



Australian Fair Pay Commission

Executive Summary

July 2008

Executive summary

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The *Workplace Relations Act 1996* (WR Act) assigns the Australian Fair Pay Commission (Commission) an overarching objective 'to promote the economic prosperity of the people of Australia'. To achieve this objective, the Commission must have regard to the following criteria in performing its wage-setting function:

- the capacity of the unemployed and the low paid to obtain and remain in employment;
- employment and competitiveness across the economy;
- providing a safety net for the low paid; and
- providing minimum wages for junior employees, employees to whom training arrangements apply and employees with disabilities that ensure those employees are competitive in the labour market.

As in previous years, the Commission invited submissions to its 2008 Minimum Wage Review to address some or all of the criteria. In addition, the criteria guided the Commission's consultations with stakeholders, and its internal and external research programs.

Views were sought directly through submissions and a range of consultations, including focus groups, online bulletin boards and meetings with key stakeholders in each state and territory. The Commission also drew on the available data and research literature in considering the impact of its previous decisions.

The Commission has implemented a robust and transparent process to monitor the effects of its decisions. Some of the main insights have been collated in the Commission's first *Economic and Social Indicators - Monitoring Report*, published in February 2008.

This third general Wage-Setting Decision, like its predecessors, is informed by the research evidence available to the Commission at the time of writing. In addition, the Commission considers a range of information included in the Australian Government Budget, Reserve Bank of Australia (RBA) statements and recent business surveys.

The Commission has conducted a wage review and now exercises its wage-setting function as set out in s. 22(1) of the WR Act.

The Commission grants a general pay increase that will adjust the standard Federal Minimum Wage (FMW) and Australian Pay and Classification Scales (Pay Scales) as follows:

- an **increase** of \$21.66 per week (\$0.57 per hour) to the standard FMW, bringing the weekly rate to \$543.78. The standard FMW increases from \$13.74 to \$14.31 per hour; and
- an **increase** of approximately \$21.66 per week (\$0.57 per hour) in adult¹ Pay Scales.

The general Wage-Setting Decision 2008 takes effect from the first pay period on or after 1 October 2008.

¹ Where adult means a basic periodic rate of pay that does not explicitly apply to a class of employees with a disability or employees to whom a training arrangement applies or junior employees.

Executive summary

The general Wage-Setting Decision 2008 will flow on to junior employees, employees to whom training arrangements apply, employees with disabilities, casual employees, and basic piece rates of pay in ways that preserve existing relativities to the extent this is possible.

The general Wage-Setting Decision 2008 only adjusts minimum rates of pay in special FMW's, the standard FMW and Pay Scales. This increase may be offset against any equivalent amount in rates of pay received by employees whose actual wages are determined by above minimum Pay Scale arrangements.

In making this Decision, the Commission has sought to balance a range of key trends and developments in the economy, including inflation, employment conditions and factors affecting the safety net for low-paid workers.

The Commission has been especially cognisant of the financial pressures on low-income households at this time. Movements in consumer prices, in particular, have put many low-income households under considerable financial stress. While most submissions to the Commission raise this issue, there is no agreement on forecasts of inflation.

Submissions also raise the impact of changes to the tax and transfer systems, including those announced in the Australian Government's 2008-09 Budget. Some argue that these changes should be taken into account in assessing household income for low-paid workers in a variety of family circumstances, while others maintain that they should not be taken into account.

The Commission agrees that low-income households have been adversely affected by recent movements in consumer prices. It considers that the quantum of the increase awarded reflects the Commission's focus on the circumstances of low-paid Australians.

The Commission considers that this increase of \$21.66 per week, together with relevant tax and transfer changes, will provide low-income households with real increases in disposable income.

While the Commission has placed emphasis on the role that minimum wages play in maintaining a safety net for low-paid people, it has not ignored the potential for the increase awarded to add to inflationary pressures. However, the Commission believes the inflationary impact of its Decision will be relatively minor.

The Commission also believes the impact on employment and unemployment will be relatively minor in the context of current economic circumstances. The Commission will continue to monitor the impacts of its Decision closely.

Unlike previous decisions, the Commission's general Wage-Setting Decision 2008 is not a differential decision and therefore applies to all minimum rates of pay in Pay Scales. The Commission is aware that continuing to award differential increases could overlap, duplicate or even conflict with parts of the award modernisation process currently being undertaken by the Australian Industrial Relations Commission.

Executive summary

The capacity for the unemployed and low paid to obtain and remain in employment

To date, strong growth in the economy has delivered solid employment outcomes to a broad cross section of the working-age population. Unemployment has continued to decline for most groups, including those identified as more disadvantaged in the labour market.

The Commission notes that the economic outlook is uncertain. Economic activity and employment growth are forecast to slow in the near term, while unemployment is expected to increase. These weaker conditions may place low-paid workers in a more vulnerable position.

In monitoring labour market outcomes for low-skilled people and the relevance of minimum wages, the Commission examines transitions into and out of low-paid employment. While there is evidence of upward earnings mobility for both unemployed people and low-paid employees, a sizeable proportion of low-paid employees is likely to 'churn' between low-paid jobs and unemployment, or out of the labour force, or remain in low-paid employment over time.

The Commission regards labour market transitions as an important dimension of the experiences of low-paid and unemployed people. Setting minimum wages too high could exacerbate churning between low-paid employment and unemployment, reducing the chances of people moving into better-paid jobs.

In considering the capacity of unemployed and low-paid people to obtain and remain in employment, the Commission notes the effect of minimum wages on labour supply. It is important that unemployed people have adequate incentives to take up low-paid work and that people in low-paid work are encouraged to maintain their employment.

The Commission's monitoring indicates that on a range of measures the incentive for unemployed people to move into work has either been stable or improved in recent years. In addition, the most recent tax cuts will improve marginal incentives for many low-paid workers to increase their earnings.

Employment and competitiveness across the economy

The Australian economy performed strongly over the past year, recording solid growth in economic activity and employment. Wage pressures have generally been contained to date. However, inflation accelerated through 2007, prompting the Australian Government and the RBA to act to restrain aggregate demand.

Over the year to May 2008, unemployment fell in most states and territories, with the exception of Western Australia and Queensland, which already had comparatively low unemployment rates, and South Australia. Broader measures of labour underutilisation also point to an improvement in labour market performance.

Assessments of the underlying trends in labour costs vary in submissions to the 2008 Minimum Wage Review. Some consider that wage growth has been generally steady, while others are concerned by a gradual acceleration in wages since early 2007.

Executive summary

Most submissions regard the Wage Price Index (WPI) as the most accurate measure of underlying wage growth.² The WPI increased by 4.1 per cent over the year to March 2008, similar to the annual rates recorded over the previous two years.³ Higher wage growth appears to have been contained to those segments of the economy with skill shortages or already low unemployment rates.⁴

Wage growth in collective agreements reached in each quarter over the past three years has been steady. The most recent data indicate that the average annualised wage increase (AAWI) in all wage agreements current in the March quarter 2008 was 4.0 per cent, while the AAWI for new agreements was 3.7 per cent.⁵

Consistent with a tight labour market, recent data indicate that wage growth has been firm across most industries. However, there are some variations around the aggregate trend, with some Pay Scale reliant industries experiencing high rates of wage growth, and others recording slower growth.

The Commission will continue to monitor the effects of minimum wages on particular industries. As part of this monitoring, the Commission will undertake a series of detailed industry profiles.

While most submissions acknowledge the recent solid performance of the economy, they vary on the outlook. The Australian Government updated its view of the economic outlook in May 2008. It forecasts that economic activity will slow to a moderate pace, with employment growth slowing quickly over the next year. The unemployment rate is expected to increase to 4¾ per cent by mid 2009.⁶

The headline Consumer Price Index (CPI) demonstrated some volatility over the past eighteen months, ranging from a year-ended increase of 1.9 per cent in the September quarter 2007 to 4.2 per cent in the March quarter 2008. The RBA's measures of underlying consumer price inflation discount extreme changes in prices. Even so, this measure increased by an average of 4.3 per cent over the year to the March quarter 2008, which was well above the RBA's medium term inflation target band of 2 to 3 per cent per annum.

The RBA forecasts that the inflation rate will peak at 4½ per cent through the year to December 2008, before declining to 3¼ per cent by December 2009.⁷ By comparison, the Australian Government considers that inflation will have peaked in the March quarter 2008 before steadily declining.

Both the RBA and the Australian Government highlight the opposing influences on future growth and inflation, and the uncertainty that remains. On the one hand, slower global growth and tighter credit conditions are expected to reduce domestic activity, while on the other hand, large rises in Australia's terms of trade will boost national income.⁸

² For example, ACTU, *Australian Council of Trade Unions Submission to the Australian Fair Pay Commission*, March 2008, p. 37; and ACCI, *2008 Minimum Wage Review*, ACCI Submission, March 2008, p. 58, para. 2.94.

³ ABS, *Labour Price Index*, Australia, Catalogue No. 6345.0, Canberra, March 2008.

⁴ Australian Government, *Submission to the Australian Fair Pay Commission Minimum Wage Review 2008*, 14 March 2008, p. 6, para. 2.7.

⁵ DEEWR, *Trends in Federal Enterprise Bargaining*, March Quarter 2008, <<http://www.workplace.gov.au/workplace/Publications/ResearchStats/Agreement/TrendsInFederalEnterpriseBargaining.htm>> at 20 June 2008.

⁶ Commonwealth of Australia, *Budget Paper No. 1: Budget Strategy and Outlook 2008-09*, Canberra, AGPS, 2008, p. 2-6.

⁷ RBA, *Statement on Monetary Policy*, 9 May 2008, <<http://www.rba.gov.au/PublicationsAndResearch/StatementsOnMonetaryPolicy/index.html>>, at 12 May 2008, p. 68.

⁸ Commonwealth of Australia, 2008, p. 2-3. RBA, May 2008, p. 68.

Executive summary

The Commission notes that there is general agreement that inflation will decline over the period to October 2009. However, there is disagreement over when and at what level inflation will peak. The Commission has taken into account the range of estimates and the uncertainty surrounding the outlook for inflation in making its Decision.

The Commission acknowledges that minimum wage increases may affect wider wage growth in the economy and therefore inflation. However, it considers that the direct effect of a moderate increase in minimum wages on aggregate inflation is likely to be minor. Wages paid to employees who are directly reliant on the Commission's decision comprise only a small percentage of the economy's total wage bill.

There can also be indirect effects from minimum wage adjustments, as they flow on (in one form or another) from minimum wage decisions to wages set under other instruments. However, the available evidence on the size of these effects is limited.

Including both direct and indirect effects, and considering historical wage-price relationships, the Commission estimates that the 2008 minimum wage adjustment may increase prices by up to 0.4 per cent over the medium term.

On balance, the Commission believes that its general Wage-Setting Decision 2008 to increase minimum wages by \$21.66 per week will have only a minor impact upon aggregate wage and inflation outcomes in the economy as a whole.

Providing a safety net for the low paid

The Commission considers that the Australian income safety net comprises minimum wages, tax benefits and income support payments. While the Commission is responsible for setting and adjusting the first of these components, the Australian Government is responsible for the remainder.

By definition, the safety net concept is primarily concerned with the living standards of people at the lower end of the income distribution. The Commission therefore focuses its attention mainly on those households that rely most heavily on minimum wages, either alone or in combination with income transfers.

The Commission does not favour a formulaic approach to balancing the respective contributions of tax/transfer changes and wage increases to disposable income. Nor does it believe that tax/transfer changes should be completely ignored, since their effect on disposable income can be significant.

Recently legislated changes to income tax for the 2008-09 financial year will benefit lower-income Australians. The combination of tax/transfer changes, and lower effective marginal tax rates (EMTRs), means that low-paid employees who benefit from the Commission's general Wage-Setting Decision 2008 will retain, on average, more than three-quarters of their gross pay increase.

The Commission also considered a wide range of disposable income modelling. The modelled scenarios covered a range of family types, with one or two earners, employed at various points in the Pay Scale distribution. Two different inflation scenarios, corresponding with Australian Government and RBA forecasts, were also used to predict future values of income transfers.

Executive summary

The modelling shows that, whether eventual inflation is at the lower (Australian Government) estimate or at the higher (RBA) estimate, all household types modelled will experience a real increase in disposable income in October 2008, when the Commission's minimum wage increase comes into effect, relative to their income one year previously.

Many submissions express a concern that low-income employee households spend a higher percentage of their income on items experiencing higher inflation, than other households. The Australian Council of Trade Unions highlights increases in interest rates, rents, childcare and health care costs, among others, as contributing to financial stress.⁹

The CPI increased by 4.2 per cent in the year ended March quarter 2008. There is considerable diversity within the CPI. For example, prices for the food component increased by 5.7 per cent; housing by 5.7 per cent; and transportation by 6.8 per cent, with clothing and footwear prices decreasing by 0.5 per cent.

In any given period, the prices for some items will be increasing faster than those for other items. The CPI is able to take these variations into account by weighting the items according to household expenditure patterns. Preliminary analysis by the Commission indicates that there would be on average only minor differences between expenditure-weighted CPIs for low-income employee households and all households.

In considering the impact of movements in consumer prices on the living standards of low-income households, the Commission acknowledges that it is appropriate to use a variety of benchmarks.

The Commission's modelling finds that all households earning the standard FMW have disposable incomes well above the Henderson Poverty Line. Moreover, all households receive above 60 per cent of median equivalised household disposable income, except for single-earner couples with two children and not taking up Newstart Allowance.

The Commission will continue to monitor relevant Australian and international research, including that published by the Organisation for Economic Co-operation and Development.

The Commission is confident that the minimum wage increase of \$21.66 per week, in combination with the 2008-09 tax cuts and regular indexation of transfer payments, will provide the great majority of workers earning Pay Scale wages with household disposable incomes in October 2008 that are higher in real terms than in October 2007.

Employees with a disability

The Commission has decided to adjust the minimum weekly amount payable to employees with a disability under the Supported Wage System to retain its nexus with the income-test free threshold of the Disability Support Pension – increasing this from \$66 to \$69 per week.

The Commission will also undertake monitoring and evaluation focusing on wage outcomes under different wage assessment tools.

⁹ ACTU, March 2008, p. 105, para. 10.1.

Executive summary

Impact of the drought on farm businesses in regional Australia

The Commission's general Wage-Setting Decision 2007 deferred the 2007 general wage increase for some employees in the drought-affected agricultural sector.

The Commission considers that the need for a continued deferral of wage increases for employees of employers in the agricultural industry receiving Exceptional Circumstances Interest Rate Subsidy (ECIRS) has declined to the extent that no further deferral is necessary.

In accordance with Wage-Setting Decision 4/2007, the deferral of the general Wage-Setting Decision 2007 for employees of employers in the agricultural industry receiving ECIRS will cease on 1 October 2008.

Casual loadings

The Commission notes that its general Wage-Setting Decision 2008 flows on to casual employees through adjustments to the basic periodic rates of pay (or as otherwise specified where Pay Scales provide for different methods of compensating casual employees).

The Commission notes that, as a result of the passage of the *Workplace Relations Amendment (Transition to Forward with Fairness) Act 2008*, it can no longer adjust the default casual loading percentage of 20 per cent for employees covered by the standard FMW, the special FMW for employees with a disability, or a workplace agreement.

The Commission will not adjust casual loadings expressed as a percentage contained in preserved Pay Scales.

Where preserved Pay Scales provide a flat dollar amount for casual employees, these rates will be increased to give effect to the general wage increase.

Piece rates

The Commission will flow on the general Wage-Setting Decision 2008 to basic piece rate Pay Scales by applying a 4.15 per cent increase to basic piece rates in preserved Pay Scales which are not otherwise increased as a result of the general Decision.

However, recognising the diversity within basic piece rate Pay Scales, an affected person or business may make a submission to the Commission on the grounds that such an adjustment would result in an anomalous outcome inconsistent with the Commission's intention to flow on the general increase to piece rate workers.

Preserved pay equity and work value wage increases under section 208(4)

Section 208(3) of the WR Act prohibits a preserved Pay Scale from including automatic pay increase mechanisms. However s. 208(4) provides an exception by preserving future pay increases in an instrument where these increases were 'wholly or partly on the ground of work value change or pay equity'.

A number of submissions seek an exemption from the Commission's general Wage-Setting Decision 2008 for the preserved Pay Scale derived from the Social and Community Services (State) Award [NSW] (SACS Pay Scale). This exemption is sought on the ground that the SACS Pay Scale retains an increase of 3.5 per cent which will take effect on 1 July 2008 as a result of the operation of s. 208(4).

Executive summary

The Commission considers that, consistent with its view in 2007, it is not possible to identify the proportion of the relevant increase that is attributable to the separate elements of work value and safety net.

To give effect to this intention, the Commission grants a partial exemption from the general Wage-Setting Decision 2008 for the SACS Pay Scale.

Consistent with its Decision in 2007, the Commission intends that the higher wage increase of either this general Wage-Setting Decision 2008 or any increase already received on 1 July 2008 as a result of the operation of s. 208(4) will apply.

Discrimination

The Commission received a number of submissions addressing discrimination and pay equity issues in the Australian labour market.

Submissions generally argue that vulnerable groups are over-represented among low-paid employees. Several submissions address a wide variety of factors affecting vulnerable employees, including economic and social issues which lie beyond the Commission's remit.

A number of submissions raise the issue of gender pay equity, focusing on the gap between male and female earnings. They argue that the Commission should more explicitly refer to pay equity when making its wage-setting decisions.

While data suggest there is less of a gender pay gap among the lowest-paid Australians, the Commission believes that further investigation is warranted.

Future directions

Section 24 of the WR Act provides that, in performing its wage-setting function, the Commission may inform itself in any way it thinks appropriate including by 'monitoring and evaluating the impact of its wage-setting decisions'.

Drawing on recommendations received from two research reports commissioned in 2007,¹⁰ the Commission has put in place a monitoring framework that will inform its deliberations and its future decisions.

The Commission is committed to strengthening and refining its monitoring capability, and will seek out all available expertise and information sources in order to fill any gaps in the coverage and scope of its monitoring activity.

¹⁰ J Healy and S Richardson, *A Strategy for Monitoring the Micro-Economic and Social Impacts of the Australian Fair Pay Commission*, National Institute of Labour Studies, report commissioned by AFPC, 2007; Access Economics, *Monitoring Strategy for Wage-Setting Decisions*, report commissioned by AFPC, 2007.

Executive summary

In addition to research undertaken for monitoring purposes, the Commission conducts short-term and long-term research on a range of issues relating to the four criteria guiding minimum wage adjustments. Some of this research has informed this Decision. As it becomes available, additional research will inform the deliberations of the Commission regarding future minimum wage decisions. The Australian Fair Pay Commission Secretariat (Secretariat) will undertake further consultation with stakeholders and seek advice on priority areas of research to assist in informing the Commission's decisions on research directions and priorities.

Proposals for further research put forward in submissions will be considered by the Commission's Research Advisory Committee (RAC).

In particular, the Secretariat will continue to consult the RAC, through which stakeholders can provide advice on the future research agenda. For the first time in 2008, the Commission has benefited from representation on the Committee of all state and territory governments. This will ensure these jurisdictions' research priorities are considered alongside those of other private, public and community sector organisations.

In order to enhance access to quality research and expertise on minimum wages, the Commission will convene its first annual Minimum Wage Research Forum in October 2008. Australian and overseas researchers will present and discuss papers commissioned on a range of topics. The Forum will be an opportunity for researchers and stakeholders to exchange ideas and compare findings.

The Commission will publish proceedings from the Minimum Wage Research Forum following the event. These proceedings will be disseminated widely to inform discussion and debate on aspects of minimum wage-setting in Australia.