

# Is worker fund a viable substitute for severance pay?

**Austria has the lowest unemployment rate in Europe. IESE's Sandalio Gómez examines whether their model would be feasible in Spain.**

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Austria has become an example welfare state, with a highly developed market economy and a high standard of living. It is one of the world's richest countries in terms of per capita income, and has an unemployment rate of 4.9 percent, the lowest in the European Union.

Similar to other European countries, its pension system required reforms to adapt to shifting demographics, longer life expectancy and a decline in the working population.

In 2003, a major social and political agreement was reached to introduce a capitalization fund for each worker to complement the state pension system.

A [study](#) by IESE's [Sandalio Gómez](#) questions whether such a model could be applied in Spain, given many of the same challenges the country faces.

## **A system with high turnover**

Before the reform of 2003, the Austrian severance pay system was similar to that of the Spanish Statute of Workers' Rights: In the event of dismissal, severance pay was based on the employee's last gross monthly salary and seniority.

Employees with less than three years were not entitled to severance. As such, most companies preferred to end the contractual relationship with the employee before the three years were up, to avoid the accumulation of severance rights. This resulted in high turnover.

Workers who resigned voluntarily or who were dismissed for disciplinary reasons did not receive any form of compensation. As occurs in Spain, leaving to join another company meant losing seniority and the right to collect any type of severance pay.

The maximum period for severance was one year, compared with Spain, where severance is up to two years, and that has only been since the 2012 labor reform.

## **From severance to capitalization fund**

Austria introduced a new labor law in 2003, which was the result of an agreement reached between the government, trade unions and employers. Severance pay was abolished in exchange for employers contributing to a capitalization fund for each worker.

The employer contributes 1.53 percent of the gross salary to an individual account for each employee. In this way, the company is released from having to pay severance at the time of dismissal.

These are specially created accounts, which are managed in the capital market to achieve the highest profitability. The managing entity is agreed between the employer and the works council.

These entities, which are private and independent, must comply with all legal conditions and guarantee a minimum return that is equal to the payments made.

When employees leave to join another company, whether voluntarily or by being made redundant, they may choose whether to maintain their investment in the same fund or transfer it to that of a new company.

In the event of being fired, a third option is available: If they have contributed for at least three years, they can simply take the money with them, though in reality few actually do that.

This model allows for dismissal at no additional cost to the employer. It also encourages greater labor market flexibility and mobility for employees.

Although this may worry companies who fear the ease with which they may lose good employees, they should also remember the greater benefits this brings for productivity and competitiveness.

## **Would this work in Spain?**

The post-crisis economic situation, the opposition of social actors, and the differences in terms of culture and compensation have prevented similar reforms from being implemented in Spain.

However, the author believes the current situation in Spain makes it even more necessary to adapt a system like the Austrian one.

At first, the capitalization fund would represent an additional cost for employers. And Spain's trade unions would be radically opposed to eliminating any forms of severance pay.

This would require a major social pact between trade unions, business organizations and the government, which itself would require all of the major political parties to come together behind it.

For a proposal like this to prosper, the author sees the main challenges not so much logistical as sociocultural, necessitating a sea-change in attitude on the part of all social actors and a remarkable spirit of solidarity.

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