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Regulating Public Sector Wages in Times of Inflation and Constitutional Restraints

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ABSTRACT

Purpose: The article discusses the impact of public sector wages and inflation on various aspects of a country's socioeconomic development.

Methodology: Using Slovenia as a case study, the article focuses on how inflation impacts collective bargaining and wage regulation in the public sector, as well as the role of constitutional fiscal restraints in collective bargaining in the public sector. The research employs qualitative methods and focuses on patterns in existing documents and empirical case studies, and a comparative method involving Hungary.

Findings and Academic contribution to the field: The article examines the impact of inflation on collective bargaining and wage regulation in the public sector. It concludes that inflation, even with (some) constitutional fiscal restraints in place, can affect collective bargaining and wage regulation in the public sector, depending on the bargaining power of unions and employers and specific provisions outlined in collective bargaining agreements and wage regulations.

Keywords: *public sector, wage system, inflation, constitutional restraints*

JEL: Z00

1 Introduction

The wage or salary system in the public sector affects the socioeconomic development of a country, the labour market, the budget and fiscal policies, public spending, the social security of public employees, and ultimately inflation. There is no denying the importance of such a complex system in any country. In relation to the public sector wage system, the state acts in two roles - as an authority and as an employer. The state, as an authority, regulates the field of wages in the public sector through legislation. On the other hand, as an employer, the state concludes collective agreements with public sector unions within the framework of social dialogue. Those are facts, regardless of whether a country is big or small.

Government (or wider public sector) employment is an important aspect of fiscal policy and a sizable element of the labour market. Given the proportion of this type of expenditure, it seems plausible that fiscal policy is at least partially transmitted through the labour market. And yet policymakers seem to acknowledge government wages (mainly) as a stabilization tool (Gomes, 2015). But one thing is its connection to fiscal policies and another to inflation.

Wheatley (2022) claims (based on data from the UK) that the correlation between public sector wage increases and inflation is negligible and not statistically significant. This means that public sector wages are unrelated to inflation. And yet, public sector employees are striking and demanding wage raises in response to inflation. And some Governments respond negatively, even though there is no evidence that their wage increases are producing inflation. In effect, the wage-price spiral does not exist for public sector wages. A key reason for this is that the public sector labour force makes up a small percent (17) of the total workforce, meaning that it has much less of an impact on the economy than the private sector. The upshot of all this is that public sector employees are being penalized by reductions in their wages for reasons that do not bear up to scrutiny.

Some analysis agrees to some extent, claiming that the global surge in inflation in the last year or so has largely been driven by three key factors (1) supply in global goods markets was unable to keep up with surging demand during the pandemic, (2) many advanced economies made a stronger-than-expected recovery from the Covid-19 pandemic and (3) commodity prices rose sharply. Therefore, on one hand, headline inflation has surged in most advanced economies, driven by various factors, while wage growth has also picked up considerably, but more slowly and by less than inflation (Suthaharan and Bleakley, 2022).

If public wages and public employees are not the reason for the inflation, they suffer from it, since in a period of rising living costs (inflation), the purchasing power of consumers decreases. Considering that the worker receives a fixed wage, this means that he can afford less and less with the income from work. Therefore, it is only a question of time before the proposal to harmonize wages with the increase in living costs to maintain the value of wages and purchasing power will be put on the bargaining table.

The relationship between inflation and approaches to regulating public sector wages lacks theoretical findings, as well as empirical support since the latter is provided mainly by high-inflation countries, during high inflation periods. And this was lately (and luckily), not the case for most developed countries. Consequently, there was not much need for regulating the effects of inflation on public wages, and vice versa. Therefore, there will not be much focus on the periods when the inflation was above the European Central Bank's (ECB) inflation target rate of 2 percent.[1] The period on which the research will focus is the high inflation periods following 2007 with a special focus on the last inflation surge between 2021 to 2023. There are two main reasons supporting this decision. First, On January 1, 2007, the euro became legal tender in Slovenia and in 2008, a new public sector wage system was introduced, that is still in force. Meanwhile, it should be noted in advance, that in Hungary still the forint is the national currency,[2] and the rules regarding the public servants were modified in the last decade multiple times. This complexity is also compared to Slovenia in the following parts of the paper.

This article will aim to answer two research questions:

RQ 1: How does inflation impact collective bargaining and wage regulation in the public sector?

RQ 2: What is the role of constitutional fiscal restraints on collective bargaining in the public sector?

Constitutional fiscal restraint refers to the legal and institutional framework that limits government spending and borrowing. It includes provisions such as balanced budget requirements, debt ceilings, and spending caps, which are intended to ensure that governments operate within their means and do not accumulate excessive debt. The research will be carried out using empirical data from Slovenia. The results might not be entirely applicable to other countries, because of specifics countries have in their public sector wage system and different constitutional restraints regarding fiscal policies. Nonetheless, some common ground can be found, since most of the countries with similar political and economic systems are all facing similar problems regarding inflation and its effect on collective bargaining and wage regulation in the public sector.

To answer the research questions, we will analyse and present the findings that are useful in offering some answers. Legal documents, national reports, as well as other data and documents from the Slovenia Statistical Office and from the Hungarian Central Statistical Office are analysed in combination

1 ECB's 2 percent inflation target is assessed on the basis of inflation developments in the euro area economy and is low enough for the economy to fully reap the benefits of price stability while also underlining the ECB's commitment to providing a safety margin against the risk of deflation and among other things providing a sufficient margin to allow for downward wage rigidities, which risk raising unemployment excessively [https://www.ecb.europa.eu/mopo/strategy/pricestab/html/index.en.html].

2 The Fundamantal Law of Hungary even expressis verbis declares, that the official currency of Hungary shall be the forint. [Article K)] see: https://www.parlament.hu/documents/125505/138409/Fundamental+law/

with qualitative research methods as well as desk research were used in the paper. By using qualitative methods and focusing on patterns in existing documents, reviewing relevant literature, and empirical case studies of collective bargaining in the public sector in times of inflation as well as comparing Slovenia with Hungary regarding the discussed dilemmas of the paper are also presented. Thus, the research also worked with the tools of comparative law, comparative administrative law and analyses the chosen research topic with the main steps of the comparative law research program.[3] LŐRINCZ, Lajos defined two dimensions of comparisons in public administration: territorial comparison and temporal comparison.[4] The present article applies both methods together and can be identified as a micro-comparative work[5] focusing on the regulation of public sector wages in times of inflation and constitutional restraints in Slovenia and in Hungary. Attempts will be made to find existing constitutional court decisions regarding constitutional fiscal restraints on collective bargaining in the public sector. The article represents an incentive for further study of the field and solving the problem of the complex relationship of collective bargaining and wage regulation in the public sector regarding inflation and constitutional fiscal restraints, which in some form or another exist in many countries that can benefit from shared experience and findings. The result of the paper also proves that the article was a non-conceptual comparative work, consciously wished to analyse the substance of the issue and to promote its understanding. Finally in connection with the research methodology, it should be also noted that – where it is interpretable – recommendations of the authors are given.

2 Current situation in Slovenia and in Hungary

Slovenia is a small country in the center of Europe, an EU member state since 2004, and has 2 million inhabitants. In Slovenia (data from the end of 2022) there were 925 thousand active persons in the labour market, out of which 190 thousand were employed in the public sector, which makes for about one-fifth (20 percent) of the total workforce. All people employed in the public sector are subject to the Public Sector Salary System Act[6].[7]

Before the implementation of the Public Sector Salary System Act (ZSPJS), our wages were regulated by the Salary Ratio Act in Public Institutions, State Bodies, and Local Community Bodies (ZRPJZ)[8]. ZSPJS was adopted in 2002, but

3 Fekete B.: *A jogösszehasonlítás magyar történetének és alkalmazásának alapkérdései* in: Jakab A. – Menyhárd A. (ed.) (2015): *A jog tudománya*, HVG-Orac Lap- és Könyvkiadó, Budapest, 419–451.

4 Lőrincz L.*: Összehasonlítás a közigazgatásban* in: Lőrincz L. (ed.) (2006): *Közigazgatás az Európai Unió tagállamaiban. Összehasonlító közigazgatás, Unió Kiadó*, Budapest, 139-170 .

5 Gerencsér B. Sz. (ed.) (2015): *Összehasonlító és európai uniós közigazgatási jog. Közigazgatási jog IV*. Pázmány Press, Budapest, 23.

6 Official Gazette No. 108/09, 13/10, 59/10, 85/10, 107/10, 35/11 – ORZSPJS49a, 27/12 – odl. US, 40/12 – ZUJF, 46/13, 25/14 – ZFU, 50/14, 95/14 – ZUPPJS15, 82/15, 23/17 – ZDOdv, 67/17, 84/18, 204/21 in 139/22.

7 Republic of Slovenia Statistical Office, https://www.stat.si/StatWeb/en/News/Index/10705.

8 Official Gazette No. 18/94, 36/96, 20/97 – ZDPra, 39/99 – ZMPUPR, 86/99 – odl. US, 98/99 – ZZdrS in 56/02 – ZSPJS).

it came into force in 2008, providing a single payment scale, composed of 65 wage grades, for all public sector employees. It specifies that wages shall be composed of a basic wage, additional payments, and a part related to the workers' performance. To date, the law has been amended (in one way or another) over thirty times. At the end of 2007, 155 thousand people were employed in the public sector. Despite the period of the financial crisis, the number of employees grew to 160 thousand by the end of 2011. The current number of employees in the public sector has reached almost 190 thousand at the end of 2022. They are employed by more than 3 thousand budget users (state bodies (government, ministries, administrative units) and self-governing local communities (municipalities), public agencies, public funds, public institutes, etc.), and the total volume of wages almost reached 5 billion EUR in 2022.[9]

Hungary is the east neighbour of Slovenia and similarly to Slovenia, it became EU member state in 2004. Hungary's population is around five times bigger than Slovenia's population,[10] the average number of employed people aged 15–74 was 4 million 707 thousand people in March 2022. Regarding the salary regulation of public servants – contrary to Slovenia - Hungary[11] do not have one act on the salaries which determines all wages of public servants, but it is regulated in the different status acts. From which, the most important are: Act CXCIX of 2011 on civil servants (Kttv.), which is primarily applied to public employees in local government administration bodies. Act CXXV of 2018 on government administration (Kit.) is regulating the status of public servants working in central and territorial state administration. Administrative bodies with special status like as autonomous government agency, independent regulatory organs[12] have their own legal regulation (Act CVII of 2019 on Bodies with Special Legal Status and the Status of Employees, this is referred to as Küt. in Hungary). One of the latest acts of Hungarian civil service legislation is the Act CXXX. of 2020 on the Legal Status of Personnel of the National Tax and Customs Administration (NAV szjtv). The primary goal of this Act was to implement the integration of the personnel after the organizational integration processes.[13] Another category is the public service employees in budgetary institutions (for example education, health and social care institutions), to whom the Act XXXIII of 1992 on the Legal Status of Public Servants (Kjt.) is applied. We shall also note that there is a special act regarding the professionals and contract agents in defence and law enforcement.

These before-mentioned acts are funded in a various range of personal policy solutions: while one regulation seems to prefer centralized regulatory meth-

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9 Public sector wages portal http://www.pportal.gov.si.

10 More precisely: 9 689 010 Data is from the Hungarian Central Statistical Office see: https://www.ksh.hu

11 See regarding Hungarian public administration: Patyi, A.: *A közigazgatás a magyar állam rendszerében* in: Orbán, B. - Szalai, Z. (ed.) (2019): *Ezer éve Európa közepén: A magyar állam karaktere*, Mathias Corvinus Collegium, Tihanyi Alapítvány, 283–310.

12 Like as: National Election Office, Hungarian Energy and Public Utility Regulatory Authority, the National Media and Info communications Authority, Hungarian Competition Authority

13 Kiss, Gy. - Hazafi, Z.: *Az életpálya fogalmáról* in Kiss, Gy. (ed.) (2009)*: Közszolgálati életpályák jogi szabályozása,* Dialóg Campus Kiadó, Budapest,. 19–62.

ods (for example: Kttv.), the other one a decentralized solutions (for example: Kit.), the other one a mix version (for example NAV szjtv.).

The current law on public servant status in Hungary is completely over-differentiated, which also has a serious impact on the remuneration system: several different salary tables based on different logics apply to those employed by the state, which results in significantly different salaries. Without getting into the detail, we would like to describe two Acts (Kttv. and Kit.) salary system to show the differences in the regulation: in the Kttv., the salary consists of three components: a) the basic salary, which is the biggest part of the salary b) the salary supplement and c) various allowances. It is important to note that the basic salary creates a link between the wage and the advancement. The Kttv. contains the characteristics of career systems: advancement can take place in grades, titles and manager positions. Salary increases are related to advancement in grades which is also linked to the spent years in work. Oppositely to this regulation, the wage regulated in the Kit. are not decided on the education and length of service in the public sector, but by the characteristics of the position, the professional conditions for filling the position. Thus, classification is made for a post like as administrator, the professional manager, professional senior manager, the person with the status of a commissioner, the consultant and the political senior manager. The Kit contains two salary scales: the first applies to government officials employed in ministries, while the second applies to government officials in government agencies, central offices, the capital and county government offices. Regarding the method of determining the exact amount of the salary, the parties have the option of a kind of wage bargaining in the minimum and maximum limits of the post salary determined in the Act. This also means that the calculation of the salary does not depend on the amount of the salary base and the multipliers related to the salary grades (contrary to the Kttv., in the Kit. we cannot find salary grades and multiplies, salary supplements). [14] Lastly, we should underline that both Acts refers that the salary should reach the guaranteed minimum wage.

Regarding the salary system we would like to emphasize two critical points:[15] 1) it is over-differentiated. However, this is not a constitutional problem.[16] 2) The other anomaly concerns the level of civil service salaries. Since 2008, the civil service salary base is unchanged, which is a fixed amount of HUF 38,650 (around a 100 EUR), decided yearly by the Budget Act.[17] This salary base shall be multiplied by the number determined in the Kttv.. With salaries that have been frozen for more than ten years, the predictable progress and competi-

14 Ludányi, D. (2022):. Regulation of Advancement and Salary Systems in the Hungarian Public Administration, *Belügyi Szemle*, 70(SI1), 35–52.

15 See also: Petrovics, Z.: *Quo Vadis Civil Service Law?: Tendencies in the Hungarian Civil Service Law i*n: Auer, Á. - Bankó, Z.- Békési, G.- Berke, Gy.- Hazafi, Z .- Ludányi, D. (ed.) (2023): *Ünnepi tanulmányok Kiss György 70. születésnapjára : Clara pacta, boni amici*, Budapest, Magyarország, Wolters Kluwer Hungary, 560-567., Linder, V.: *Qui est qui? Aperçu de la cavalcade de la réglementation dans la fonction publique hongroise* In: Árva, Zs.- Barta, A. (ed.) (2021): *Évtizedek a magyar közigazgatás szolgálatában : Ünnepi tanulmányok Balázs István Professzor 65. születésnapjára,* Debreceni Egyetem, Állam- és Jogtudományi Kar, Debrecen. 279–288.

16 See: 3222/2017. (IX. 25.) Hungarian Constitutional Courts's decision

17 See: Article 65. § of th Act XXV of 2022 on the Hungarian budget of 2023.

tive remuneration considered to be the comparative advantage of public employment obviously cannot be realized.[18] Thus there is a tension within the public sector and between the public and private sector too.

A small country costs money. It must have practically all the institutions that the "big ones" have. Universal access to quality public services and the implementation of public services in the fields of education, healthcare, social services, etc. cost. However, understanding this simply as a cost is a mistake. It is necessary to invest in large systems. And the foundation of large systems is not only investments in premises and material equipment, but also investments in people, in employees. Without them, the system cannot function. These large systems are necessary for the normal functioning of the country and the economy.

In Slovenia, the public sector wage setting is primarily carried out within the public sector collective bargaining process where state or government representatives and public sector unions negotiate on the specifics of the public sector wage changes. Social dialogue and in connection to it - the bargaining system - have always been seen as a tool of centralization through a unified wage system in the public sector, aimed at concluding general agreements.

3 A centralized public wage system in Slovenia

Since Slovenia's independence in 1991 - similarly to Hungary - steps were taken to maintain and complement the centralized bargaining system over wages and other terms and conditions of employment in the public sector. In 2006 the Collective Agreements Act (Zakon o kolektivnih pogodbah - ZKolP) was adopted.[19] The general provisions of the ZKolP also apply to collective bargaining in the public sector. The exception is the normative, substantive part of public sector collective agreements that refers to wages, which is regulated by the Public Sector Salary System Act. In the public sector, the system of centralized collective bargaining has endured, with a 'central platform' or framework for collective bargaining, the beforementioned Public Sector Salary System Act, which ensures a high degree of coordination. The collective agreement for the public sector was concluded in 1991 and then amended several times. In 2008, the already mentioned ZSPJS came to power. Soon after, the global economic and financial crisis started and austerity measures began to be enforced, and pressures on public sector employees began to intensify. In 2010, the government decided to terminate collective agreements in the public sector. The Minister of Public Administration demanded that the public sector unions agree to the proposed austerity measures regarding wages for 2011 and 2012. If not, the collective agreements were to be terminated because failure to do so would endanger the passing of the budget. No agreement was reached, so the government rescinded the terminations and adopted the Intervention Measures Act that extended non-payment of the

18 Kártyás, G.: *Díjazás a közszolgálati foglalkoztatási jogviszonyokban* in: Kiss, Gy. (ed.) (2019)*: Közszolgálati életpályák jogi szabályozása,* Dialóg Campus Kiadó, Budapest. 231–232.

19 Official Gazette No. 43/06 in 45/08 – ZArbit.

performance-related bonus for public employees, froze payments for promotion, set the holiday allowance at a lower level, and limited the funds for increased workloads for two years. The pressure on public sector employees culminated in the spring of 2012 when the government announced a 15 percent pay cut in the public sector. A general strike of public sector employees ensued, followed by the adoption of the Fiscal Balance Act[20] (Stanojević and Poje in (ed.) Müller, Vandaele and Waddington, pp. 545–551).

Slovenia has a centralized bargaining regime regarding public wages. Collective bargaining takes place at the national or state level. Central negotiations are attended by all representative public sector unions, where they usually discuss common foundations and matters which apply to everyone in the public sector. One of the problems was that the existing public wage system, established in 2008, can hardly be called uniform. In the analysis presented by the Ministry of Public Administration before the start of negotiations on the wage reform, it notes, among other things, that by concluding partial agreements with individual professional groups, represented by different public sector unions, and introducing wage provisions into sectoral legislation, the uniform system was circumvented, while individual groups gained substantially more than others. More and more wage classes are below the minimum wage, and the ratio between the lowest and the highest wage has dropped from 1 to 10.5 when the system was established to 1 to 4.7.[21]

4 Inflation and public sector wages

Some authors claim that the current low unemployment level could trigger a wage-price spiral, particularly if public sector wage is increased. So it could be argued that the government's refusal to raise public sector wages is a strategy to control inflation (Whiteley, 2022). Zaranko (2022) on the other hand argues that public sector wages policy should not be set regarding distributional objectives or used as an inflation- or demand-management tool. Instead, wage awards should be set up to ensure that the government/state can attract, retain and motivate the appropriate number and mix of public employees required to deliver the government's desired range and quality of public services. Zaranko, therefore, suggests that while the government is right to be concerned about the plight of low-income households struggling to cope with the rising cost of living, and right to be concerned about higher inflation expectations becoming embedded, these are issues best dealt with using tools other than public sector pay policy. Instead, pay decisions should be made regarding ensuring that the right people with the right skills are in the right places to deliver on public service objectives.

20 Fiscal Balance Act, Official Gazette No. 40/12, 96/12 – ZPIZ-2, 104/12 – ZIPRS1314, 105/12, 25/13 – odl. US, 46/13 – ZIPRS1314-A, 56/13 – ZŠtip-1, 63/13 – ZOsn-I, 63/13 – ZJAKRS-A, 99/13 – ZUPJS-C, 99/13 – ZSVarPre-C, 101/13 – ZIPRS1415, 101/13 – ZDavNepr, 107/13 – odl. US, 85/14, 95/14, 24/15 – odl. US, 90/15, 102/15, 63/16 – ZDoh-2R, 77/17 – ZMVN-1, 33/19 – ZMVN-1A, 72/19, 174/20 – ZIPRS2122 in 139/22 – ZSPJS-AA.

21 More data is available on https://www.gov.si/zbirke/projekti-in-programi/prenova-placnega-sistema-v-javnem-sektorju/ [accessed 30. 3. 2023].

In such a regime encompassing the public sector unions are forced to moderate their wage claims within confederal agreements because expansionary wage policy across-the-board generates inflation spill overs, thereby jeopardizing their members' purchasing power and export-sector jobs (Di Carlo, 2022, p. 4).

Empirical evidence from Slovenia shows that the average wage for 2022 was 2,023.92 EUR gross or EUR 1,318.64 EUR net. It was nominally higher than the wage for 2021 (in the gross amount by 2,8 percent or in the net amount by 3,8 percent), but in real terms lower (in the gross amount by 5,5 percent or in the net amount by 4,6 percent). The reason was inflation and rising costs of living. This statement is also true for Hungary, where the average wage for 2022 was 499 980 Ft. (around 1250 EUR) gross or 332 487 Ft. (around 830 EUR) net, and for 2021. 425 915 Ft. (around 1065 EUR) gros or 283 234 Ft (around 708 EUR) net.[22]

Compared to the wage for 2021 in Slovenia, the average gross wage for 2022 was higher by 6,2 percent in the private sector and lower by 2.5 percent in the public sector (in the state bodies or government sector it decreased by 4,9 percent). Among other things, the mentioned wage movement was influenced by the measures related to the Covid-19 epidemic, which were in effect in the first half of 2021.[23] At the same time, Slovenia had the lowest unemployment rate on record. The rate of registered unemployment, which is calculated by the Employment Service of Slovenia, was 5.6 percent in January 2023, which is 0.2 percentage points higher rate than last December and 1.3 percentage points lower than in January 2022.[24] Meanwhile in Hungary the rate of unemployment is lower than in Slovenia, 4,1 in 2021 and 3,6 in 2022.[25]

In Slovenia, the ZSPJS, with its 65 wage grades, for all public sector employees and elected officials, states that the values of the wage grades are (or better should be) adjusted once a year. There is no automatic wage indexation to the costs of living in the public sector neither in Slovenia, nor in Hungary.

In Slovenia public wages are not automatically indexed to inflation, nor does inflation play a formal role in wage setting. Only a minor part of public wages (e. g. meal allowances, business trips, tenure allowances) are indexed to past inflation; the minimum wage is also adjusted (at least) in line with inflation (Checherita-Westphal, 2022, p. 6).

The level of adjustment must be the same for public employees and elected officials. The level of coordination for public employees is determined by the collective agreement for the public sector, and for elected officials, after a carried out prior coordination with the elected officials, according to this law. In addition, ZSPJS Article 5 has a reference norm that bargaining starts no later than May 1 and, as a rule, ends 30 days before the deadline set for the submission of the state budget to the National Assembly of the Republic of

22 See more data: https://www.ksh.hu/stadat_files/mun/hu/mun0001.html
23 Republic of Slovenia Statistical Office, https://www.stat.si/StatWeb/News/Index/10891.
24 Employment Service of Slovenia, https://www.ess.gov.si.
25 See: https://www.ksh.hu/?lang=hu

Slovenia. Since the beginning of the ZSPJS application, the value of the wage grades has been changed several times, but not with the aim of annual reconciliations according to the procedure set out in this article, but within the framework of anti-crisis austerity measures to mitigate the economic and financial crisis after 2008. As part of these measures, there was a decrease in the value of wage grades, their compression (reduction of the range between the values of wage grades on the wage scale), and then renewed decompression. The value of the wage grades has thus been valid from 2016 onwards (Apohal Vučković, 2022, p. 124).

The Collective agreement for the public sector from 2008[26] stated that this year, the basis for the adjustment of basic salaries will be determined by the amount of the expected growth rate of consumer prices (inflation) for 2008 in Slovenia.[27] If the actual growth in the prices of consumer goods in Slovenia from December 2007 to December 2008 will exceed the projected inflation growth from the first paragraph of this article, the basic wages in January 2009 will be increased by the resulting difference. A similar agreement was set for 2009, with an exception that in case of an actual increase in the prices of consumer goods in Slovenia from December 2008 to December 2009 exceeding the expected increase in inflation from the first paragraph of this article, the basic wages in January 2010 will be increased by half of the resulting difference.[28]

Those were the times of financial crisis. In 2011 the Additional 2012 Intervention Measures Act[29] decreed that notwithstanding Article 5 of the ZSPJS and based on the adopted regulations or collective agreements, and regardless of the difference between the actual and predicted growth in the prices of consumer goods (inflation) in the period from December 2010 to December 2011, the value of the wage grades from the wage scale does not increase in correspondence until June 30, 2012. And this period was later prolonged until 2014 by the Act Amending the Public Sector Salary System Act[30] stated that regardless of the provision of Article 5 of ZSPJS, the values of the wage grades from the wage scale from the beginning of January 2014 to the end of December 2014, shall not be adjusted to the growth in the prices of consumer goods (inflation). In 2012 the Public Finance Balancing Act was adopted.[31] The austerity measures were aimed at saving a good 818 million EUR in 2012, and almost 949 million EUR in 2013. The result was the largest public

26 Collective agreement for the public sector, Official Gazette of the Republic of Slovenia, No. 57/08.

27 In 2008 inflation in Slovenia reached 7 percent. Year-on-year inflation decreased rapidly in the first half of 2009, hovering around zero from August to October, but began to rise again in the last months of the year and amounted to 1.8% in December (Institute of Macroeconomic Analysis and Development, https://www.umar.gov.si/en/public-info).

28 Collective agreement for the public sector, Official Gazette of the Republic of Slovenia, No. 57/08.

29 Additional 2012 Intervention Measures Act, (Official Gazette of the Republic of Slovenia, No. 110/11 , 40/12 – ZUJF, 43/12 and 3/22 – ZDeb), Article 5.

30 Act on Amendments and Supplements to the Act on the Salary System in the Public Sector (Official Gazette of the Republic of Slovenia, No. 46/13), Article 44. C.

31 Public Finance Balancing Act (Official Gazette of the Republic of Slovenia, No. 40/12 , 96/12 – ZPIZ-2, 104/12 – ZIPRS1314, 105/12 , 25/13 – od. US, 46/13 – ZIPRS1314-A, 56/13 – ZŠtip-1, 63/13 – ZOsn-I, 63/13 – ZJAKRS-A, 99/13 – ZUPJS-C, 99/13 – ZSVarPre-C, 101/13 – ZIPRS1415, 101/13 – ZDavNepr, 107/13 – decision US, 85/14 , 95/14 , 24/15 – decision US, 90/15 , 102/15,

sector strike in the history of independent Slovenia. Yet after this, there was not much talk about inflation and its impact on public sector wages. That is until 2022. Annual inflation in Slovenia was 1.1 percent in 2020, 4.9 percent in 2021, and 10.3 percent in 2022.

5 Regulation of public sector wages in times of inflation

When researching the link between fiscal deficit and inflation some authors suggest that the link is relatively strong, but it becomes weaker in the absence of the public sector wage expenditure (Ekanayake, 2012, p. 3). Therefore, the overall inference is that public sector wage expenditure is (or can be) a key factor in explaining the deficit-inflation relationship. On the other hand, some authors regarding this issue argue that the public sector wage cycle effect underlies the weak correlation between fiscal deficits and inflation rate (Buffie, 1999).

Rising public wages have an impact on many areas. For instance, some countries' empirical research was used to determine that the rising public sector wage bill and inflation have a significant impact on the value and exchange rate of the national currency in the country's economy. The research also suggests independent non-political fiscal bodies must be established to undertake responsibilities such as: ensuring wage sustainability through negotiation of public sector wage adjustment subject to budgetary constraints. (Ofori-Abebrese et al., 2017, p. 377 and 378).

Findings suggest that governments should be cautious so that wage-setting and employment policies do not lead to negative repercussions on fiscal and economic performance. First, there appears to be a need to strengthen fiscal discipline and reduce the risk of pro-cyclicality in government wage expenditure. To this end, strict domestic fiscal rules and medium-term budgetary frameworks could be effective tools to constrain the volatility and pro-cyclicality of this spending item. In addition, reforms to labour market institutions may be needed to avoid institutional biases towards pro-cyclicality, e. g. originating from indexation, which ties government wages to inflation (Holm-Hadulla et al, 2010, p. 5). International Labour Organization report also shows that inflation and consequently high-interest rates can increase the attractiveness of public debt among investors because government bonds bring greater returns at a risk that is considered low, the interest payments on public debt faced by governments increase and this may ultimately divert resources away from public employment creation (ILO, 2022, p. 115).

The government and public sector unions in Slovenia, in October 2022, signed an Agreement on measures in the field of wages and other labour costs in the public sector for the years 2022 and 2023. The agreement also contained changes to the Social Insurance Institution, which adopt measures that will mitigate the consequences and impact of high prices and inflation on the avail-

63/16 – ZDoh-2R, 77/17 – ZMVN-1, 33/19 – ZMVN-1A, 72/19 , 174/20 – ZIPRS2122 and 139/22 – ZSPJS-AA).

able incomes of employees in the public sector. The changes provided for a 4.5 percent increase in the value of the salary classes of the salary scale, which will have financial consequences in the amount of 43.4 million EUR in 2022 and 260.3 million EUR in 2023 and the following years.[32] The agreement predicted that the value of the wage grades would increase by 4.5 percent as of October 2022. Employees in the public sector will feel this increase for the first time when their October salaries are paid in November. Most people employed in the public sector will then have their wages raised again, starting April this year (2023), by one wage grade, which means an increase of about four percent.

The ZSPJS is not subject to harmonization with the legal order of the EU. From the data obtained by the Government in the framework of the European Network for Public Administration - EUPAN in July 2022 regarding the questions of how EU member states are facing rising inflation and generally higher living costs through wages in the public sector and whether countries have taken any special measures in this area (e.g. annual adjustment of wages), it follows that, given the otherwise different regulation of the public sector wage system, countries react(ed) differently to these two factors, and in several countries, discussions are still ongoing about measures that would mitigate the effects of increased inflation and rising costs.[33]

Although the government represents the state in collective bargaining procedures and enjoys some discretion, we must not forget democratic safeguards – such as the checks and balances system – that are in power and limit the government's discretion. The government can bargain with the public sector unions and sign a Collective Agreement for the Public Sector, but when regulating legislature (e.g. Collective Agreement for the Public Sector – ZSPJS) the final decision is up to the legislator, in Slovenia to the National Assembly. The same goes for the state budget or Acts on the implementation of the budgets of the Republic of Slovenia, where the government can prepare a budget proposal, but it is up to the legislator to adopt it. So even the government discretion has its limits. Keeping in mind our first research question on how inflation impacts collective bargaining and wage regulation in the public sector, we can conclude that inflation has certain impacts on collective bargaining, while the extent of the impact is left to the discretion of the government. If inflation is high, public-sector unions may demand higher wage increases to offset the increased cost of living for their members, which is exactly what happened in Slovenia, where the government's answer to inflation was a rise in public-sector wages. This can also be attributed to the power of the public sector unions. Inflation on the other hand also had an indirect impact on public sector wage regulation, since the changes in the public sector wage regulation were a result of collective bargaining.

In Hungary, the status acts also state several forums and organisations that can act in the interest in their public servants. As an example, the Kit. states that the

32 Act on Amendments to the Act on the Salary System in the Public Sector (Official Gazette of the Republic of Slovenia, No. 139/22), Article 10.

33 Proposal of the Act on Amendments to the Act on the Salary System in the Public Sector, October 12, EVA No.: 2022-3130-0049.

protection of social and economic interests as well as the maintenance of peace in the labour this Act regulates the connection between the trade union and the government's administrative body and the representative organisations.[34] Even the initiative could come from the trade union, from the request of the public servants the decision is in the hand of the government, and in the Parliament to decide in the wages of the civil servants. In this paper we would like to underline only one fact of the latest changes, in May 2023, the government –after increasing several public servants' wages like doctors, nurses, police officers – there is a possibility to increase the public servants' salary, those who work in the territorial or central state administration. After the initiative of the trade union, and the several weeks of negations regarding the increase of the salary is a possibility not an obligation in the hands of the employers. This increase is ensured by fact that the positions is decreased by 10%. Thus, this practically means that the free post are "frozen" and the salary of these post will finance the current increase.[35] This could be seen as a very logical need as the inflation is 24% (April, 2023) in Hungary, the highest in the European Union.[36]

6 Constitutional fiscal restraint and collective bargaining in the public sector

The connection between these two concepts lies in the fact that collective bargaining can have a significant impact on public finances. Collective bargaining agreements can result in higher public sector wages, benefits, and pension obligations for public sector employees, which can increase government expenditures and affect the budgetary process. Therefore, constitutional fiscal restraint is necessary to ensure that governments can balance their budgets and responsibly manage their finances, even in the face of collective bargaining demands.

After the first period of inflation around 2008, and at the end of the financial crisis (2008-2014) the Constitutional Act amending Article 148 of the Constitution of the Republic of Slovenia was adopted.[37] With it, a so-called constitutional golden rule of fiscal policy was implemented at the constitutional level.[38] Following soon after the Fiscal Rule Act was adopted with the intent

34 See: Article 170-172 of Kit.

35 Governement Decree 180/2023. (V. 15.).

36 See: https://www.ksh.hu/?lang=hu.

37 Constitutional Act amending Article 148 of the Constitution of the Republic of Slovenia, Official Gazette RS No. 47/13, Constitution of the Republic of Slovenia, Article 148 (budget) "All receipts and expenditures for the financing of public spending must be included in the state budgets.

The revenues and expenditures of the state budgets must be balanced in the medium term without borrowing, or revenues must exceed expenditures. This principle can only be temporarily deviated from in exceptional circumstances for the country. The law, which is adopted by the National Assembly with a two-thirds majority of the votes of all deputies, determines the method and time frame of implementing the principle from the previous paragraph, the criteria for determining exceptional circumstances and the way to act when they occur. If the budget is not adopted by the first day when it is necessary to start implementing it, the beneficiaries who are financed from the budget are temporarily financed according to the previous budget."

38 For better understanding of the golden rule in public finance see Zeyneloglu, I. (2018). Fiscal policy effectiveness and the golden rule of public finance. Central Bank Review, Volume 18,

to determine the method and time frame for implementing the principle of medium-term balance of revenues and expenditures of state budgets (the beforementioned constitutional golden rule of fiscal policy) without borrowing, the criteria for determining exceptional circumstances in which medium-term balance may be deviated from, and the manner of dealing with their performance or termination.

The Fiscal Rule Act is, on the one hand, a warning and, on the other hand, a guide on how to act when and if we are faced with a new economic and financial crisis, with a significant reduction in budget revenues and, at the same time, with large burdens on the side of budget expenditures (Arhar and Avbelj (eds.), 2019, p. 381).

The Act also regulates the operation of the Fiscal Council as an independent state body.[39] This law partially transposes the Council Directive 2011/85/EU on requirements for budgetary frameworks of the Member States into the Slovenian legal system.[40] The Fiscal Council in one of its last assessments noted that in addition to one-off factors, budgetary movements will also be characterized to a large extent by large-scale factors discretionary measures taken in the last year, and the high expected level of investment. Discretionary measures should worsen the state of public finances by around 2 percent of GDP per year in the coming years and are operating on the side revenues and expenses. The latter, due to the (at the time) proposed amendments to the tax legislation, which in part neutralize the effect of the original changes, strongly dominates. Most of them relate to wages in the public sector and social benefits, even with high inflation based on existing legislation and, in addition to measures in the field of growing costs of living, ensure the preservation of their real value. The predicted growth of the current expenditures of the government sector in the next two years thus amounts to around 6 percent per year, which is about twice the long-term average. The risks that their growth will be even higher are considerable, especially in the area of public wages.[41]

If we regard the new Hungarian constitution, named as the Fundamental Law of Hungary, we find similar. Constitutional fiscal restraint too as Article 37 states that the Government shall be obliged to implement the central budget in a lawful and expedient manner, with efficient management of public funds and by ensuring transparency.

With the exceptions specified in the Fundamental Law, no such borrowing may be contracted, and no such financial commitment may be undertaken in the course of the implementation of the central budget that would allow the government debt to exceed half of the total gross domestic product. Moreover, similar to Slovenia , in Hungary the status and the most important tasks of the Financial Council is stated in the Fundamental Law of Hungary as follows:

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39 Fiscal Rule Act (Official Gazette of the Republic of Slovenia, no. 55/15 , 177/20 - compr. and 129/22), Article 1.

40 Official Journal of the European Union L 306/41, 23. 11. 2011.

41 Assessment of budget documents for years 2023 to 2024 (October 2022), https://www.fs-rs.si/wp-content/uploads/2022/10/Ocena_oktober2022.pdf.

as an organ supporting the legislative activity of the National Assembly, the Fiscal Council shall examine the feasibility of the central budget.[42]

The Constitutional Court of Slovenia on the other hand did not deal with inflation and public sector wages on many occasions. This can in part be attributed to the fact that high inflation periods did not happen very often. Yet some decisions made by the Constitutional Court of Slovenia related to inflation do exist. In case U-I-159/08[43] it noted (regarding judges' salaries) that in addition to the total amount of judges' salaries, their relative stability also plays a key role in ensuring judicial independence, and that the reduction of judges' salaries, (prohibited by Article 125 of the Constitution), can also cause a considerable drop in their real value. The determination of the specific level of coordination is left to the arrangement with the collective agreement for the public sector, the actual coordination is tied to the conclusion of such an agreement between the parties to the collective agreement for the public sector - the conclusion of which may also be uncertain and in the conclusion of which judges cannot even participate. When relating to judges, the Constitutional Court found the fourth paragraph of Article 5 of the Act on the Salary System in the Public Sector (ZSPJS) to be inconsistent with the Constitution. Yet such a decision was only made since they were discussing judges and no other public employees.

Regarding our second research question, we can only reply that constitutional fiscal restraints have little legal weight on the collective bargaining procedure (and even outcome) in the public sector in Slovenia. The reason lies in the constitutional soft approach, where there are no strict rules preventing government discretion. On the other hand, the relationship between constitutional fiscal restraints and collective bargaining can be complex, since there is ongoing (political and economic) debate over the appropriate balance between budgetary discipline and the right to fair compensation for public sector employees. And such a debate is usually decided on election day.

7 Conclusion

National public sector wage systems are not subject to harmonization with the *acquis communautaire* or legal order of the EU. They present an area where (even) EU member states enjoy discretion in regulating different aspects of the system. Harmonizing and indexing public sector wages with inflation is one of those areas.[44] Unless a state determines certain criteria (e. g. automatic indexation of public sector wages with inflation) in its regulatory

42 Aricle 44 of the Fundamental Law of Hungary. See: Halász Zs.: *Public Finances* in: Varga Zs. A. – Patyi A.- Schanda B. (ed.) (2015): *The Basic (Fundamental) Law of Hungary : A Commentary of the New Hungarian Constitution* 321-344.

43 Decision on the partial finding of unconstitutionality of the Act on the Salary System in the Public Sector and the Act on Judicial Service (Official Gazette of the Republic of Slovenia, No. 120/08).

44 Price indexation of public wages is relatively limited (to about one fifth) in the euro area since full and partial price indexation is reported in five countries (Belgium, Luxembourg, Cyprus, Malta and Italy). In most euro area countries, public wages are not automatically indexed to inflation, nor does inflation play a formal role in wage setting (Checherita-Westphal, 2022, p. 6).

framework it is relatively free to respond to rising inflations in its own accord. It of course must be kept in mind that every person is entitled to pay for the work they have done, that people enjoy inherent dignity etc. Many countries or governments often refuse to raise public sector wages, saying doing so will fuel inflation. Researchers' views on public sector wages' impact on inflation differ (Wheatley (2022) or Gomes (2015)). One must also keep in mind that every period of enhanced inflation has its specifics and reasoning behind it.

Inflation can have a significant impact on collective bargaining and wage regulation in the public sector. If inflation is high, public-sector unions may (and have done so in Slovenia and many other countries similar tendencies were in Hungary too – in the last year or so) demand higher wage increases to offset the increased cost of living for their members. Inflation can also impact the timing of collective bargaining agreements. Regarding public sector wage regulation in times of inflation governments are allowed to be flexible and enjoy some discretion in the approach they choose to tackle the situation. Even with (some) constitutional safeguards in place – such is the case of Slovenia. Some collective bargaining agreements and wage regulations include indexation clauses that tie public wage increases to inflation – this is also not the case for Slovenia.

Overall, inflation – without serious and strict constitutional fiscal restraints - can (significantly) impact collective bargaining and wage regulation in the public sector. The real impact depends on the existence of different factors, including the level of inflation, the bargaining power of unions and employers, and the specific provisions of collective bargaining agreements and wage regulations (e. g. indexation). In Slovenia, the constitutional restraints regarding public sector wages can be considered toothless or paper tigers. And since wage indexation does not exist in Slovenia, the factor truly influencing wage regulation is the (existing) bargaining power of public sector unions and employers. Rising public sector wages are therefore not (the only) contributor to rising inflation and vice versa.

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