
THE CORRELATION OF WAGES WITH INFLATION RATE AND APPLICATION OF THE PERFORMANCE CRITERION

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Abstract

The field of work relations is regulated by the Labor Code. In the course of the working relations, the participants in the employment relations, the employees and the employers are informed and consult each other, under the law and the collective labor agreements for the good functioning of the labor relations, because both participants are interested in realizing the rights on the one hand, and a favorable financial result, on the other.

The clause on wage correlation with the inflation rate is frequently included in collective labor agreements. Concurrently, the parties agree on wage increases by applying the performance criterion. In the case of inclusion of these clauses in the collective labor agreements, without the practical application, labor conflicts may arise.

To provide a basis for negotiating wage increases by applying the two criteria, I illustrate some practical ways to apply this article.

Keywords: *social protection, wages correlation, performance criterion, labor conflict, inflation rate.*

JEL Classification: E24, E31

Introduction

According to the provisions of art. 41, paragraph 2 of the Romanian Constitution, employees have the right to social protection measures regarding the security and health of the employees, the working regime of women and youth, the establishment of a minimum national salary, the weekly rest, paid rest and other specific situations.

In a democratic society, the restriction of some rights or freedoms, if necessary, can only be done by law.

The Labor Code and Collective Labor Agreements regulate labor relations and labor jurisdiction.

At the time of the conclusion of collective labor agreements, the parties are equal to expressing the claims of the rights claimed in the case of employees and the possibilities of granting them, if we refer to employers.

By signing a collective labor agreement, it becomes the law of the parties.

In the practice of litigation and labor disputes, collective conflicts are often encountered, which have come to justice, ultimately damaging both parties.

The wage growth clauses are sometimes too poorly expressed, or when applied, it is noted that the social dialogue partners considered different ways of applying.

Literature review

Compensation of wages with the consumer price growth index was approached by Carp (2017). In order to avoid labor conflicts, the author proposed the existence of a set of definitions of terms used in collective labor agreements.

The methodology for calculating the index of consumer price growth and its concept, definitions and calculation methods are presented by Anghelache, Marinescu, Lilea, Stoica (2017).

Methods and models of inflation measurement are extensively analyzed by Anghelache, Voineagu, Gheorghe (2013).

The possibilities for increasing wage and pension income were addressed by Anghelache, Carp (2016), and Carp (2017) presented the correlation between gross average wage and pensions.

The concept of clearing contract was promoted by Kanagaretnam, Sarkar (2011).

Anghel, Anghelache, Carp (2017) illustrated the correlation between the main macroeconomic indicators and the models built on them.

Gheorghiescu, Schmutzer (2016) presented case studies based on court rulings in disputes and labor disputes.

Research methodology, data, results and discussions

▪ Collective labor agreement

In accordance with the provisions of Article 229 of the Labor Code, the collective labor agreement is the written agreement concluded between the employer or the employers' organization on the one hand and employees represented by trade unions or otherwise provided by law on the other side which lay down clauses on:

- working conditions
- salaries
- other rights and obligations arising from employment relationships.

Collective bargaining agreements that last for two years usually include clauses on wage correlation and salary increases.

By correlation, the employer and the employees are considering keeping the same wage purchasing power throughout the lifetime of the collective labor contract. The reason for including this clause is rising prices, inflation rates.

The second clause, which is included in the Payroll section, is to provide salary increases. These are conditioned by the favorable development of the employer's financial situation.

Salary increases are granted in the form of wage increases for all employees, or for certain employees.

The stimulation of professional development, the performance of service duties in favor of the employer, determines employers to include the performance criterion as a criterion for granting salary increases. This means that in order to benefit from wage increases, an employee competes with himself and with other employees.

When collective labor agreements include several wage clauses, they are executed in turn, requiring a prioritization of the criteria, a consecutive enforcement order.

▪ **Labor conflicts**

The Labor Code and the Social Dialogue Law define labor conflicts. These are usually generated by the execution or non-execution of certain clauses stipulated in the Collective Bargaining Agreement or in the individual labor contract, as the case may be.

In the event of conflicts between employees and entrepreneurs „concerning the economic, professional or social interests or the rights resulting from the labor relations”, they take the form of labor conflicts (art.231-Labor Code). Law No. 62 / 10.05.2011 of social dialogue defines these terms and illustrates the situations that generate collective labor disputes.

Inappropriate fulfillment of the obligations arising from individual and collective labor contracts generates conflict. Employees may be directed against the employer for payment of damages, being considered prejudiced by the failure to grant rights.

▪ **Correlation of wages with inflation rate**

As early as 1991, the concept of „compensation-indexation of basic salaries” was introduced in Romania, due to the fact that salaries negotiated through collective / individual labor contracts were depreciated in relation to the evolution of consumer prices.

In the Romanian wage system two methods were applied: compensation and indexation of salaries.

Wage correlation targets one of the two methods.

When no provision is made in the contractual clause, we understand that by correlation with the inflation rate, we have in mind a compensation procedure with the inflation rate so that the salary has the same purchasing power throughout the life of the individual labor contract, related to the clause in the collective labor agreement.

If the contractual parties do not provide for a correlation between wages, it follows that the correlation process is continuous and as a consequence any increase in prices must result in the payment of a monetary compensatory amount.

Because inflation is measured monthly, rising inflation rates lead to monthly wages that are payable to employees.

If the parties provide for periodic salary adjustments, quarterly or yearly, then the resulting amounts may be included in the basic salary, resulting in increases in other salary items.

A method of correlating distinct compensation salaries is indexing, which consists of a direct increase of each salary by applying a percentage increase to basic salary.

In my opinion, indexing is a wage increase process that is regularly applied, usually annually.

Salary compensation and indexing are current methods of correlating wages.

To calculate the amount of compensation to which the base salary is correlated, the relationship (1):

$$Compensation = \frac{Sthe\ initial\ wages * Inflation\ rste}{100} \quad (1)$$

unde:

$$Inflation\ rate = IPC - 100 \quad (2)$$

The advantage of correlating wages with the inflation rate is that for all employees, amounts proportional to the basic salary are granted..

▪ **Performance criteria and wage increases**

Assessing the performance of employees in the performance of their duties is an employer's right provided for in Article 40 (f) of the Labor Code. Performance criteria and evaluation methods may be subject to internal rules. In order to stimulate the increase in the achievement of individual service tasks, employers can set individual performance targets and criteria to assess their achievement.

The performance criterion may be included in a clause in the collective labor contract for wage increases. In this case, employees are directly interested in obtaining a grade / grade for higher wage growth.

Concurrent application of several criteria for salary increases involves the establishment of a calculation algorithm, the approval of an employer-employee method leading to the same wage increases.

▪ **Case study. Applying the criterion of correlation with the inflation rate and applying the performance criterion**

To illustrate how to apply the two criteria, we present a case study.

Either a company that has concluded a Collective Labor Agreement for the period July 2017-June 2019. According to the provisions of art. 100, after each calendar year the wage correlation will be correlated with the inflation rate, based on the consumer price indices communicated by NIS. The first year expires in June 2018.

Under the provisions of Article 101, the company will grant salary increases of 2% per annum on the performance criterion, according to annual assessments. The so-called salary increases are granted from July each year. After the first year of work, human resources management awarded grades from 1 to 10 depending on the performance criteria being met by each employee.

The company has not established the concrete way of applying the criteria, so there may be different methods of calculating new base salaries. Since the first year of the CCM 2017-2019 expired, salary increases are required under Article 100 and Article 101.

Knowing that the CPI June 2018 / June 2017 is 105.41% and knowing the grades obtained by the employees, we will determine the salaries to be paid on 01.07.2018.

As stated in the introductory part of the study, when there is no concrete way of applying the clauses, there may be different outcomes.

It is assumed that the company has a number of 10 employees, numbered in the table from a1 to a10.

In relation to the performance criterion and the total salary fund existing on 01.07.2018, the employees have the amount of 720 lei to be distributed to each employee. This criterion is stimulating for the a6 employee, whose share is 19.44%, while the employee a1 receives only 2.78% of the total wage bill growth. In terms of the performance criterion, the new wages payable to employees are in column 10.

Method no. 1:

The two criteria, the correlation with the inflation rate and the performance criterion, are applied separately.

According to this method, it is considered that both salary increases, ie the percentage shares in column 4 and the CPI (inflation rate of 5.41%) in column 7, apply simultaneously to the same salary base (initial salaries in column 3).

According to the results of the calculations, the total salary increases amount to 2668 lei. The new salaries payable to the employees are in a gross amount of 38,668 lei.

Angajati	Nota evaluare	% notei	Fond salarii	Cota procentuala Sal./FSA L	Suma acordata (dupa perf.)	Cota criteriu perf	IPC	Sal. compensat (dupa IPC)	Compensatia cu IPC	Sal. Criteriu perf	Crestere salariala totala
col.0	col.1	col.2	col.3	col.4	col.5	col.6	col.7	col.8	col.9	col.10	col.11
a1	8	10.00%	1000	2.78%	72	7.20%	105.4	1054	54	1072	1126
a2	9	11.25%	2000	5.56%	81	4.05%	105.4	2108	108	2081	2189
a3	10	12.50%	3000	8.33%	90	3.00%	105.4	3162	162	3090	3252
a4	6	7.50%	5000	13.89%	54	1.08%	105.4	5271	271	5054	5325
a5	7	8.75%	6000	16.67%	63	1.05%	105.4	6325	325	6063	6388
a6	8	10.00%	7000	19.44%	72	1.03%	105.4	7379	379	7072	7451
a7	9	11.25%	5000	13.89%	81	1.62%	105.4	5271	271	5081	5352
a8	10	12.50%	3000	8.33%	90	3.00%	105.4	3162	162	3090	3252
a9	7	8.75%	2500	6.94%	63	2.52%	105.4	2635	135	2563	2698
a10	6	7.50%	1500	4.17%	54	3.60%	105.4	1581	81	1554	1635
	80	100.00%	36000	100.00%	720	2.00%	105.4	37948	1948	36720	38668
Total crestere:				720							
Diferenta inflatie:				1948	Total crestere		2668				

Method no. 2:

The performance criterion is first applied, followed by the criterion of correlation with the inflation rate.

According to the results of the calculations, the total salary increases amount to 2707 lei. The new salaries payable to the employees are in gross amount of 37,948 lei

Angajati	Nota evalu-are	% notei	Fond salarii	Cota procentu a Sal_1/FSA L	Suma acordata (dupa perf.)	Cota criteriu perf	Sal. Criteriu perf	IPC	Sal. Corelat cu IPC	Crestere salariala totala
col.0	col.1	col.2	col.3	col.4	col.5	col.6	col.7	col.8	col.9	col.10
a1	8	10.00%	1000	2.78%	72	7.20%	1072	105.41	1130	130
a2	9	11.25%	2000	5.56%	81	4.05%	2081	105.41	2194	194
a3	10	12.50%	3000	8.33%	90	3.00%	3090	105.41	3257	257
a4	6	7.50%	5000	13.89%	54	1.08%	5054	105.41	5327	327
a5	7	8.75%	6000	16.67%	63	1.05%	6063	105.41	6391	391
a6	8	10.00%	7000	19.44%	72	1.03%	7072	105.41	7455	455
a7	9	11.25%	5000	13.89%	81	1.62%	5081	105.41	5356	356
a8	10	12.50%	3000	8.33%	90	3.00%	3090	105.41	3257	257
a9	7	8.75%	2500	6.94%	63	2.52%	2563	105.41	2702	202
a10	6	7.50%	1500	4.17%	54	3.60%	1554	105.41	1638	138
	80	100.00%	36000	100.00%	720	2.00%	36720	105.41	37948	2707
Total crestere:				720	Total crestere		2707			
Diferenta inflatie:				1948						

Metoda nr.3:

The two criteria apply separately. According to this method, it is considered that both salary increases, ie the percentage shares in column 4 and the CPI (inflation rate of 5.41%) in column 7, apply simultaneously to the same salary base (initial salaries in column 3).

The employer considers that for employees a1 and a10 correlated salaries with the inflation rate because salaries calculated according to the first criterion are lower than salaries related to the inflation rate.

Employees a2-a9 are paid the wages in column 9. The union notes that this option, favorable to the employer, is a proposal that leads to a state of conflict.

Thus, employees a2, a3 and a8, who obtained grades 9 and 10 in grades, benefit from salary increases of 5.41%..

	Nota evalu-are	% notei	Fond salarii	Cota procentu a Sal_/FSA L	Suma acordata (dupa perf.)	Cota criteriu perf	Sal. Criteriu perf	IPC	Sal. Corelat cu IPC	Crestere salariala totala
Angajati	col.1	col.2	col.3	col.4	col.5	col.6	col.7	col.8	col.9	col.10
a1	8	10.00%	1000	2.78%	72	7.20%	1072	105.41	1054	1072
a2	9	11.25%	2000	5.56%	81	4.05%	2081	105.41	2108	2108
a3	10	12.50%	3000	8.33%	90	3.00%	3090	105.41	3162	3162
a4	6	7.50%	5000	13.89%	54	1.08%	5054	105.41	5271	5271
a5	7	8.75%	6000	16.67%	63	1.05%	6063	105.41	6325	6325
a6	8	10.00%	7000	19.44%	72	1.03%	7072	105.41	7379	7379
a7	9	11.25%	5000	13.89%	81	1.62%	5081	105.41	5271	5271
a8	10	12.50%	3000	8.33%	90	3.00%	3090	105.41	3162	3162
a9	7	8.75%	2500	6.94%	63	2.52%	2563	105.41	2635	2635
a10	6	7.50%	1500	4.17%	54	3.60%	1554	105.41	1581	1581
Total	80	100.00%	36000	100.00%	720	2.00%	36720	105.41	37948	37966
Total crestere:				720						
					Total crestere	1966				
Diferenta inflatie:				1948						

Conclusion

In a collective labor contract it is necessary to have uninterpretable clauses.

Correlation of wages with inflation is in principle a compensation with the consumer price growth index, so a method of granting a salary amount, calculated as the difference between the actual value with the CPI of the basis on which it is applied, ie the salary and the value initially outdated. Indexing is the result of a percentage increase in salary.

If, apart from correlation with the inflation rate, other criteria for wage increases were also provided, the priority of the criteria and the algorithm for their application are established.

Clauses in a collective labor contract generating wage rights can not be waived, making all clauses mandatory.

By the calculation methods shown, it can be concluded that in the absence of a clear algorithm for the application of the correlation criteria and salary increases, there may be different results.

When the partners signing a collective labor agreement reach different outcomes, the only way to avoid a labor dispute is to initiate a social dialogue. In the author's view, calculation method 1 corresponds to an objective understanding of the clauses taken as a benchmark in our analysis.

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