

Overview

Starting a business

Dealing with construction permits

Employing workers

Registering property

Getting credit

Protecting investors

Paying taxes

Trading across borders

Enforcing contracts

Closing a business

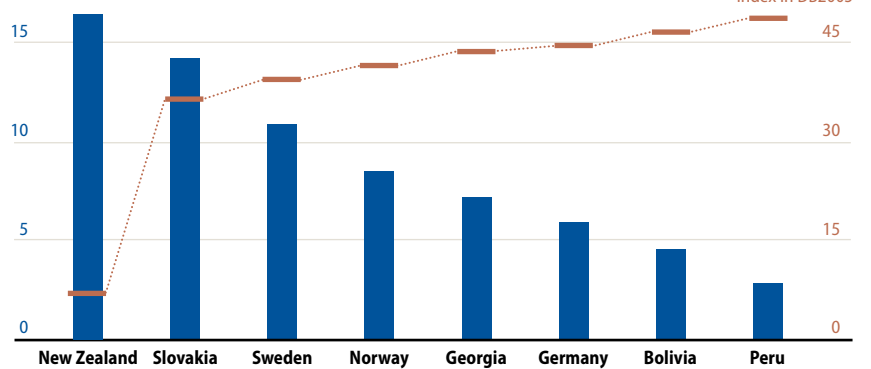
Aissa, a successful designer, owns a business exporting traditional Senegalese handwoven fabrics to upscale international brands like Hermès and Christian Lacroix. Demand is growing, so much so that Aissa would have to quadruple production to meet it. But that would mean hiring more workers—and that seems too risky.¹ What if demand should decline? It would be difficult to downsize again. “People can sue you and say you have fired them illegally,” Aissa explains. “You have to give them a letter and then a long process begins.”

That process would involve multiple letters to the labor inspector, all requiring a formal response. Aissa would have to give specific reasons for dismissing workers and prove that she had tried other solutions. She could not choose

FIGURE 4.1

Economies with rigid labor regulations have fewer business start-ups

Average entry rate, 2000–04 (%)



Source: *Doing Business* database; Djankov, Ganser, McLiesh, Ramalho and Shleifer (2008).

which workers to dismiss; she would have to follow a particular order of seniority. And she would have to prove that her industry is suffering a slowdown. This is nearly impossible, since Senegal lacks reliable statistics on industrywide trends. Besides, there are no formal criteria on what constitutes a slowdown. The labor inspector decides.

Senegal’s restrictive labor laws make it difficult to adjust to demand. Besides the burdensome dismissal requirements, employers face tight restrictions on working hours and a ban on using fixed-term contracts for permanent tasks. All this leads to another problem for Aissa: many of her competitors circumvent labor regulations altogether by operating in the informal sector.

Aissa is not alone. A study of 1,948 retail stores in large Indian cities finds that 27% see labor regulations as a problem.² The study also finds that making labor laws more flexible could increase employment in stores by 22% on average. This is substantial: the retail sector is India’s second largest employer, providing jobs to 9.4% of workers. Similarly, a study in Brazil finds that enforcement of rigid labor regulations limits firm size and reduces employment.³

Employment regulations are needed to allow efficient contracting between employers and workers and to protect workers from discriminatory or unfair treatment by employers. In its indicators on employing workers, *Doing Business*

measures flexibility in the regulation of hiring, working hours and dismissal in a manner consistent with the conventions of the International Labour Organization (ILO). An economy can have the most flexible labor regulations as measured by *Doing Business* while ratifying and complying with all conventions directly relevant to the factors measured by *Doing Business*⁴ and with the ILO core labor standards. No economy can achieve a better score by failing to comply with these conventions.

Doing Business supports the ILO core labor standards—the 8 conventions covering the right to collective bargaining, the elimination of forced labor, the abolition of child labor and equitable treatment in employment practices. Respect for these standards helps create an environment in which business can

TABLE 4.1

Where is it easy to employ workers—and where not?

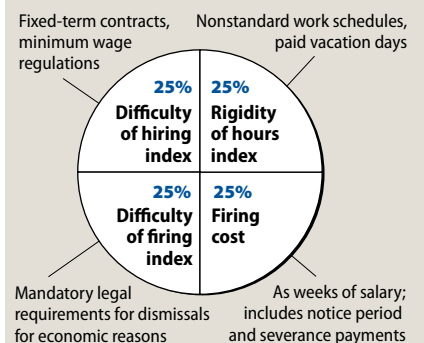
Easiest	RANK	Most difficult	RANK
United States	1	Panama	172
Singapore	2	Sierra Leone	173
Marshall Islands	3	Angola	174
Maldives	4	Congo, Dem. Rep.	175
Georgia	5	Guinea-Bissau	176
Brunei	6	Paraguay	177
Tonga	7	Equatorial Guinea	178
Australia	8	São Tomé and Príncipe	179
Palau	9	Bolivia	180
Denmark	10	Venezuela	181

Note: Rankings are the average of the economy rankings on the difficulty of hiring, rigidity of hours, difficulty of firing and firing cost indices. See Data notes for details.

Source: *Doing Business* database.

FIGURE 4.2

Rankings on employing workers are based on 4 subindicators



Note: See Data notes for details.

FIGURE 4.3

Rigid labor regulations are associated with high informality and high unemployment

Note: Relationships are significant at the 1% level for size of the informal sector and at the 10% level for female unemployment, and remain significant when controlling for income per capita.

Source: *Doing Business* database; WEF (2007); World Bank, World Development Indicators database.

develop. *Doing Business* does not measure compliance with them, however, and these 8 conventions are not reflected in the employing workers indicators. This year's report shows which of the 8 conventions have been ratified by each of the 181 economies it includes (see table on ratification status of the 8 ILO conventions regarding core labor standards, page 147). Ratification of the core labor standards is not necessarily a good indicator of compliance. A measure of compliance is being developed under the *Doing Business* project for future inclusion in the employing workers indicators.

Governments all over the world face the challenge of finding the right balance between worker protection and labor market flexibility. Denmark, for example, seeks to reconcile job flexibility with employment security through "flexicurity." Employers face no regulations against laying off workers for economic reasons. They only provide advance notice. More than 80% of workers belong to a voluntary unemployment insurance scheme.⁵ Workers benefit from the flexible regulations, which give them the opportunity for a job in the formal sector and easy transitions from one job to another. Indeed, more than 70% of Danes think it is good to change jobs frequently.⁶

But in developing countries especially, regulators often err to one extreme—pushing employers and workers into the informal sector. Across developing economies, overly rigid labor regula-

tions are associated with a larger informal sector⁷ (figure 4.3). This pattern is evident in Venezuela and Bolivia. Both have laws that ban dismissing workers on economic grounds and are among the economies with the most rigid employment regulations (table 4.1). And both are among the 5 economies with the largest informal sectors (41% of GDP in Venezuela, 43% in Bolivia).⁸

In the end, workers in the informal sector lose out the most. They are generally paid lower wages and enjoy no legal protections or social benefits. The most vulnerable groups, women and young workers, are often at the greatest disadvantage. A study in Indonesia finds that if it had enjoyed the same flexibility in labor regulations as Finland, for example, its unemployment rate might have been 2.1 percentage points lower and, among young people, 5.8 percentage points lower.⁹

Finding the right balance can be difficult, but the quest is worth it. Another recent study looks at the effects of labor regulation in Latin America, using survey data for 10,396 firms in 14 countries.¹⁰ Firms were asked how many permanent workers they would hire and how many they would dismiss if labor regulations were made more flexible. The analysis suggests that the result would be an average net increase of 2.1% in total jobs. Firms with fewer than 20 employees benefit the most, with average gains of 4.2%.

Flexible labor regulations also en-

courage entrepreneurship. Two recent studies suggest that flexible regulations increase the probability of start-ups by about 30%.¹¹ The researchers offer 2 explanations. For employees, lower job security makes starting their own business attractive. For entrepreneurs, the greater flexibility in running a business makes business ownership more attractive.

Reforms making labor regulations more flexible also may increase industrial production and reduce urban unemployment. In the Indian states of Andhra Pradesh and Tamil Nadu such reforms increased manufacturing output by 15%. In West Bengal, by contrast, reforms making labor regulations more rigid cut output by 20%.¹² The estimated result: 1.8 million more urban poor in West Bengal.¹³

WHO REFORMED IN 2007/08?

Fifteen economies made significant changes to their labor regulations in 2007/08. Six economies increased flexibility; 9 reduced it. Eastern Europe and Central Asia introduced the most reforms increasing flexibility, followed by Africa and Latin America and the Caribbean (table 4.2).

Burkina Faso was the most active reformer, adopting a new labor code that replaced its 2004 code. Employees and employers can now determine the weekly rest day without having to seek the approval of the authorities. And employers may be encouraged to take greater risks in hiring new workers thanks to increased flexibility in using fixed-term contracts and less rigid dismissal procedures. For example, strict priority rules, including seniority, no longer apply in dismissing workers for redundancy.

Azerbaijan was the second most active reformer. Working hours became more flexible, with restrictions on night work now applying only where labor conditions are hard or hazardous. Before the reform, an employer could dismiss a worker for economic reasons only if the worker could not be reassigned to another position. That requirement is

TABLE 4.2

Easing restrictions on fixed-term contracts—a popular reform feature in 2007/08

Eased restrictions on fixed-term contracts	Azerbaijan, Burkina Faso, Mozambique, Slovenia
Made working hours more flexible	Azerbaijan, Burkina Faso, Czech Republic
Reduced dismissal costs	Argentina, Mozambique, Slovenia
Removed requirements for dismissal	Azerbaijan, Burkina Faso
Made dismissal more difficult	Cape Verde, China, Fiji, The Gambia, Italy, Kazakhstan
Increased restrictions on fixed-term employment	Korea, Sweden
Increased paid annual leave	United Kingdom

Source: *Doing Business* database.

gone. Specific notification and approval requirements for redundancy were also eased. And as in Burkina Faso, fixed-term contracts can now be used for any task. On the basis of the new labor code, Azerbaijan now ranks among the 10 economies with the least rigid employment regulations as measured by *Doing Business* (table 4.3).

Mozambique's new labor law also increased flexibility in the use of fixed-term contracts. It reduced the notice period for dismissals, from 90 days to 30. And it introduced phased reductions in severance pay.

In Eastern Europe, Slovenia and the Czech Republic provided for greater flexibility in using employment contracts. Slovenia now permits employers to extend fixed-term contracts from the statutory 24 months to the duration of a project. It also reduced the notice period for dismissals from 75 days to 60. The Czech Republic introduced flexibility in overtime hours, probationary periods and length of the workweek. In addition, its amended labor code simplified the working hours account, allowing choice in the distribution of working hours over a 4-week period.

Continuing the trend toward greater flexibility in Eastern Europe, the former Yugoslav Republic of Macedonia is in the final stages of passing a new labor relations law that will increase flexibility in working hours and reduce dismissal costs for redundancies. The new provisions will allow flexible use of fixed-term contracts, increasing their maximum duration from 4 years to 5. It will also

eliminate restrictions on weekend work and ease constraints on the dismissal of redundant workers.

In Latin America, Argentina reduced the severance payment for a worker with 20 years of seniority from 30 months to 20. After its unemployment rate fell below 10%, a 2007 decree abolished the 50% increase in severance payments that had been part of the 2002 "emergency laws."

Reforms in East Asia and Pacific were a mix, both increasing flexibility and reducing it. China introduced new priority

rules for group redundancy dismissals, making it more difficult for employers to adjust during economic downturns. In Fiji new legislation strengthened protections against discrimination in employment and shifted dispute resolution from litigation to mediation. But it also introduced new notification requirements for dismissals and reduced the flexibility of working hours by imposing a limit of 48 hours in a 6-day workweek.

Among OECD high-income economies, Korea introduced important provisions on equality of opportunity and nondiscrimination in hiring and promotion. It also limited fixed-term contracts to 24 months.

Several economies made employment regulations more rigid. Kazakhstan now requires employers to first transfer an employee to another job when considering redundancy. Italy increased the notice period for dismissal of workers from 2 weeks to 75 days, The Gambia from 2 months to 6 and Cape Verde from 30 days to 45. Sweden reduced the maximum

TABLE 4.3

Who makes employment workers easy—and who does not?

Rigidity of employment index (0–100)			
Least		Most	
Hong Kong, China	0	São Tomé and Príncipe	63
United States	0	Angola	66
Singapore	0	Equatorial Guinea	66
Maldives	0	Guinea-Bissau	66
Marshall Islands	0	Panama	66
Australia	3	Congo, Rep.	69
Azerbaijan	3	Niger	70
Uganda	3	Congo, Dem. Rep.	74
Canada	4	Bolivia	79
Jamaica	4	Venezuela	79
Firing cost (weeks of salary)			
Least		Most	
Denmark	0	Equatorial Guinea	133
New Zealand	0	Mozambique	134
United States	0	Ecuador	135
Puerto Rico	0	Sri Lanka	169
Afghanistan	0	Ghana	178
Iraq	0	Zambia	178
Marshall Islands	0	Sierra Leone	189
Micronesia	0	Zimbabwe	446
Palau	0	Bolivia	NOT POSSIBLE
Tonga	0	Venezuela	NOT POSSIBLE

Note: The rigidity of employment index is the average of the difficulty of hiring index, rigidity of hours index and difficulty of firing index.

Source: *Doing Business* database.

duration of fixed-term contracts from 3 years to 2. The United Kingdom increased the paid annual leave to which workers are entitled from 20 working days to 24.

WHAT ARE THE REFORM TRENDS?

Across the world, *Doing Business* has recorded only 77 reforms affecting the employing workers indicators since 2004. Of the 77 reforms, 47 made labor regulations more flexible; 30 made them more rigid. Labor reforms are rare. This is unsurprising. Governments work on such reforms for years, and there are many stakeholders involved. Labor reforms normally imply a tripartite consultation—between government, employers’ representatives and workers’ representatives. Finding the right balance of interests is a challenging and important exercise.

MOVING TOWARD MORE FLEXIBLE REGULATIONS

Governments in Eastern Europe and Central Asia have been the most active reformers in the past 5 years, introducing 19 reforms increasing the flexibility of labor regulations (figure 4.4). OECD

high-income economies follow with 16, with Australia, Germany and Switzerland all reforming more than once.

In Africa, Uganda (in 2006), Mozambique (in 2007) and Burkina Faso (in 2008) enacted new labor laws, introducing worker protections while increasing the flexibility of labor regulations. Namibia (in 2004) eased restrictions on working hours. Yet among regions, Africa continues to have the most rigid labor regulations. Dismissal costs for a worker with 20 years of employment amount to more than 3 years of salary in Sierra Leone and more than 8 years in Zimbabwe. Africa is also home to the countries with the largest numbers of mandatory paid annual leave days: Eritrea with 34, Ethiopia with 33 and Cameroon with 32.

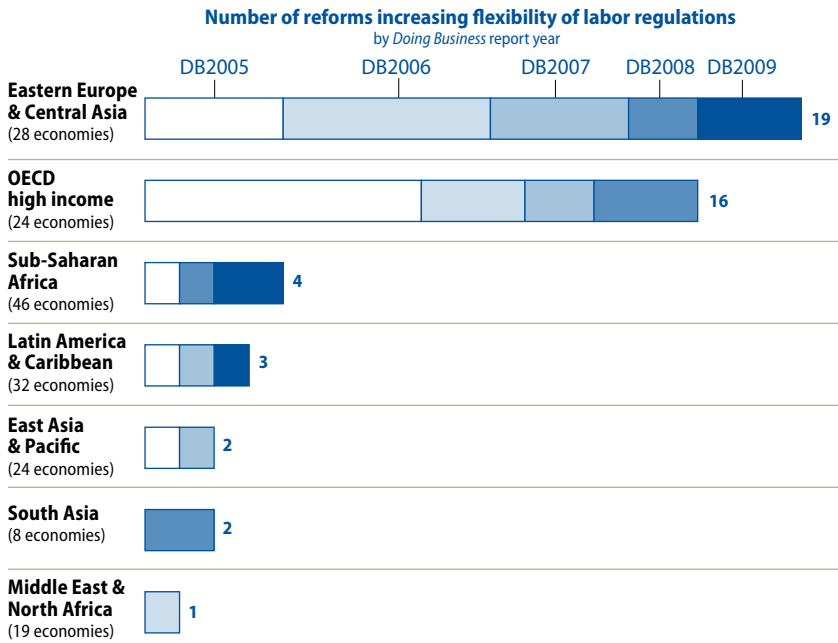
Three reformers stand out in Eastern Europe and Central Asia. Slovakia (in 2004) and Azerbaijan (in 2008) introduced flexibility in the use of fixed-term contracts, in work schedules and in redundancy requirements. Georgia made big changes in those areas in 2005 and 2006 and also introduced changes in notice periods and severance payments.

Reform was widespread: 8 of the 10 countries in the region that have joined the European Union have reformed their labor laws. Several, including Lithuania and Romania, did so to harmonize their laws with EU legislation.

In South Asia 2 economies have reformed. Bhutan went far, implementing its first labor code in 2007. The new labor code established protective measures for workers without imposing heavy burdens on employers. The protections created incentives for workers to join the private sector—and employers now have a larger pool of candidates to choose from. The better working conditions have led to higher productivity.¹⁴

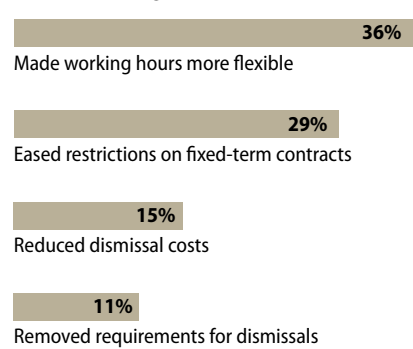
In Latin America, Colombia and Argentina made labor regulations more flexible. Both made redundancy dismissals easier—Colombia in 2004 and Argentina in 2005. Argentina also reduced dismissal costs in 2007. In East Asia and Pacific, Vietnam eased restrictions on fixed-term contracts, and Taiwan (China) on working hours. Except for Israel, no economies in the Middle East and North Africa made labor regulations more flexible.

FIGURE 4.4 Most reforms in Eastern Europe & Central Asia



Note: A reform is counted as 1 reform per reforming economy per year. Source: *Doing Business* database.

FIGURE 4.5 Top 4 reform features in employing workers Reforms including feature since DB2005 (%)



Note: A reform may include several reform features. Source: *Doing Business* database.

INCREASING FLEXIBILITY IN SETTING HOURS AND USING CONTRACTS

Over the past 5 years 36 reforms have been aimed at increasing flexibility in working hours and the use of fixed-term contracts (figure 4.5). Five reforms have made scheduling working hours more difficult. Nine have restricted the use of fixed-term contracts.

Most of the reforms aimed at increasing flexibility in working hours took place in Eastern Europe and Central Asia. These reforms, concentrated in 2004 and 2005, allowed more flexible arrangements for overtime and permitted businesses to shift working hours from the low to the high season. In Latvia and Poland working hours must balance out within 4 months; in Hungary, within a year. Overtime hours have become more predictable for employees, and employers can more easily adjust to cyclical demand. Elsewhere in the world, Pakistan eased limits on overtime, while Uganda allowed employers and employees to freely set the legally required rest day. Bhutan eased restrictions on night work.

Sixteen economies allowed greater flexibility in the use of fixed-term contracts. In Azerbaijan and Burkina Faso, for example, fixed-term contracts can now be used for permanent tasks. Latvia and Togo extended their maximum duration. That makes it easier for both employers and employees to adapt work arrangements to their needs.

REDUCING DISMISSAL COSTS

Ten economies granted businesses more flexibility in dismissals during economic downturns. But 15 economies (including Bolivia, Fiji, Kazakhstan and Zimbabwe) made such dismissals costlier or more difficult. In Bolivia and Venezuela an employer cannot let workers go for economic reasons without their consent. Under these circumstances employers might think twice before hiring a new worker.

High dismissal costs can deter employers from creating jobs in the formal sector. That argues for reducing dismissal burdens. But excessive flexibility leads to another problem: concern among existing employees about losing their jobs and being left without a safety net.

One solution is to offer unemployment insurance rather than severance pay. In Austria employers contribute to a fund from which they may withdraw if a worker is made redundant after 3 years of employment. In St. Kitts and Nevis severance payments are made from a government-administered fund that employers pay into over time. In Italy employers deposit a portion of each employee's salary into a designated fund over the course of the employment relationship. In Korea employers adopting the new defined contribution plan will contribute 1 month's salary annually to each employee's private pension account.

Chile adopted a successful unemployment insurance system in 2002. The reform introduced individual savings accounts to which both employee and employer contribute. It also reduced severance pay from 30 working days to 24 for each year worked. Unemployed Chilean workers receive benefits from their individual savings accounts for 5 months.

NOTES

1. This example is from the World Bank's *Doing Business: Women in Africa* (2008a), a collection of case studies of African entrepreneurs.
2. Amin (forthcoming).
3. Almeida and Carneiro (forthcoming).
4. ILO Convention 14 on weekly rest (industry), ILO Convention 171 on night work, ILO Convention 132 on holidays with pay and ILO Convention 158 on termination of employment.
5. Data on the share of the labor force covered by unemployment insurance, from Clasen and Viebrock (2008), are for 2002.
6. Eurobarometer (2006).
7. Djankov and Ramalho (2008). A 10-point increase in the rigidity of employment index is associated with an increase of 0.9% of GDP in the size of the informal sector.
8. Djankov and Ramalho (2008).
9. Feldmann (2008).
10. Kaplan (forthcoming). The study uses data from the World Bank Enterprise Surveys, available at <http://www.enterprisesurveys.org>.
11. Van Stel, Storey and Thurik (2007) and Ardagna and Lusardi (2008).
12. Aghion and others (forthcoming).
13. Besley and Burgess (2004).
14. Wangda (forthcoming).