requires that we address the economic autonomy of municipalities and local systems of wage agreements and interest reconciliation channels (*Leisink et al.*, 2013). While the wide range of municipal services is very similar in different countries, there are significant differences as to the division of labour among governmental levels and the financial approaches applied; therefore there are considerable differences with respect to the financial autonomy of local governments. OECD data show that the proportion of transfers from the central budget (subsidies, shared taxes, etc.) is high in the United Kingdom (70%) and in Hungary (59%); it is smaller in France (29%), in Germany (18% in the constituent states and 35% at the level of municipalities) and Sweden (24%).<sup>3</sup> The order of course is reversed when looking at the proportion of local taxes and other revenues.

Depending on their fiscal autonomy, local governments can decide about how to react to the austerity measures introduced by the central government. They may choose to reform the local tax system, shrink the range of services they provide, or – under some circumstances – it can be the opposite: they may be prompted to experiment with a “countercyclical policy”, to ameliorate the impacts of the economic crisis by increasing wages or concluding outsourcing contracts on better terms, etc. – thus endangering the implementation of the central government’s budgetary goals. In the absence of autonomy, however, municipalities may be instructed or impelled – by changing political and economic conditions – to curb their services, investments, employment level and, if possible, increase taxes. Such reforms may be followed by what is called the vision of the “Big Society” (UK), which encourages citizens’ self-reliance, volunteer activities and the involvement of not-for-profit organisations (*Bach*, 2012). In welfare states settlements with a greater proportion of low-paid or unemployed inhabitants are more affected by subsidy cuts, as they are more dependent on targeted subsidies for the disadvantaged sections of the population. In the United Kingdom these include a large part of centrally provided subsidies, which the current administration decreased by 25% on average, while in the poorest locations central support dropped by 72% (*Grimshaw, Rubery and Mariano*, 2012). If the central government cuts support for local governments, while also delegating to them the responsibility for service provision, there will be strong pressure at the local level to organise services more efficiently.

All this must have an impact on the employment of those providing public services locally. In their paper *Leisink et al.* (2013) sum up the conclusions of another international research project, where case studies were conducted in three countries (Italy, the Netherlands, United Kingdom), describing two municipalities in each country, exploring industrial relations at municipal level in the wake of the crisis and examining if they are similar or different in the case of the municipalities studied. When austerity measures reach the level of mu-

<sup>3</sup> 2011 data, source: [OECD Fiscal Decentralization Database](#), Table 17.

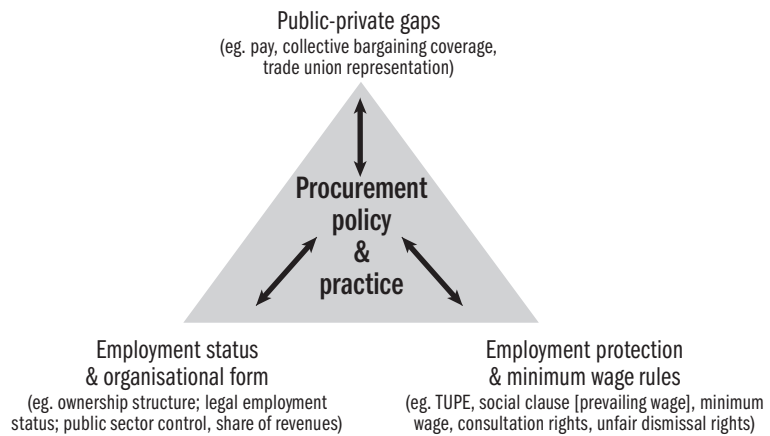
municipalities then interest reconciliation channels prove to be an important factor: whether there is a sectoral or local forum of social dialogue, whether trade unions are strong or not, and the level of institutionalization, all play a role.

From this point of view institutions in Italy and the Netherlands are strong, whereas in the UK they do not really have a place in the liberal economic model. Despite the traditional dual-level collective bargaining, municipalities in Italy, for instance overrode the central government's unilateral decision on a wage freeze, while in the Netherlands interest representation bodies of local governments drew on a 1994 law to retain their entitlement to conclude collective agreements in the face of pressure from the central government to implement a wage freeze. In the United Kingdom, however, municipalities were able to exempt themselves from the scope of national wage bargaining – in the few areas, that is, where they had such a role. Thus in the Netherlands and the UK municipalities and trade unions had a legitimate scope of action against the central will, while in Italy the unilateral government decision on wages allowed no such opportunity. In the latter case, however, municipalities' financial potentials were decisive and the fairly wealthy local governments negotiated employment terms without formal authorization as well. So despite the fact that fiscal constraints in the three countries prompted municipalities to act, the implementation of restrictions at the local level was determined by national intermediary institutions and the structure of the local government – thanks in main to their autonomy *vis-à-vis* the central government and the institutions of social dialogue. Thus local governments and employee representation bodies had some freedom in deciding how to react to the central austerity measures. There were, however, significant differences within the countries, and therefore the differences despite a similar institutional set-up suggest that the strategies and decisions of local actors also had an impact.

b) *Decisions on outsourcing, labour market regulation and the role of interest representation.* The extensive body of literature on privatisation and outsourcing decisions generally emphasizes two main labour market factors: the public sector's wage advantage over the private sector and the different influence in interest representation (works council entitlements or the trade unions' bargaining power). The latter is usually weaker in the private sector, which is evidenced by the rough indicator of trade union density. The wage advantage of the public sector is typically considerable in the Anglo-Saxon countries, therefore in these countries there is a possibility to decrease costs by restraining wages; no wonder this approach was mostly emphasized in the Anglo-Saxon studies. Large wage gaps provide a strong impetus for outsourcing low-wage jobs, especially in times of austerity. Obviously, wherever wage differences are smaller or of the opposite direction, then it can hardly be the main motivating factor.

*Grimshaw, Rubery and Mariano (2012)* suggest that beside wage differences and the strength of interest representation, a third factor also plays an important role the different levels of legal protection of employees in the two sectors, whether it concerns the status of civil servants or other public sector employment statuses (non-civil servant). The difference in employees' legal protection within the public sector manifests itself in labour market segmentation as well: in differences concerning employees' remuneration, access to promotions and job security. These three factors of course carry different weight from country to country when it comes to decisions about outsourcing (see: *Figure 3.5.1*).

**Figure 3.5.1: Procurement policy and the labour market**



Source: *Grimshaw, Rubery and Mariano (2012)*.

Decision-making is further complicated by two additional factors. On the one hand service provision often does not take place in pure community or private frameworks but in a varied combination of ownership structures: there may be countless variations for this from 100% privately owned, profit-oriented companies to 100% publicly owned, not-for-profit enterprises.<sup>4</sup>

On the other hand, beside the consequential external and internal labour market segregations, other aspects are taken into account when considering outsourcing. These may include regulations about the transition, most prominently the regulations concerning transfer of undertakings and wages following the outsourcing (for more details see later). These regulations differ from country to country and if they prove effective, then they make the transition to outsourcing a smoother process and alleviate the impact of the consequential labour market segmentation. Decisions about outsourcing seek to be sensitive to the specificities of the service concerned, while reacting sensitively to financial constraints and the legal regulations related to (public) procurement. The choice of organisational form is influenced by the

4 In an extreme case, for instance, the municipality contracts the self-employed, keeping its *de facto* control over service providers. It is a typical decision in many countries to use an enterprise with the municipality having majority ownership, thus retaining control over the operation, which may also be a source of income and may provide the opportunity to circumvent the headcount limitation in the public sector, while applying employment regulations valid for the private sector.

VAT regulations as well. In Germany, for example, VAT is applicable where the local government is participating in service provision, which is a way to encourage decisions towards favouring the private sector. At the same time acquiring investment sources is another important incentive for outsourcing, while the establishment of municipal enterprises is justified by the revenues generated by the sale of shares, which is a way to decrease debts.

In France there is some pressure to in-source, which is, in all likelihood, due to the disappointment at the obscure, uncontrollably complicated organisational structure and the great costs and low quality of previously outsourced services. The decision to outsource/contract a private provider thus – according to the literature – is the result of decisions made on the basis of various viewpoints, and not only a reaction to price signals.

Outsourcing decisions are by no means exempt from ideological aspects – political motives play a role too. In the United Kingdom it is essentially up to the municipalities to decide how they cope with the cuts in subsidies from the central budget, while they have to retain the responsibility of service provision. In connection with geriatric care, for instance, they often had to cut the fees of outsourced services, laid down in the contracts, meaning they had no choice but to economize at the cost of service quality. On top of that, the current government is encouraging outsourcing by financial means as well, as local governments may apply for funding if they involve the private sector. Therefore every new school is built in such a setting without any real supervision of municipalities. Joint financial structures of the public and private sectors are encouraged in the entire municipal sector, not least for the purpose of decreasing the amount of recorded debts within local governments and the employment level in the public sector.

*c) Interaction between regulation and outsourcing practices.* The appearance of private sector actors in the provision of public services raises the question of interaction between different labour market regimes, including the nature of labour market segmentation and the possibility of a regulation to prevent the emergence of considerable differences between the two sectors. A general presumption is that employees working in jobs outsourced to the private sector receive lower wages, their promotions lack predictability, and they are more exposed to changes in market demand, therefore additionally making their jobs more at risk. This logically follows from the fact that the goal of outsourcing is to ensure more efficient work for lower pay and/or more flexible working conditions. Experience shows, however, that this is not always the case. Our first counter-example is not about outsourcing to the private sector, it is only about organisational decentralization. During the reforms of the 2000's in France, as many as 128,000 employees (mainly primary school teachers) were transferred to the municipalities. Most of them accepted this move voluntar-

ily in the hope of better payment conditions, as the municipalities' scope for action was greater despite the fact that salaries – as determined by the civil servants' pay scale – were lower than those set in the central pay scales.

It is also an experience in France that in-sourced employees usually lose their benefits in-kind that they are entitled to in the private sector, such as the supplementary health insurance, and those other benefits that the works council at the private enterprise have achieved. Having returned to the public sector, they constantly suffer disadvantages compared to those employees with long-term employment in public service. Although their salaries are unchanged following their transfer later on they are excluded from seniority-based pay rises because their years spent in the private sectors are only partially taken into consideration. All this explain why employees and their trade unions are reluctant to support in-sourcing. An in-depth study revealed that interest representation bodies always consider the conditions of the concrete transition and its expected outcome when deciding whether to support or oppose the proposed changes (*Audier et al.*, 2012).

The study conducted by *Grimshaw et al.* found that of the four Western European countries there are only two where the outsourced private sector offers lower wages: Germany and the United Kingdom. In Germany, however, this difference is decreasing following the introduction of a new lower tariff category (see later) in the public sector and the minimum wage in certain services, while in the UK the collective agreement concluded with the local governments may improve the situation. In France the situation is similar, although the private sector allows longer working hours and greater work intensity, while in Sweden the collective agreement is applicable in each sector. Trade union reactions to outsourcing correspond to wage considerations. There is no resistance in France and Sweden, but there is general opposition from the trade unions in Germany (because of worse working conditions and because there are no guarantees warranting the application of the collective agreement) and in the United Kingdom (due to less favourable working conditions and the loss of pension entitlement).

The transition is tempered by the regulation of the relevant public service act, insofar as it may maintain status change over time, for instance by applying the more flexible conditions of the private sector to the new employees only. This is what happened in Germany, where in the 1990s the transfer of employees with a civil servant status led to complicated legal problems because they sought to both keep their special legal position and also facilitate the application of the wage setting mechanisms and working conditions of the private sector. Similarly, in France, when state-owned companies were privatized – e.g. in telecommunications and the electricity industry – employees who had already been employed were able to keep their status based on a separate law and the conditions pertaining to the private sector only applied to newcomers.

Transition between the two sectors, and competition among labour regimes may be moderated by more general regulations as well: a relatively high minimum wage, the rules concerning the transfer of undertakings, the law on the prevailing wage, the extension of collective agreements and social clauses added to the outsourcing contract – the practices differ from country to country (*Schulten and Brandt, 2012*). A high national minimum wage may imply a lower limit in the wage competition (especially in those countries and sectors, where the proportion of low-paid employees is relatively high). The connection between the minimum wage and the wage regulations in the public sector is also interesting, especially when the minimum wage catches up with the lower wage categories of the public sector pay scale as a result of the faster rise of the former.

Of course the reforms of the public sector may result in a decreasing difference between the two sectors if pay and employment are made more flexible. There are reforms with the opposite intentions as well, such as the overhauling of the tariff agreements in the public sector in Germany in 2005, when a new, lower wage category was introduced for “extremely simple activities” (*einfachste Tätigkeiten*) that in Hungary would be called unskilled labour requiring no qualifications. The new tariff was introduced explicitly to ensure that wage differences do not necessarily lead to outsourcing. Its reception was quite controversial even in trade union circles (as the goal of job protection clashed with the principle of fair wages) and there is no convincing evidence that it successfully prevented outsourcing (*Bosch et al., 2012*). Examples of more successful interest representation are connected mainly to consultations preceding concrete decisions of outsourcing or in-sourcing. In France it was trade unions, while in Germany the works council, that were able to intervene proactively, partly using formal channels (e.g. at local governments’ committee meetings preparing economic decisions, where they are regularly heard) or through informal ones (that is, through their political channels) (*Grimshaw, Rubery and Mariano, 2012*).

Transfer of Undertakings (Protection of Employment) – “a change in the person of the employer”, as the new Hungarian Labour Code terms it – have been regulated by EU’s TUPE directives since 1977; however, there are great differences between countries as to their interpretation and the protection they ensure. For instance some countries allow employees to “refuse” “automatic” continuation of the employment relationship at the new company, in which case the rules that apply are those related to the termination by the employer. In the United Kingdom, for instance, the application of the directive ensures only a relatively small degree of protection. Although the government has included in the regulation the right “to refuse” it did so in a way that there would be practically no legal consequences if those rights were to be infringed (*Hartzen et al., 2008*, citation by *Grimshaw, Rubery and*



*Mariano*, 2012, p. 70). Refusal practically entails resignation but it does not entitle employees to any kind of compensation, there is no protection against an unlawful procedure. (The Hungarian regulations in the market sector are basically on these lines.) In these countries there is no guarantee for the long-term maintenance of employment, while elsewhere the successor (transferee) employer is obliged to maintain employment for a certain period of time: for 15 months in France and 12 months in Germany and Sweden.

The application of social (employment) clauses stipulating equal treatment in the context of outsourcing contracts was introduced by a 1949 ILO convention.<sup>5</sup> The ruling of the European Court of Justice on the *Rüffert case* in 2008 concluded that the employment clauses in contracts with private enterprises restrict competition, which practically determines the European Commission's stand as well.

The practice of the extension of collective agreements including wage tariffs also differs from country to country. Nowadays they are widely applied in the German constituent states. In North Rhine-Westphalia – where case studies for the research were conducted – the first law regulating wages in the course of outsourcing was passed in 2002 (*Schulten et al.*, 2012).<sup>6</sup> They were later abolished after the governmental change in 2006 – when the red-green alliance was replaced by the CDU/FDP. The new government argued that they did not fulfil their goals effectively enough. In 2008, a law in Lower Saxony, similar to the above-mentioned Rüffert decision, led to the reappraisal of contractual clauses on wages. However, in 2010–2011 a new wave of legislation on “prevailing” wages (*Tariftreugesetz*) swept through the constituent states, which complied with the requirements of the European Court of Justice. Their essence is that during outsourcing entrepreneurs in the private sector should comply with wage tariffs included in collective agreements, provided the agreement has been extended to the entire sector.

In the United Kingdom, however, there are examples of the voluntarily application of the standards common in the public sector, when – at the initiative of local governments and trade unions – certain employers apply the wages common in the public sector without any legal or contractual pressure. An example for such an initiative is the so-called living wage in London, which tracks living costs that are far above the average, its main supporter being the city's mayor (*Grimshaw, Rubery and Mariano*, 2012).

5 Convention No. 94 – Hungary did not ratify this convention.

6 At this point about half of the German constituent states applied similar laws, mainly for construction works and in public transportation, but their scope was extended to other services as well.

### **Outsourcing and in-sourcing of municipal services in Hungary**

a) *Local governments' system and economic management.* In the West European countries rather different local government systems have been evolved, depending on the size of the country, the local traditions and the level of economic development. Despite recent convergence in the level of economic development and of cohesion efforts of the EU, there have remained sub-

stantial differences in terms of the number of local governments, autonomy of municipalities and the division of tasks between various governance levels. We cannot enter into a detailed discussion due to limited space, and the following presentation of features of the Hungarian local government system will also necessarily remain sketchy. The principle “one settlement–one local administration” became established in Hungary in the 1990s. The Local Government Act assigns the responsibility of provision of a wide spectrum of mandatory services (public education, health care and social welfare services, maintenance of the local infrastructure, environmental protection, social housing, fire services, public safety, etc.) to local governments – regardless of their largely varying size in terms of population and economic power. At the same time they are given a free hand to determine the organizational framework of service provision and how to spend their own revenue. The “Hungarian model” resembles the Mediterranean one with respect to its fragmented nature, and is similar to the Scandinavian system in terms of the wide range of local government functions (*Vigvári*, 2011).

Despite the existing legal framework providing for strong decentralization, centralization occurred from the early 1990s, mainly as a result of fiscal incentives. Local administrations’ own revenues are generally modest, primarily based on revenues from property sales, local business tax and top-down income tax distributions, a system which has generated considerable financial disparity among local administrations. This has led to the state periodically intervening to provide uniform per capita support for mandatory services, development subsidies and by reorganizing the tax system. In order to guarantee their continuing functioning, local administrations that are “in a disadvantaged situation through no fault of their own” – are entitled to supplementary state support. According to OECD statistics, government transfers accounted for a relatively high share, 59 per cent, of local government expenditure in Hungary in 2011. Due to the decrease in state subsidies, EU tenders emerged as the sole source of funds to finance development works.<sup>7</sup>

State subventions for local government functions have been continuously decreasing since 1995. On joining the EU, the state undertook the obligation of observing budgetary discipline, based on the Maastricht criteria. Thus the 2006 convergence programme brought about a new phase in budget cuts in the local government system. The brunt of stabilization costs was borne by local government. Direct cutbacks in the municipal subventions are estimated to have improved the balance by 0.7% of the GDP (*Vigvári*, 2011). In addition, cutbacks in the healthcare and other sectors affected local governments’ ability to maintain their institutions, from hospitals to fire brigades. (Then local government expenses made up 11% of the GDP.) Cuts in subsidies provided from the central budget for mandatory functions did not necessarily take the form of limiting the wage bill paid to local government employ-

<sup>7</sup> The importance of EU grants is indicated by the fact that their winning prompts an opportunistic approach; as one interviewee, a mayor, put it, before they sought grant opportunities for what the community needed, today they would apply to any open call for proposals, like for building a football pitch, as is the case now: “if the prime minister is mad about football, ... then we will build a football pitch next to the pool, we will join the crowd. What we build stays here and adds to the town’s assets.”

ees. Unfortunately, no statistics are available concerning the extent of budget cuts for an unchanged, comparable set of mandatory services. According to a study conducted by the State Audit Office, between 2007–2010 in the cities of county status, cuts varied in different services (1% in child welfare, 6% in primary schools, 16% in school dormitories). In this period the lack of resources which emerged was compensated for by institutions' own revenues and increasing local government support (*ASZ*, 2011).

Municipalities reacted to government austerity measures by raising considerable external funds, predominantly by issuing bonds denominated in foreign currencies. Even the credit limit stipulated in the Local Government Act was not enough to close the loopholes that used various “financial innovations”. The financial crisis triggered a major increase in interest payments, accompanied by dwindling local tax income and increasing claims for social assistance due to the economic crises. There were substantial differences among municipalities as to the level of their indebtedness, and in some towns bankruptcy was an everyday threat by 2012. With the decrease in revenues, local governments had to adopt a new approach towards private enterprises – in some settlements this meant a withdrawal of benefits (for instance, tax-exempt status) provided for them earlier. Others opted for a strategy of not only maintaining the level of levies imposed on enterprises but also made efforts to retain their presence by easing their situation, hoping that they would expand their operation after the crisis and that tolerance on the part of the local government would pay off later in employment creation and the increase in local business tax.)

With the majority of mayors affiliated to the governing party, local government indebtedness became a political issue. In October 2012 the Prime Minister announced a fiscal consolidation programme for municipalities, under which the state budget would take over the debts of small municipalities (under 5000 inhabitants, i.e. a total of 1700 villages), and on average 40 per cent of the debts of larger ones. However, in practice the government negotiated conditions town by town in 2013, with the process lacking in transparency and strongly influenced by party politics.

Although the law defines the minimum standards of services, the government itself sought to narrow the extent of certain service provisions in response to the crisis, The Law on Social Care assigns the duty of providing care for the elderly to local government. Paradoxically, however, municipalities can freely decide as to the scope of beneficiaries, as well as on the quality of services provided and also regarding the extent of co-payment. In 2009, however, a ministerial decree ordered that entry to residential care facilities, run by the state (local government), ought to be subject to a doctor verifying the need for care of a minimum of four hours per day in the case of each person. Although the number of beneficiaries did not decrease in residential care

facilities (KSH, 2011). According to our case studies however, it resulted in a dramatic increase in the proportion of in-patients with dementia, whose care implies a far greater workload and is subject to specific standards.

The government in power has taken a number of steps promoting the centralization of public administration and institutions providing public services. As of 2013, local governments' public administration functions have been transferred to government agencies, either at central government level or at district (micro-regional) level. This process began in the health care sector, affecting hospitals belonging to small municipalities. From January 2013 a large share of public education was transferred to state management, meaning that all teachers are now employed by a single government agency. School facility management has however mostly remained with the local administrations. Parallel to centralization the current government is facilitating the transfer of certain services (education, health care and social care) to church-based institutions by providing these with higher per capita subsidies compared to those run by municipalities. The current wave of public service centralization and their transfer to church-based institutions is motivated more by ideological and political considerations than based on evidence or on negotiations with key stakeholders.

b) *Interest reconciliation and employment policy in local government.* Either directly or indirectly (through their institutions and business companies) the municipalities employ about half of the public sector employees in Hungary. Despite local governments' budgetary autonomy, the base salary of public sector employees and civil servants is defined according to the pay scales specified in the relevant laws. As we have shown in sub-chapter 3.2, in national level interest reconciliation related to legislation and government policies local government alliances also take part, in their capacity as employers, besides trade union confederations. (Pluralism prevails here as well, as there are three such organisations.)

Employees of municipal companies are subject to the Labour Code (which applies to the genuine private sector, too) and the mandatory minimum wage that implies there is no tariff system to apply to their wages. Sectoral level interest reconciliation takes place at the Subsectoral Social Dialogue Committee on Communal Services. The Committee has no direct influence over wages; its members did not conclude a sectoral collective agreement. As to the typical remuneration practice of local government organisations, a recently conducted survey found that although a large proportion, 84%, of local government organisations carry out performance evaluation, only at 17% of them did the results influence annual pay (Bordás, 2012).

In the local government sector collective agreements are concluded only at company level. On the employer side, the agreement is signed by the com-

pany's management. Although the lack of management autonomy is a common barrier to collective wage bargaining in the entire public sector, this is particularly the case in certain municipal companies. According to the head of the sectoral trade union, local governments, as owners, are not represented at the bargaining table, and the management does not have the necessary authorization. Moreover, the management is often unable to meet its legal obligation to provide information because the local government as owner disallows it. As a consequence, there is no consultation on important or strategic decisions of the owner. The competence of the local company's management to enter into negotiation is further curbed by the practice that larger towns set up a holding-organisation over their municipal companies, which determines company managers' scope for action and centralizes resources.

As a result, trade unions in the municipalities do their best to negotiate directly with the owner, i.e. the local administration. In larger towns there is an interest reconciliation forum where trade unions can have direct negotiations with the local administration's chief officials. For instance, the Budapest Public Service Consultative Forum has been in existence since 1993, with the vice-mayor consulting with trade unions on such topics as restructuring. Although, legally speaking, this is not collective bargaining, each year they develop guidelines acting as recommendations for local wage agreements. It seems that a prerequisite to operating such a forum is to have a large number of institutions and companies, as well as well-organized trade unions. One of our case studies also shows that in a small town, however, there was no evidence of any collective bargaining, and wages in the public service companies were low, corresponding to conditions on the local labour market. According to our interview data, everyone is paid "on the minimum wage". This means that employees receive the lowest level of remuneration allowed by the law. Two organisations had previously had collective agreements (in a vocational secondary school and at the local hospital). However, subsequently, both organisations were integrated with a third that is non-union and as a result their collective agreements will become void 12 months after the merger. In any event, the collective agreement at the hospital included no provisions on wages and benefits. Because employees of local government organisations and local government-owned companies practically have no interest representation whatsoever, there is an absence of collective wage bargaining that could influence employment conditions and remuneration practices. (*Berki et al., 2012.*) All in all, municipal-level social dialogue remains immature in Hungary.

c) *Local government policies of outsourcing and re-municipalisation.* The Local Government Act and other sectoral laws specify the services that local governments, depending on the settlement's population size, are obliged to provide. Additionally, the municipalities may undertake other services on a voluntary

basis. As we have seen, local governments are free to decide how service provision will be organised. A traditional arrangement is for local governments to maintain institutions with public service employees providing services. In such institutions the administration of finances is carried out in line with the – rather rigid – protocol, customary in budgetary institutions. According to this arrangement, the maintainer (i.e. the local government) may determine, beyond the institutions' budget, the number of employees and also the wage costs. The other arrangement implies that the local government outsources some public services, which might take the following forms:

- The municipality establishes and operates a business company. It does not necessarily need to maintain 100 per cent ownership, and may sell some of its shares or involve an external investor. This was the most common form of the privatization of public utilities in the 1990s.
- The municipality runs a public procurement procedure to select an enterprise for providing the service or offering it a concession.
- The municipality concludes an agreement, generally with civil organizations or churches, for providing the mandatory tasks.
- It forms a consortium with other local administrations to provide the public service using any of the above three approaches.

In each of the above-mentioned outsourcing forms, the municipality signs an agreement with the selected enterprise/non-profit organisation. Nevertheless, the local government bears a secondary liability for ensuring the uninterrupted delivery of public services; if the contracted enterprise is unable to provide an adequate level of service, then the municipality has to take back the responsibility of provision. Depending on the contract and the legal provisions, for services the local government continues to have the competence to determine service fees (e.g. water bill, public transportation fees) (*Dicső*, 2010, *Horváth et al*, 2002).

According to a survey conducted in 2011, 55% of local governments have shares in business associations and in 28% of such associations local governments have controlling stakes (*Bordás*, 2012). Privatisation of local government operated corporations, and involving external investors, became a major trend in the mid-1990s. The reasons behind privatisation of local government businesses were the same as that of state enterprises: intention to modernize financially weak corporations that had partially lost their markets, with the involvement of foreign technology and expertise in marketing and management. On the other hand, the budget revenue generated by privatisation was equally important for an indebted municipality. However, municipality level privatisation was even less transparent than that of state corporations; instead of the central State Property Agency, decisions were made by the elected general assemblies. A great deal of publicity was given to contracts that had been scandalous in being greatly disadvantageous for the local community.<sup>8</sup>

<sup>8</sup> A study, prepared on the basis of a research by the State Audit Office on corruption, also uses the conditional tenses when discussing this issue: "Ownership in a business association is, among others, a risk factor from the point of view corruption because the motivation behind owners' decisions is not necessarily to serve public interest, and there are no legislative or other kind of controls. In the case of privatisation, it would require an extensive study on efficiency and cost-effectiveness to decide whether an enterprise, selected to run a public utility service, is any better at it – or put otherwise, if privatisation serves the public interest or not –, and to answer the question whether they were undersold." (*Bordás*, 2011.)

Outsourcing certain auxiliary activities (cleaning, security and maintenance services, etc.) has for decades been a common practice at state and local government institutions. As of 2004, however, service providers, or the beneficiary of a concession, have to be selected through a procurement process. The motives behind local governments' outsourcing decisions are not sufficiently well known, however, and public statements rely on the same rhetoric as in the privatisation (increasing efficiency, bringing in special tools and knowledge, etc.). It is probable that the attempt to evade regulations on headcount may have been a more important factor here than in the private sector, although this is more likely to hold true for centrally managed institutions than for local governments which have more flexible financial administration. According to the above-referred survey from 2011, 31.7% of local governments outsource services; 25.1% of the outsourced services pertain to mandatory services of municipalities, 9.6% to specialized tasks, while 65% are linked to voluntarily undertaken functions of municipalities. As much as 37.9% of local governments have long-term cooperation agreements with civil organisations, although it is unknown what proportion of these covers the outsourcing of public services (Bordás, 2011).

The present government – referring in part to some well-known examples of privatization debacles – has been pursuing a policy of re-nationalization. Local politicians are also keen to regain full control over service providers and follow a re-municipalisation policy. Service-providing enterprises and beneficiaries of concessions constitute a different story: the government's approach in these cases is to renegotiate the contracts, i.e. not necessarily to nationalize them but instead starting a new procurement process and possibly replacing former providers. The emphasis here is on providing opportunities for Hungarian rather than foreign companies. Such attempts have however engendered scandals, such as when the new beneficiary turned out to be an entrepreneur from the clientele of the party in power, or a family member or friend of a well-known politician of the ruling party. Our case studies confirmed that such “political advantages” are prevalent among the motives of local decision-makers and similarly influence outsourcing or the redistribution of profitable businesses in line with a partisan-clientele rationale.

d) *Impact of outsourcing and in-sourcing on employment and wages.* Probably our most interesting research question was connected to transitions (privatisation, outsourcing, in-sourcing) between various service providers. We tried to reveal the motives of related decision making as well as the consequences, namely their influences on employment and wages.

Whether it is a private company, a church or other non-profit organisation that takes over service provision from the local government, employees' legal status will change regardless of the new provider: instead of the Act on the

Legal Status of Public Service Employees, they will be subject to the Labour Code following the transfer.<sup>9</sup> In the event that public sector employees refuse to accept a position offered to them, they receive a lower amount of severance pay than they would otherwise be entitled to.<sup>10</sup> Given that Hungarian law is in compliance with the TUPE Directive, dismissals cannot be effected at the moment of transition. However, as in many other EU member states there is a possibility to do that before and after. In our case studies we have come across restructuring, implying lay-offs of moderate scale, and the narrowing of the scope of services. In the case of institutional transferrals to church institutions, looking to the higher per capita subsidy for which they are eligible, there is no point in narrowing the scope of service, at least as long as the relevant law is in effect, although the issue of rationalizing operations is raised because of efforts at cutting costs. In the same manner, management is more rationalized in the case of services provided by the private sector than by state institutions. All in all, however, our case-study data suggest that the stability of employment has been retained despite the transfer. Moreover, in some cases some improvement in employment security has been noted, compared to the precarious situation which existed before.

In general – and particularly after the relevant changes in legislation effected in 2012 – the Labour Code implies far less constraints for the employer than the Act regulating the employment of public service employees, especially when it comes to pay: instead of applying mandatory wage tariffs, only the two-level statutory national minimum wage system must be observed.

With respect to wage levels and wage bargaining after outsourcing, the case studies allow only limited conclusions. Outsourcing and the subsequent remunicipalisation of public utility services in the bigger town in our scrutiny, where trade unions have a strong bargaining position, had practically no impact on the advantageous position of employees. Interestingly enough, in this town the geriatric care organization acquired by the church made no changes to pay conditions. As the new provider, the church was in a position to do so without any risk in the short term, since the majority of employees were paid the minimum wage anyhow and a large state subsidy covered additional costs. It is telling, however, that the new collective agreement for this particular organization does not set base wages or benefits. Therefore it is possible that in the longer run it will be easier to deviate from the wage scale. Moreover it also indicates that the employer does not foresee any wage bargaining taking place.

In the other small town investigated, wages in the local government sector are low, irrespective of whether the service is run by the municipality or a private company. Although drivers working at the bus company, operated by a private entrepreneur, earn somewhat more than the minimum wage their salaries are precisely half of that which bus drivers in the other bigger town receive, not to mention the difference in fringe benefits. (a strikingly higher

9 Both laws refer to the question of transition, more or less in compliance with the Transfer of Enterprises Protection of Employees (TUPE) Directive.

10 This is an exceptional ruling in Hungarian labour law, as in other cases employees do not have the right to refuse a transfer and are automatically taken over by the new employer.



difference than the usual 20–30 per cent disparity between regional averages). Wage differentials between different local labour markets are thus boosted in the case of services outsourced by the local administration, while the public service employees' pay scale – though very depressed – has had a levelling effect.

The law prescribes the obligation to provide information when public service employees become subject to the Labour Code, which may ideally facilitate collective bargaining. The case studies of the two towns indicate that such bargaining takes place only if the trade union has engaged in robust interest representation beforehand. Similarly, even in the towns where municipal-level information and consultation forums formally exist they hardly ever allow employee representatives to have a say in restructuring, outsourcing and re-municipalisation decision-making.

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However, as the excerpts cited in the introduction suggest, the industrial relations climate has radically changed at the bus company since the field-work in 2012. As was promised at the beginning of the sub-chapter, we now return to the case highlighted in the introduction – and presented in Box 3.5.1 – in order to shed light on the background to the events which have unfolded at the public transport company since December 2012. Though related labour court cases are still pending at the time of writing, one can pose the question as to what has changed over a half year period. What are the new circumstances which strengthened the employer position so much that it has become able to challenge the union's long-established bargaining power? It is very likely that the position of the city's right-wing dominated leadership has been consolidated since the general election of 2010. In addition to direct political support – and by no means independent thereof – the town's economic situation has been improving. The timing is noteworthy: negotiations with the government had just ended in a 70 per cent bailout – much higher than could have been expected from the initial announcement of the prime minister – and now the city is considering purchasing buses. If the city were able to upgrade its run-down fleet, this would mean less demand for experienced drivers and there would be no grounds for the drivers' work-to-rule actions.

In addition, legislation also contributed to the strengthened management position. The sectoral law on essential services established a level of service provision so high that it practically ruled out any lawful strike at the company. The new Labour Code erodes the position of local unions, especially that of maintaining the position of full-time president. The law also imposes specific limits on the scope of collective bargaining in the state and municipality-owned company. Sanctioning of unfair dismissal has also been weakened drastically. Moreover, a new ground for dismissal is an employee's inappropri-

ate behaviour. This includes violating the obligation to “behave in accordance with the necessary trust relationship related to the given job”.<sup>11</sup> It worth noting that the CEO went further in terms of legal tools by criminalising workers engaging in a wildcat strike. In his report to the police the employer accused the trade union leader with “disturbing the operation of works of public interest” (*Közérdekű üzem működésének megzavarása*), a statutory definition in the Hungarian Penal (Criminal) Code, which threatens the perpetrator of the offense with a two to eight year period of imprisonment.

### Final thoughts

While studying the local governments’ response to the crisis, trends of privatisation and outsourcing, the researcher may find a lot of similarities between Hungary and Western European countries. Nonetheless, it is difficult to draw far-reaching conclusions owing to the striking differences in local government systems, traditions of local autonomy and division of labour between various levels of governance. Constraining the conclusions to the core issue of our investigation, the privatisation and outsourcing efforts, one can witness diverging trends in Western countries. While in a part of the countries the ongoing process of building New Public Management (NPM) was reinforced (most characteristically in the UK), elsewhere numerous examples of in-sourcing or “re-municipalisation” emerged, partly as a result of the autonomous deeds of local actors, partly due to the regulatory efforts of the central governments or Lands in federal states. In the long run, however, in western countries these changes seem to occur in an *ad hoc* manner. Recent changes in Hungary, however look very strange by international comparison, and neither follow the model of UK moving to NPM, nor that of the other countries which pursue parallel outsourcing and in-sourcing policies. The Hungarian processes, namely the systematic re-nationalisation, “re-municipalisation” or centralisation of control over public services, as well as government incentives to reverse secularisation cannot be matched to any Western mainstream crisis responses and seem to be rather unique developments.

Relatively few foreign research projects have dealt with the impact of adverse economic conditions on social dialogue at the local level. In their theory focused on developed market economies, *Marchington and Kynighou* (2012) sketched various alternative scenarios concerning changes in employee involvement and participation. One of the extreme poles is the expected marginalisation of participative institutions, for employers/decision makers are becoming less interested in the meaningful operation of employee participation. At the other pole, a more intense operation of institutions can be imagined, for employers/decision makers are well aware that they can utilize the institutions with a view to legitimizing their measures and thus they can rely on employees’ participative support. According to the authors, the actual fate

<sup>11</sup> Article 52(5) of the Labour Code contains this obligation of employees. Legislators basically incorporated previous court jurisprudence into the new Code. (For the latter explanation, special thanks to *István Horváth*.) On the other hand, such justification of the dismissal may be attributable to the similar option recently introduced in the public servants’ employment relationship (see sub-chapter 3.1).

of employee involvement and participation depends both on the actors' strategic choice and on the institutional context. Stated differently the first means whether the representatives of the employers/decision makers and those of the employees are willing to cooperate in order to promote changes or not. The well-known theory of "Varieties of Capitalism" (Hall and Soskice, 2001) embraces one set of important factors of institutional context – whether the given country can be classified as a liberal or as a coordinated market economy. Another important factor is the established trust relationship between employers and employees. Although Hungary can hardly be classified as one of the main models of "Varieties of Capitalism", an evaluation of the above mentioned preconditions would be highly topical.

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### 3.5.1 Case studies on municipalities' service provision

LÁSZLÓ NEUMANN & MÁRK EDELÉNYI

#### *Reorganisation of geriatric care in a big town*

In the past two years, the indebted town has transferred the provision of the majority of social services as well as three public educational institutions to churches. In both areas, outsourcing was justified by financial gains: churches being immediately entitled to higher per capita funding than local governments. The difference between per capita amounts is calculated every year on the basis of the financial resources provided by the municipalities to supplement state funds for service provision.

Prior to the transfer, the system of social service provision had been reorganized twice for cost reasons. In the 2007 reorganization, services were centralized and bringing back in-house the delivery of cleaning services previously outsourced. From 2009, in the second reorganization further streamlining occurred, with just three organizations retained in-house: day care services, care for people with disabilities and geriatric care. In the latter case, the number of residents decreased, with residential geriatric care being transferred to a church organization in 2011. Four workplaces and 343 employees were taken over by the Hungarian Baptist Aid. Two of the remaining three sites were closed, with the third taken over by the Jewish Community.

Having outsourced these activities, the town is no longer obliged to subsidize elderly care, and saved 0.5 billion HUF (EUR 1.8 million) per year (1.25% of the entire town budget); moreover, it proved to be advantageous despite the fact that the municipality undertook the responsibility of renovating some of the buildings after the transfer. The

outsourcing contracts include a clause stipulating that the municipality is obliged to “re-municipalize” geriatric care homes should there be any changes in financing. This would be relatively easy to put into practice, as the outsourcing is restricted to the operation of the organization and does not cover its assets and property. At the same time, the contract contains no guarantees as to the quality and price of services beyond that laid down in the relevant law. In 2012 the new provider was thus allowed to increase fees significantly. Not only did the local administration not interfere with this action but it also appreciated the advantages of not having to take such an unpopular measure itself.

In the residential care home taken over by the Hungarian Baptist Aid, a church organization, the largest employee group is made up of nurses and mental health professionals. As services are not outsourced, cleaners, laundry and kitchen personnel and drivers are also employed. Given the nature of the work, the majority of the workforce are women. Prior to the takeover, employees experienced a great deal of uncertainty, not only because of the previous lay-offs, but also because – aware of the municipality’s serious financial problems – they were very much concerned that their wages would not be paid. Such concerns were not unfounded, given that the local administration had previously revoked certain fringe benefits (the so-called cafeteria package and other benefits). On the other hand, they were afraid that the new provider would bring in its own people to replace existing personnel.

The local trade union has a 60–65 per cent unionization rate, although this has been in decline. Before the transfer, two trade unions had local or-