

# Analyses Économiques

vol. VI-03 (Oct. 2007)

## The Newsletter of the French Council of Economic Analysis

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### EDITORIAL

## Working Time, Income and Employment

Report by Patrick Artus, Pierre Cahuc and André Zylberberg

France is benefiting from globalisation, despite negative public opinion in this respect. The emergence of Asian and Central European countries is creating new export opportunities that are working to France's advantage. Imports from emerging countries are enabling French consumers to purchase every-day consumer goods at lower prices and resulting in substantial gains in spending power. France could, nonetheless, gain more from globalisation. The purpose of the contributions in this report is to identify the ways and means of attaining this objective. The goal is to combine transversal policies with measures of a more sector-specific nature. All sectors, including services and intangible products, are now affected by globalisation. Whilst the challenges are transversal and global, the potential solutions are likely to vary not only from one country to another—as some are at a more advanced stage than others—but also from one sector and one company to another.

**Christian de Boissieu**  
Executive Chairman of the CAE

France is not succeeding in mobilising its labour resources efficiently. Per capita income is 30% lower in France than in the United States. The difference corresponds almost exactly to the gap between these two economies in terms of the per capita number of hours worked. The reason for the shortfall in hours worked in France is twofold: i) the high level of non-employment and ii) the reduction in the length of working time.

In their report, Patrick Artus, Pierre Cahuc and André Zylberberg examine the means of organising and regulating the length of working time.

The first step is to pinpoint the economic grounds for public sector intervention in this field. The authors then provide explanations as to why the regulation of working time has never resulted in the creation of jobs. In more specific terms, they analyse the results of the reduction in the length of working time and then address the issue of overtime—notably with respect to taxation—and Sunday opening. The report is backed up by a wealth of empirical research based on findings both in France and abroad.

Patrick Artus, Pierre Cahuc and André Zylberberg conclude with the following recommendations: the simplification of French regulations—leaving much of the responsibility to sector-based collective bargaining; the testing, on a limited scale, of reduced mandatory welfare contributions on overtime; and greater flexibility in legislation governing Sunday opening.

The report was presented to the French Prime Minister, Dominique de Villepin, and to the Minister for Economy Finance and Industry, Thierry Breton, during the CAE meeting held on 6<sup>th</sup> March 2007. This letter, written under the responsibility of the permanent team, summarises the main conclusions.

Effective legislation requires transparent, well-defined and attainable targets. Continuity is also another major wager of effectiveness. In the opinion of Patrick Artus, Pierre Cahuc and André Zylberberg, French legislation governing working time fails to take account of these requirements. Over the last twenty years all that legislation has done is to accumulate devices that are constantly amended and, in the end, prove hard to apply. The accumulation of devices is partly attributable to the frequent changes in the targets set. Between the early 1980s and 2002, French legislation has been geared to the objective of “work sharing”. According to this concept, the economic machine engenders a fixed number of jobs which can be “shared”

between the working-age population via the reduction in the length of individual working time. Attempts to achieve compatibility between the shortest possible working time—for the purposes of sharing work—and the flexibility that companies need to organise their workforce have led to a highly complex legislative structure. Since 2002, the pendulum would appear to have swung. More recent thinking is that those who wish to increase their working time should be given the possibility to do so, if they so wish. As a result, part of the legislative patchwork has been “unravelling”, although the main fabric has been left in tact. This has hardly enhanced its transparency or effectiveness.

## What are the goals regarding the regulation of working time?

French working time legislation continues to hamper the domestic economy. For example, according to the Amcham barometer released in 2006, 93% of Americans who invest in France consider the restrictions on working time to be a drawback and 84% take the same view of the flexibility and organisation of working time. There is now an urgent need to anchor French working time regulations upon several simple principles that can be understood by all and that will enable economic agents to establish lasting relations. In order to achieve this goal, it is imperative that agreement is reached over the targets at which such regulation is aimed. By and large, four frequently-mentioned objectives are, in principle, conceivable:

- working time legislation ought to protect the health of workers and prevent them from being overexploited. This objective warrants the introduction of a maximum working time limit and special treatment for night shifts;
- working time legislation ought to provide for free time spent with others. Limiting the possibilities of working during certain periods, Sunday for example, would pave the way for improved coordination of work schedules;
- working time legislation could be used to create jobs by fostering work sharing via a reduction in the length of working time;
- working time legislation could constitute a means of enhancing the value of work via the introduction of incentives to work over and above the legal working time limits by increasing overtime rates and reducing mandatory welfare charges on overtime worked.

Patrick Artus, Pierre Cahuc and André Zylberberg provide comments and analysis of each of these four objectives. The first two objectives correspond to the prime goal of working time regulation: i.e. the protection of workers and the facilitation of the coordination of work schedules.

The third objective is based on a false perception of the way in which the economy functions and should be abandoned in no uncertain manner. The fourth objective is aimed at enhancing the value of work via financial incentives. However, incentives can have positive or negative consequences. For instance, the impact of the revision to overtime pay rates in terms of employment and total income is not clear cut. Regardless of the form that it takes, special tax treatment for overtime will not necessarily prove beneficial to employment and total income and entails two risks: i) a deterioration in public finances; and ii) an increased complexity of the taxation system. This sort of measure ought to be avoided. It does not constitute an effective means of enhancing the value of work. Broadly speaking, the report recommends that working time legislation should be limited to the first two objectives –namely protecting workers and improving the coordination of work schedules. A number of potential solutions to achieve these objectives are proposed.

The report is broken down into four sections. The first section provides a summary of macroeconomic trends in working time, employment and income. The second casts light upon the arguments used to justify the regulation of working time. The third section explodes the myth that jobs can be created by ill-adapted adjustments to such regulations. The fourth and final section provides a detailed account of the authors' recommendations.

## Sharp reduction in the annual length of time worked by full-time waged workers

The reduction in the length of working time is a long-term trend. The annual length of working time fell sharply worldwide between 1950 and the early 1980s –with a slowdown or even stop in some countries, the United States for example, from this period onwards.

In France, the annual length of time worked tumbled from 2,024 hours in 1960 to 1,434 hours in 2005. The introduction of the 35-hour working week accentuated the pace of the reduction in working time compared to France's main trading partners. Between 1998 and 2004, the annual average length of time worked by employees fell by 1%, on an annual basis, in France, versus declines of 0.1% in the United States, 0.2% in Spain, 0.4% in the United Kingdom and 0.9% in Germany. More significantly, the sharp reduction in the annual average length of working time in France concerned full-time employees, whereas, in the other countries mentioned, the reduction was caused by growth in part-time employment. Unless there is a major difference in terms of hourly productivity, per capita income in a country where the average length of time worked is lower than elsewhere will be less substantial. Per capita income in France is 30% lower than in the United States due to lower utilisation of labour resources. As almost half the relative weakness in the number of per capita hours worked in France is attributable to the low length of time worked by full-time employees, the latter does account to a large extent for the income differential between France and some of its key trading partners.

There is little doubt that French regulation has played a major role in the sharp decrease in the average length of working time and, by the same token, the decline in relative income levels. However, it is sometimes argued that French regulation and the resulting consequences might stem from a "choice of society". It is possible that the French, like many of their European peers, have a stronger preference for leisure than Americans. This theory is both true and false. A large number of surveys on the subject show unquestionably that the majority of the French population does not wish to work longer hours, but that there is a significant minority prepared to sacrifice its free time in order to

earn more money. One of the challenges that will have to be met in order to achieve effective regulation is the taking into account of these differences.

## Ensuring that free time is spent with others

The low proportion of salaried employees who work on Sunday –and at the weekend in general– is most probably due to the fact that the value of free time depends upon the possibility of spending it with family or friends and having the opportunity of taking part in collective activities. The benefit derived from free time is related to what others do. Within the family circle, time spent together plays an extremely important defining role, not only for children but also for adults. Without precise rules, it can prove difficult to coordinate work schedules in order to spend free time with others or to take part in collective activities. Regulation aimed at defining periods of free time spent with others or on collective activities offsets "market shortcomings". The partial or total ban on Sunday work is a good example of this.

The decision to ban or authorise Sunday work must also take account of the major differences that exist in terms of individual circumstances. The advantages reaped via enhanced value of leisure time for various categories of the population need to be weighed up against the disadvantages for other categories of the population who want to work on Sundays or whose free time would be more beneficial if they had access to shopping facilities. Analysis of opinion polls on Sunday opening reveals the strong divergence of opinion among socio-demographic categories. To make a sweeping generalisation, the typical person in favour of Sunday opening is young, lives in a large town or city and has a modest social background.

The objective of coordinating working schedules, preserving the possibility of spending free time with family or friends and of taking part in collective

activities, must make allowance for a constant result of empirical analysis: Sunday opening creates a significant number of jobs in the retail trade sector. Appropriate legislation must achieve a balance between apparently contradictory requirements.

### Can the length of working time be used as an instrument for creating jobs?

A common sense solution for creating jobs immediately springs to mind: if the amount of working time is reduced, work can be shared. In reality, research conducted for more than ten years in several countries and based on tens of thousands of observations shows that the theory that a reduction in the length of working time creates jobs has no empirical validity. The authors of the report are insistent on this point: to date, there are no examples of well-founded research which prove that a reduction in the length of working time leads to job creations. Empirical analysis indicates that the Aubry reforms, which introduced the 35-hour working week, probably resulted in job creations. However, such analysis also suggests that these job creations were due to the reduction in welfare contributions on low wages and increased workplace flexibility. At best, the reduction of the statutory working week played a marginal role.

### Can overtime be used as a means of boosting income?

The reduction of the length of working time no longer arouses much interest. The focus of attention has shifted to the reduction in the surcharge and welfare contributions on overtime, aimed at boosting income and enhancing the value of work. However, there is nothing to suggest that such measures are likely to result in the attainment of these objectives. On the contrary, they will render legislation more complex and

could prove excessively costly, in terms of public finances. In addition, the impact on employment and income is highly uncertain.

A reduction in the surcharge on overtime results in increased private sector demand for overtime and in the use of overtime as a replacement for new jobs –which is detrimental to employment and total income. The negative effect is nonetheless offset by the reduction in the total cost of labour<sup>(\*)</sup>. In theoretical terms, the impact of an increase in the surcharge on overtime is therefore not clear-cut: it depends on the technology of a given company and on the sensitivity of demand to the price of its products. Empirically, current estimates of the various technological and demand-related parameters do not constitute a fail-safe method for assessing the impact on employment. Patrick Artus, Pierre Cahuc and André Zylberberg do not therefore consider a reduction in the cost of overtime to be a reliable strategy for increasing employment and income.

A reduction in the mandatory contributions on overtime increases the spending power of those who work over and above the statutory working hours. On the flip side, however, the financing of the reduction in these contributions reduces the income of salaried employees who do not accept overtime. Moreover, this measure has a negative impact on employment as it encourages companies to resort to overtime rather than take on new labour. All in all, the impact on employment and income of the reduction in mandatory contributions on overtime is far from certain when the financial costs involved are taken into account. But this is not the crux of the matter: one of the major disadvantages of this type of

(\*) These only concern employees who earn the minimum wage. Regarding other categories, flexibility in annual earnings cancels, in the long term, variations in the surcharge on overtime.

measure is that it could encourage “opportunistic” behaviour. It is in the joint interest of employers and employees to reduce (or not increase) the hourly wage rate on standard hours and to make false statements that a large amount of overtime has been worked (this is very difficult to check) in order to take advantage of the tax concessions. This phenomenon is admittedly unlikely to occur in the immediate future. Longer term, however, the real length of time worked will not change and public finances will be badly hit by the measure.

### A few recommendations

The statutory length of working time is a central issue in terms of the regulation of working time. However, the benefits of setting a statutory length of working time that has to be implemented throughout France have not been proven on an economic level. Moreover, the system has not been adopted in several European countries, such as Germany, Denmark and the United Kingdom, which are governed exclusively by statutory lengths of working time. In contrast, if one takes a more general view of the principles of life in society, the setting of a statutory length of working time can be justified, as it constitutes a potential means of achieving a “standard” length of full-time working time. The statutory length of working time can thus provide a standard or reference to orientate ways of living. The right to express an opinion as to whether the statutory length of working time should be maintained or abolished is not reserved exclusively to economists.

The legal definition of the standard length of working time does, by no means, take all the issues related to the regulation of working time into account. From this point of view, the wealth of information accumulated on this subject militates for the re-orientation of French legislation to attainable targets –namely the protection of workers and the development of free time spent

with others. The refocusing of French working time legislation on these two objectives implies drastic simplification based on the following proposals:

- legislation could be restricted to the setting of a maximum length of working time and the periods when work is authorised or limited, in accordance with existing legislation on the maximum length of daily and weekly working time and night shifts. Decisions concerning the number of hours above which overtime is payable, overtime quotas, the surcharge on overtime and compensatory leave should be *exclusively* based on collective bargaining;

- in the event that a statutory length of working time is maintained:

- it must go hand in hand with a single rate of surcharge for overtime worked that can be modified and adjusted by collective bargaining agreements;

- statutory overtime quotas for every geographical area of France and all sectors of activity (currently 220 hours per annum) are not justified –either by the objective of protecting the health of workers or by the goal of preventing the exploitation of workers. These objectives should be defined under legislation on maximum authorised working time. Compensatory leave and overtime quotas should be *exclusively* established through collective bargaining;

- tax reductions on overtime ought to be avoided. These are difficult to implement and can give rise to fraudulent practices. The cost in terms of public finances is high and the impact on employment is uncertain.

The question of Sunday opening is not an issue reserved exclusively for economists. It also depends on choices of life in society and, as a result, the decision ought to be made at the political level. Economic analysis, nonetheless, sheds some light upon the situation. Empirical research at our

disposal shows that the extension of Sunday opening hours abroad has systematically created jobs. It also has advantages for consumers as they have greater flexibility as to when they do their shopping. That said, the drawbacks must not be underestimated: the risk of a loss in the market share of small local shopkeepers, negative impact on the quality of life of some staff members and store managers, greater difficulty in coordinating work schedules. The authors of the report believe that two potential solutions (not necessarily exclusive) for maximising the advantages and minimising the drawbacks may be envisaged:

- to allow Sunday opening, but to give every employee the right to refuse to work on this day;
- to decentralise the system for authorising Sunday opening. Current legislation gives little power to local authorities. In practice, the mayor can grant the authorisation to open on Sunday for a maximum of five Sundays a year. Public opinion on the subject varies considerably from one geographical area to another. Legislation giving local authorities the right to decide whether Sunday opening should be authorised –or otherwise– would provide a more effective way of catering for differences of opinion. In this respect, the simplest solution would be to no longer restrict the mayor's

power to grant dispensations to open to a limited number of Sundays set in advance.

## Comments

Gilbert Cette's comments focus on five points. Firstly, he notes that the reduction in the length of working time (RTT) meets a social demand, as reflected by the manner in which productivity gains have been shared between increases in income and in free time over the long term. He considers that an increase in the employment rate, notably as far as senior citizens and young persons are concerned, takes top priority with respect to mobilising labour resources more efficiently. In Gilbert Cette's opinion, the impact of RTT on production costs is a crucial issue which has not been given due consideration, on an empirical level, in the report. He then makes a number of observations on the transition to the 35-hour working week in France. It would appear that production costs have not been pushed up substantially (at least as far as concerns workers who earn more than the minimum wage (SMIC)), which implies that RTT might have resulted in job creations. Gilbert Cette agrees with the authors about the need to simplify legislation on working time. He advocates the extension of a contractual dispensatory right, supervised and organised by majority agreements. Recourse to this type of right could also be made in the case of Sunday work regulations, the scope of which is not limited to Sunday opening. Gilbert Cette shares the scepticism of the authors regarding exoneration from welfare contributions on overtime.

Michel Godet welcomes the explosion of the myth that sharing work creates jobs. He is entirely in favour of developing part-time work – which could bolster the employment rate of senior citizens– and Sunday work – which creates jobs. Michel Godet draws attention to the fact that the effective number of hours worked accounts for the income differential between France and the United States. Productivity is a misleading indicator as it takes more account of the capacity of an economy to exclude the least highly-performing members of the population than of its potential to create wealth. On the subject of overtime, Michel Godet notes that he is one of the leading advocates of a lightening of the tax burden via income tax, but is more circumspect about the reduction in welfare contributions.

In Gilles Saint-Paul's opinion, the report has two main merits. Firstly, it calls the concept of work sharing into question. Secondly, it recommends ending State involvement in working time regulation. The decision-making process should be focussed on the identification of market shortcomings –in order to find appropriate measures to improve market efficiency– rather than on coercive regulations. Gilles Saint-Paul consequently suggests the creation of an in-house overtime market, responsible for determining the optimal surcharge on overtime, within each company. He is not convinced by the recommendation of decentralising decisions with

respect to the length of working time; pay rate increases or overtime quotas. There is nothing to guarantee that these measures will not work to the advantage of insiders rather than to that of outsiders and jobs. Gilles Saint-Paul concedes that there is some economic logic behind the exemption of overtime from tax, but points out that this could also lead to additional distortions due to the threshold effect. He is not convinced by the authors' arguments concerning the need to coordinate work schedules to justify restrictions on Sunday opening.