



ACOSS Submission to the AIRC National Wage Case

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The Australian Council of Social Service (ACOSS) has sought and been granted leave to intervene in a number of National Wage Cases since 1996. While we do not claim any special expertise in the area of industrial relations or wage fixation, we have an interest in the adequacy of living standards and the quality of life of low-income Australians. There has always been a close relationship between wage fixation, poverty alleviation and the social security system in Australia.

A fair safety net of minimum wages and conditions of employment is essential to stem the increase in poverty and income inequality and preserve work incentives for jobless people. Minimum wages should assist low-paid workers to meet basic needs and keep in touch with wider living standards without jeopardising the economy or jobs growth.

There is no evidence to suggest that recent minimum wage increases have weakened employment growth. Indeed, the official unemployment rate has fallen to less than 6 per cent. While the headline unemployment rate underestimates the actual level of enforced joblessness, and many social security recipients still face barriers to employment (such as a lack of skills, high unemployment in some regions, disabilities, and lack of affordable child care), the level of minimum wages is not in our view a major impediment to reducing unemployment further.

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There has been debate recently about the process of fixing minimum wages. We do not normally comment on the process of wage fixation in our submissions, but wish to raise for the Commission's consideration changes to the process that might improve it. A fair and effective wage fixing process is one that gives the parties, governments and other interests a fair public hearing, and independently weighs the arguments, taking account of expert advice. The Commission is well placed to play this role. Any changes to the process should not diminish its fairness and transparency:

- To leave the ultimate decision to Government could politicise the process. Overseas experience suggests that this would increase the volatility of real minimum wages over time, an undesirable outcome for all concerned.
- Proposals to directly involve bodies with other important economic functions, including the Reserve Bank and Productivity Commission, would have to be very carefully considered as this could compromise their other roles.

Weaknesses in the present system could instead be addressed by:

- The establishment by the Commission of a panel of independent experts in economic, employment and social policy to advise it in fixing minimum wages
- Periodically conducting a more in depth review of the economic and social factors impinging on wage fixation, including the basic living costs of wage earners.

As in the past, ACOSS does not have a view on the quantum of increase that should be awarded in 2005. We submit that minimum wages should be increased substantially over time to contain wage inequality and to enable low-paid workers (with the support of the social security system as appropriate) to meet reasonable basic living costs. We respectfully submit that in the short-term, the Commission should increase minimum wages to ensure that they do not fall behind movements in average wage rates. We also propose that in future, the Commission undertake an inquiry to ascertain an appropriate benchmark for the adequacy of minimum wages.

Inequality

A high level of inequality in the distribution of income does matter because it divides the community. Those with very low-incomes struggle to meet their basic needs and participate in society. On the other hand, those at the top are increasingly out of touch with the experience and world-view of the majority of households. Such divisions weaken a society, and ultimately undermine economic efficiency as well because social cohesion is a pre-condition for economic development.

The evidence of deep and growing economic divisions in the Australian community is overwhelming. Since the mid 1970s, the distribution of private income has become substantially more unequal and governments have attempted (without success over the medium to long term) to prevent the gap from growing. This trend has continued over the past decade, led by deepening inequality of private income. Between 1995 and 2001,

the after-tax equivalised incomes of the top 20% of households rose by 14% (\$111 per week), compared with just 8% (\$13 per week) for the bottom quintile and 11% (\$41 per week) for the middle quintile¹.

Wage dispersion is a key part of the income inequality story, since:

- wages comprise the majority of household income;
- wage inequality has been at the heart of growth in household income inequality over the past 20 years.

Earnings inequality in Australia has grown over the last 25 years mainly due to the lowering of real wages at the bottom of the wage distribution scale, together with sharp increases at the top (see table below).

Earnings inequality among full-time employees

	Ratio of bottom to middle wages (10th percentile to median)	Ratio of top to middle wages (median to 90th percentile)
Male full-time employees in 1975	68%	165%
Male full-time employees in 1999	59%	188%
Female full-time employees in 1975	63%	144%
Female full-time employees in 1999	62%	166%

Source: Borland Gregory & Sheehan, *Work rich, work poor*. Victoria University (2001).

Since the 1980s, governments have attempted to cushion the impact of earnings inequality through improvements in social security payments, especially for families with children. These efforts have helped to stem growth in inequality in household disposable income. However, there are definite and legitimate limits to the extent to which governments can continue to play this role in the face of greater wage inequality:

- There is no mechanism (except part-unemployment benefits, to a very limited extent) in place to top up the wages of low-paid single workers without children, who comprise a growing proportion of the population and a large proportion of

¹ ABS (2003) *Revised household income distribution statistics*, in *Australian Economic Indicators*, June 2003

low-paid workers. If the government introduced a payment (or tax concession) for low-paid single workers, it would find itself in the position of directly subsidising employers of low-cost labour generally². This would fundamentally change the role of government and it has wide-ranging social and economic implications, many of them adverse. Such a step should not be taken lightly.

- Increases in government transfers come at a cost. ACOSS considers that this fiscal price is worth paying where it leads to a significant and sustained reduction in poverty. However, if government were to undertake *primary* responsibility for preventing poverty among low wage-earning households (for example, if minimum wages were sharply reduced and the difference was made up by public subsidies), the outcome would be an unsustainable increase in public outlays that would probably fail to significantly reduce poverty.
- No substantive action has been taken in recent years to reduce the impact of earnings inequality (or disposable income inequality) at the upper end of the distribution scale, or to support across-the-board wage restraint in order to boost employment.

Income poverty

The Australian wage fixing system, together with our system of family payments, has been very effective in the past in insulating low-paid workers and their families from income poverty. Although only a small proportion of people in wage-earning households live in poverty today, their number is steadily increasing³.

The most recent data from the National Centre for Social and Economic Modelling, indicates that in 2001, among the 18.9 million individuals in private dwellings in Australia, 11% lived below a poverty line set at 50% of median equivalent household disposable income. This is a very austere poverty line⁴.

- 2% of people living in households whose main income was wages and salaries were in income poverty (so defined),
- but this represented 11% of people in income poverty (approximately 220,000 people, including children)⁵.

Government social security policies have always played a crucial role in reducing poverty, including among wage earning households. However, as we argued above, there are limits to the extent to which we can rely on government action alone to address the problem.

² Governments do this indirectly through the Family Tax Benefit system for low-income families with children. However, a general subsidy for low wages would have a greater impact on the decisions of employers and the Commission. There is a much greater risk that such a payment would be treated as a substitute for wage increases. This would raise the cost for Government, and diminish the benefits for minimum wage earners..

³ To simplify, we use the term "household" here to describe the statistician's concept of "income unit", although in reality there may be more than one income unit in a household.

⁴ This equates to \$194 per week for a single adult, or \$408 per week for a family of four, after tax. Other commonly used poverty lines, the 60% of median income poverty line and the Henderson Poverty Line, are significantly higher.

⁵ Lloyd, Harding & Payne (2004), *Australians in poverty in the 21st century*, NATSEM.

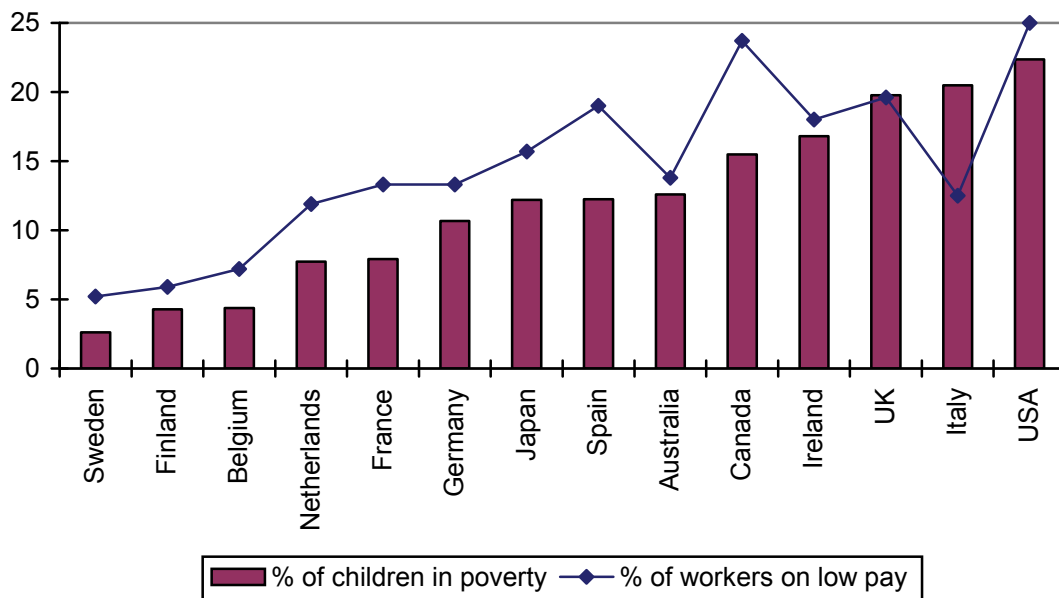
While it is true that government transfer payments are more precisely targeted towards low-income households at risk of poverty, decent minimum wages provide a critical "floor" for the incomes of many low-income households. Without this floor, governments would struggle to prevent widespread poverty among wage-earning households.

Moreover, the argument that these households should rely more on transfers and less on minimum wages to stave off poverty ignores the strong dynamic relationship between minimum wages and social security payments for people of workforce age:

- In countries where minimum wages are relatively low, social security payments are generally also relatively low and poverty rates tend to be high.
- Countries with relatively high minimum wages also tend to have relatively high social security payments and relatively low poverty rates.

This is illustrated by data contained in an international comparative study of child poverty conducted recently for UNICEF. The graph below suggests a strong positive relationship between the incidence of low pay and child poverty rates.

Child poverty and low pay (1990s)



Source: UNICEF (2000), *Child poverty in rich countries*. Florence.

Note: "Workers on low pay" refers to the % of full-time workers on wages less than 2/3 of the median. "Children in poverty" refers to the % of all children living in poor households, with the poverty line based on half median equivalent household disposable income.

This pattern is repeated in other international studies⁶.

One reason for this relationship is that governments preserve work incentives by not allowing benefit levels to come too close to minimum wages. Another way to resolve this work incentive problem in the context of low minimum wages is to extend "in work" benefits (such as our Family Tax Benefit) to low-paid working families. However, in work benefits such as Earned Income Tax Credits are very expensive, if they are made widely available to low income working families. There are fiscal limits to the capacity of governments to raise these payments while still providing adequate social security benefits for those without jobs⁷.

Part time, casual and under-employed workers

Adequate minimum wages are particularly important in sustaining a decent standard of living for the growing number of casual and part-time workers⁸. In addition, intermittent work has become a feature of life for many job-seekers, blurring the previous sharp distinction between employed and unemployed workers (the so-called "insiders and outsiders" of the labour market).

A study of low-paid workers using a longitudinal data set developed by the Australian Bureau of Statistics (ABS) concluded that there was significant movement between joblessness and low-paid employment:

- 13% of low-paid adult workers drawn from a representative sample of the whole population were out of work one year after the reference point for the study (namely, September 1995)
- 29% of low-paid adult workers drawn from a representative sample of people who were jobless four months prior to the reference point of this study (that is, in May 1995), were out of work again one year later (in September 1996)⁹.

The NATSEM income poverty study referred to above estimated that the rate of income poverty among people in households headed by a part time worker is twice that of people in households headed by a full time worker¹⁰.

Along with the social security system, minimum wages are a key foundation for the living standards of this growing body of people who move in and out of employment. Given the tenuous nature of their employment, they are less likely than the majority of workers to benefit from individual or collective bargaining arrangements.

⁶ See Smeeding Rainwater & Burtless, *United States poverty in cross-national context*. Maxwell School of citizenship and public affairs Syracuse University, New York Luxembourg Income study working paper No 244 (2000).

⁷ The United States spends more on its Earned Income Tax Credit for low paid working families than it does on welfare benefits for jobless families. See Moffitt R (2002) *Economic effects of means tested transfers in the US*, NBER Working Paper 8730.

⁸ Australian Bureau of Statistics 1999(a) "Australian Social Trends." 1999.

⁹ Australian Bureau of Statistics (1999), "Labour market outcomes of low-paid adult workers" Catalogue No. 6293.0.00.005.

¹⁰ These estimates include people in households headed by self employed people.

Employment impact of changes in minimum wages

There is no evidence to suggest that recent minimum wage increases have substantially weakened employment growth. Indeed, the official unemployment rate has fallen to less than 6 per cent, about the same level as the United States and other OECD countries with relatively low unemployment. While the headline unemployment rate underestimates the actual level of enforced joblessness, and many social security recipients still face barriers to employment (such as a lack of skills, high unemployment in some regions, disabilities, and lack of affordable child care), the level of minimum wages is not, in our view, a major impediment to reducing unemployment further¹¹.

Although there is a relationship between wage levels and employment growth, there is considerable debate over the likely magnitude of the employment response to any decline in low wages. It has been suggested that deregulating wage setting for low-paid workers would yield only a small increase in employment¹². Others argue that employment growth in Australia has been much less responsive to real wage reductions than was the case in the United States¹³. This suggests that very large reductions in real minimum wages would be required in Australia to substantially reduce unemployment, a conclusion that is reinforced by our experience with wage subsidies for unemployed people. Employers have often been reluctant in the past to take on disadvantaged job-seekers even where half their wage is subsidised by the government¹⁴.

In our view, the Australian evidence suggests that *aggregate* wage restraint will be more effective than reductions in the *relative* wages of low-paid workers in reducing unemployment. Aggregate wage restraint imposed by the Accord in the 1980s contributed substantially to the strong employment growth enjoyed during that economic recovery¹⁵.

On the other hand, there is little or no evidence to suggest that greater *wage dispersion* between different groups of workers has helped reduce unemployment in Australia. The relative value of youth wages has fallen over the past three decades but their employment opportunities have not increased commensurately. In contrast, over the same period women's wage rates have increased relative to those of men at the same time that their employment opportunities have improved. Unemployment has increased over the past 30 years across all skill levels. These *increases* in unemployment have not

¹¹ On hidden unemployment, see ACOSS (2003) *Hidden unemployment in Australia*; On the causes of structural unemployment in Australia see ACOSS (2002), *The Obligation is mutual*.

¹² Borland J and Woodbridge G, "Wage Regulation, Low-wage Workers and Employment" in Richardson S (ed.) "Reshaping the Labour Market: Regulation, Efficiency and Equality in Australia." Cambridge University Press Melbourne 1999

¹³ Gregory, B, Klug, E, Martin YM, "Labour Market Deregulation, Relative Wages and the Social Security System" in Richardson S Ibid.

¹⁴ Department of Employment Education Training and Youth Affairs: "Working Nation - evaluation of the employment, education and training elements." Canberra, 1996 The Working Nation program was the last large scale experiment with subsidising wages to encourage employers to take on long term unemployed people..

¹⁵ Chapman & Gruen, *An analysis of the Australian consensual incomes policy*. Centre for Economic Policy Research Discussion Paper No 221 (1990).

been skewed towards low-skilled workers¹⁶, as we would expect to find if these workers had been priced out of the labour market by high minimum wages¹⁷.

It might nevertheless be argued that if minimum wages were lower, then over the medium to long term more *low skilled full time* jobs would be created here. Australia lost 200,000 low skilled permanent full time jobs over the decade of the 1990s – though the situation appears to have improved significantly since then¹⁸. On the other hand, the number of casual and part time low skilled jobs rose by about 350,000 over the 1990s and has continued to rise since¹⁹. In a sense, this growth in part time and casual jobs mirrors the strong growth in low paid *full time* jobs in the United States until the recession there in 2001.

Could our growth in part time and casual work for low skilled workers be converted into long term growth in full time jobs – as experienced in the United States – if minimum wages were cut? To put this question into perspective, the reduction in our minimum wages required to reduce them to their US equivalents (in purchasing power parities) is very large. Australian minimum wages would have to fall to approximately three fifths of their present value²⁰. To cut minimum wages to the same proportion of median wages that currently applies in the US would probably require an even larger reduction. So, even if this led to a shift in the growth in low skilled jobs in Australia from part time to full time, low skilled workers are unlikely to be better off. A low skilled Australian worker would have to work five days a week at US minimum wages to earn the same gross wage as they would get in three days on Australian minimum wages. Many people would simply end up working more hours for the same wage.

The above studies also indicate that Australia has experienced a long term loss of *middle income full time jobs*. For example, the number of fulltime permanent ‘middle level’ jobs declined by around 240,000 over the 1990s²¹. This would adversely effect low skilled workers to the extent that workers with ‘medium skills’ (for example young skilled workers entering full time employment for the first time and mothers re- entering the labour force) displace those with fewer skills. This suggests that if wage restraint is needed to boost employment over the long term, it should apply to middle incomes as well as minimum wages.

In the short term, there are other more pressing reasons to restrain growth in high and middle level wages. Australia faces a shortage of skilled workers. Until this is addressed by boosting the supply of skilled workers, there is a risk that wages growth among skilled workers will trigger an inflationary spiral. This problem cannot be addressed by curbing minimum wages, as skill shortages are unlikely to occur in occupations directly affected by minimum wages. It would also be unfair to penalise low skilled workers –

¹⁶ Although it is true that this group has *consistently* faced a higher risk of unemployment.

¹⁷ Vickery J (1999), *Unemployment and skills in Australia* Reserve Bank of Australia Research Discussion Paper 1999/12.

¹⁸ Borland et al 2000, *Jobs Rich Jobs Poor*, Victoria University; Keating M, *Wage and income inequality*

¹⁹ Borland et al 2000, *Jobs Rich Jobs Poor*, Victoria University; Keating M, *Wage and income inequality*.

²⁰ See graphs above for Australian and US minimum wage rates, and OECD (2005) *Principal economic indicators*, for purchasing power parities. Note also, that this calculation assumes a 40 hour working week in both countries, which is no longer the case in Australia.

²¹ Borland et al 2000, *Jobs Rich Jobs Poor*, Victoria University

by curbing minimum wages – for problems that arose further up the skill chain. That unfairness would be compounded if wages for skilled employment rise substantially.

While ACOSS believes that aggregate wage restraint is important to help reduce unemployment further, low-paid workers should not bear a disproportionate burden. They are the least able to cope with a decline in their living standards. On the other hand, those on higher market incomes have secured the lion's share of the benefits of the strong economic growth over the past eight years.

Wage restraint should apply across the board, and the skills shortages that could lead to a wages boom should be urgently addressed.

Distributional impact of changes in minimum wages

Some argue that increasing minimum wages is a costly and inefficient way to reduce poverty and income inequality at the level of the household. The basis for this argument is that there is a weak correlation between low wages at the individual level and low-incomes at the household level. For example, the majority of poor households are jobless. Some also argue that most low-paid workers are second earners (either married women or young people) drawn from the top 50% of households.

These arguments are based on empirical work such as Richardson and Harding's study of the relationship between wages and household incomes²². However, it only holds (if it does at all) if retired households are included in the income distribution. This is misleading because household needs vary across the life cycle (and are much lower for most people after retirement), and there will always be a substantial gap between the average incomes of retirees and those of wage-earning households.

A more appropriate basis on which to locate low-paid workers within the household income distribution is to confine the analysis to households of workforce age. If this is done, the majority of low wage-earners clearly fall within the bottom half of the distribution²³.

In any event, the argument that increasing transfer payments is a better way to prevent poverty among low-income working households than raising minimum wages incorrectly assumes that we must choose between one of these two strategies. As ACOSS has argued in previous submissions, this is a false dichotomy. A sustainable reduction in poverty and income inequality requires a balanced approach. Wages should be sufficient for a single person living alone to live decently, and they should be supplemented by social security payments where a wage-earner supports dependents.

Inadequate minimum wages also raise important gender equity issues. The majority of low-paid workers are women, many of whom rely totally on award wage increases. Australia will not make significant progress in reducing the gap between male and female wages without increasing the relative level of minimum wages.

²² Richardson S "Who gets minimum wages?" ANU Centre for Economic Policy Research, Discussion Paper No 386(1998)

²³ The difference between these two measures of household income distribution can clearly be seen in Figure 1 of Richardson's paper cited above.

Moreover, an increase in rates of pay for married women whose husbands are also employed would probably reduce, not increase, household income inequality. This is demonstrated by studies showing that the large increase in (mainly part-time) employment among married women over the 1980s actually *reduced* household income inequality, despite the fact that it was mainly concentrated within two-earner households. One reason for this is that wage inequality among women is much less than that among men²⁴.

Impact of changes in minimum wages on work incentives

A major change in minimum wage levels will have a significant effect on work incentives, all other things being equal. We submit that this, along with the general relationship between the wages and social security systems, should be one of the factors taken into account in setting minimum wages. Otherwise, there is a danger that work incentives will be eroded, or that social security payments will be cut to prevent this outcome - leading to a sharp increase in poverty levels as was the case in New Zealand in the early 1990s²⁵.

At present, *benefit rates* for people of workforce age in Australia are so low that they pose virtually no threat to work incentives. Benefit rates for single unemployed people are particularly low (\$246 per week as at March 2005, which includes the maximum rate of Rent Assistance). A single unemployed adult can expect to roughly double his or her disposable income if they secure a full-time job at the minimum wage²⁶. The gap between the maximum rate of unemployment benefits for a couple and their disposable income if one partner earns the minimum full-time wage is much smaller, but still significant.

On the other hand, *low wages* probably do act as a workforce disincentive for many married women with children whose partners are employed full-time, because their effect is compounded by the following factors:

- Hourly wage rates for women employed part-time are low in both absolute and relative terms.
- Family Tax Benefit and other payments such as Youth Allowance are clawed back as family income increases above a single low full-time wage level, leading to effective marginal tax rates for second earners which often exceed 50% when income tax is also taken into account.
- Child care costs are often prohibitive. The Child Care Benefit leaves large "gap fees" for families to pay.

²⁴ Saunders P: "*Married women's earnings and family income inequality in the eighties.*" Australian Bulletin of Labour Vol 19 (199-217).

²⁵ At the same time that legislation was presented to the New Zealand Parliament (in 1990) to deregulate the industrial relations system, another Bill was presented to substantially cut social security payments for people of workforce age. The connection between these two Bills was explicit: the Government was concerned that reductions in wage levels among low-paid workers would erode work incentives if benefits were not also cut. See Stephens R: "*Budgeting with the benefit cuts,*" in Dalziel P: "*The decent society,*" Wellington, 1994.

²⁶ Based on ACOSS calculations.

To some extent, these work disincentives can be alleviated by reforms to the income tests for family assistance, and improvements in Child Care Benefit. Improvements were made in these areas in 2000 and 2004 and we advocate further change along these lines, especially to ease the harsh impact of the "stacking" of income tests for families in receipt of more than one child payment (for example, Family Tax Benefit and Youth Allowance). However, as argued above there are fiscal and political limits to the extent to which the social security system can be used to compensate for the inadequate incomes of low wage-earning households.

We submit that financial disincentives for married women to undertake part-time employment, as well as pay equity issues, should be taken into consideration in setting minimum wages. These factors both suggest that increases in minimum wages flowing to women in low paid jobs are desirable. If growth in female workforce participation falters in the coming years, then it will become more difficult to sustain economic growth in the face of the ageing of the population.

Benchmarks for adequate minimum wages

In its first "Living Wage" submission in 1997, ACOSS presented a detailed proposal for the establishment of a benchmark for the adequacy of minimum wages that is objectively grounded in research into the living standards and income needs of low-paid workers. We continue to argue for such a benchmark.

In the absence of such a benchmark, we respectfully argue that the Commission would have difficulty fulfilling its responsibilities under section 88B(2) of the Workplace Relations Act (1996) to establish and maintain a safety net of fair minimum wages, having regard to:

- (a) *"the need to provide fair minimum standards for employees in the context of living standards generally prevailing in the Australian community*
- (b) *when adjusting the safety net, the needs of the low-paid.*

Examples from countries such as Ireland, which have established official benchmarks and targets for the reduction of poverty, have highlighted both the social and economic advantages of this action²⁷. The use of such benchmarks and targets is becoming more common in European countries as a result of their adoption by the European Commission²⁸.

We also reiterate our arguments that such a benchmark should:

- be objectively constructed using contemporary social research methods and tested against indicators of actual living standards
- set at a level that enables a single adult living alone to live in "modest comfort" and participate fully in society in accordance with contemporary community standards (that is, a benchmark that is significantly above poverty levels).

²⁷ Nolan B: "Targeting Poverty: The Irish Example." Paper for Social Policy Research Centre Conference University of New South Wales, July 1999.

²⁸ European Commission (2000a) Structural Indicators, Communication from the Commission, COM (2000) 594.

The benchmark should be based on the needs of a single person rather than a family. Although the original Basic Wage introduced following the Harvester judgement was fixed at a level that was just sufficient to prevent a family of four or five from falling into hardship, minimum wages have not been set on this basis for many years. It is more appropriate in present-day conditions for the social security system to meet the additional costs of raising children in low-income families - *provided* family income is underpinned by a minimum wage that is adequate to support the wage-earner²⁹.

In our view, minimum wages should be set significantly above the poverty level for a single person, to provide a decent standard of living and a fair reward for labour, and to preserve work incentives for unemployed people. Minimum wages have been set well above poverty levels for a single adult for many years now, but it is doubtful whether they enable a person to live in modest comfort in accordance with contemporary Australian living standards.

The *Budget Standards Project*, undertaken by the Social Policy Research Centre (SPRC) at the University of New South Wales and commissioned by the former Department of Social Security, (now the Department of Family and Community Services), provides valuable information which could inform the setting of an appropriate minimum wage benchmark. This comprehensive research developed detailed household budgets for a range of family types, sufficient for those households to attain a "Modest But Adequate" or "Low Cost" standard of living. While no single benchmark of living standards should be relied upon exclusively for this purpose, this work could inform the development of appropriate benchmarks for a minimum wage³⁰.

We note that Professor Saunders from the SPRC, in a report on Budget Standards submitted to the Commission, suggests that a benchmark somewhere between the low cost and modest but adequate benchmarks would be appropriate for minimum wage fixation³¹. The modest but adequate standard is defined by Saunders as one that '*affords full opportunity to participate in contemporary Australian society and the basic options it offers*', while the low cost standard represents a level of living which '*may require frugal and careful management but would still allow social and economic participation consistent with community standards*'³².

We agree with Professor Saunders that the Low Cost standard is more appropriate for benchmarking social security payments or measuring poverty, than for wage fixation. However, it is difficult to conceive on what basis a third benchmark 'in between' these two levels would be cast. At the least, this would require very careful consideration of the *purpose* of the proposed standard, the *level of living* to which it corresponds, and how this level could be *clearly distinguished* from both a "Low Cost" and Modest But Adequate' standard.

²⁹ This implies that the wages system and the social security system should together be responsible for ensuring that families with children do not fall into poverty.

³⁰ See Department of Social Security, *Development of indicative Budget standards for Australia*. Research Discussion Paper No 74 (1998).

³¹ Saunders P (2004), *Updated Budget Standard estimates for working families in September 2003*. Report prepared for for the ACTU.

³² *Ibid*, page 4.

Saunders indicates that the Modest But Adequate standard was designed as a 'middle income' standard. His comparisons of Budget Standards with the actual distribution of household expenditures suggest that the updated Modest But Adequate standard was roughly 20% higher than the overall median expenditure level for a lone person household in 2003. However, this includes households of workforce age, and retirees, who are reliant on social security payments. He argues, and we agree, that the more appropriate comparison for wage fixation purposes is with lone person households *in employment*. On this basis, the Modest But Adequate standard was around 80% of the median expenditure for a lone employed person in 2003. If we compare this standard with the median expenditure for lone *full time* workers, this falls to around 75%³³.

This may seem a far cry from the harvester standard established in 1907. It is based on a single adult rather than a family, and on a Modest But Adequate standard rather than the more frugal one (in effect, a poverty benchmark) set by Justice Higgins. On the other hand, the principle enunciated by Higgins J was that the basic wage should meet '*the normal needs of an average employee regarded as a human being living in a civilized community*'³⁴. It is open to conjecture that one of the reasons Higgins J set his benchmark at a 'poverty' standard was that the incomes of *average* production workers were not far removed from a poverty standard at that time (especially given the lack of family allowances). This is no longer the case. Given the much higher *relative* living standards of today's production workers, it is possible that the basic wage fixed by Higgins (or perhaps the one recommended by the subsequent, more thorough, Piddington Report) bore a relationship to median full time earnings that is not much different to the Modest But Adequate standard today³⁵.

We conclude, as we have in previous submissions, that the most appropriate benchmark available *at the present time* for fixing minimum wages is the "*Modest But Adequate*" benchmark for a single person of workforce age living alone and renting privately. Its current value stands at approximately \$450 per week³⁶. This is a *consumption* benchmark, and as such it corresponds more closely to *disposable* income than gross income. The equivalent before-tax wage is approximately \$550 per week.

Accordingly, ACOSS recommends that the Commission undertake an inquiry into the living standards of low-paid workers with reference to those in the wider community, in order to arrive at an objective benchmark for a minimum wage appropriate for a single adult. We recommend that this inquiry be informed by the work undertaken by the Budget Standards Project and other relevant living standards research.

³³ Ibid, See Table 8 on page 34 (using the average of the third quintile as a rough approximation of the median) and Table 12 on page 40. Note that the equivalent proportion of *gross* median wages would be lower since median wages attract a higher tax rate than the gross equivalent of the Modest But Adequate standard.

³⁴ Johnson D (1987), *The calculation and use of poverty lines in Australia*. Australian Economic Review 4/1987.

³⁵ That is, around 75% of the median full time wage. See Piddington A (1920), *Royal Commission on the basic wage*. Justice Piddington found that the cost of living '*according to reasonable standards of comfort*' for a family of five was much higher than the then basic wage. With considerable foresight, he recommended that the basic wage be supplemented by a national system of child endowment to meet the minimum costs of raising children. This was established many years later.

³⁶ See Saunders, op cit. This Budget Standard is for a single adult renting privately. The equivalent Budget Standard for a home purchaser is significantly higher.

The wage fixation process

We do not normally comment in detail on the process of wage fixation in our submissions, but wish to raise for the Commission's consideration changes to the process that might improve it. This is in the context of proposals advanced publicly by a number of organisations that the process of fixing minimum wages might be fundamentally changed.

In our view, any changes to the system should be benchmarked against a set of principles that reflect the purpose of minimum wages and the important – and often contentious – place they occupy in our national life and public debate. ACOSS considers that any system of minimum wage fixation should be characterised by:

- *Transparency* - the competing arguments should be heard in public, with Governments and other interested organisations being given the opportunity to be heard
- *Justice* – they should be heard by a tribunal led by a person with appropriate legal standing and operate according to principles of natural justice
- *Expertise* – the tribunal should include members with expertise in economics and social policy, and draw upon such expertise from external stakeholders
- *Balance* – the tribunal should balance the needs and interests of low paid employees, employers, unemployed people, and the economy
- *A key, but not determinative, role for Government* – the Australian Government (along with State and Territory Governments) should be heard on the merits of the claims, but Governments should not be the ultimate decision makers.

The present arrangements incorporate these elements and the Commission is well placed to play this role, but we respectfully submit that the process could be improved in two ways:

- The Commission could establish an expert panel to advise it in balancing the needs of low paid workers with those of the economy and jobless people. The panel could be drawn from individuals with widely acknowledged expertise in economics and social policy.
- Periodically, the Commission could adopt a more in depth, investigative approach towards fixing minimum wages. For example, ACOSS has urged the Commission adopt a benchmark for the adequacy of minimum wages, which would require a detailed investigation of the needs of workers and their families and how those needs, and community standards regarding income adequacy, can best be measured.

We have concerns about proposals that would ultimately shift decision making over minimum wages to Government. These carry a risk that wage fixation might be politicised. There is evidence to suggest that, in countries where Governments determine minimum wages (either by legislation or through a tribunal with recommendatory powers), real minimum wages respond to the political cycle rather than the needs of low paid employees, employers, and the economy (see Attachment

below). Further, growth in real minimum wages is more volatile in some of these countries. We submit that this is not in the long term interests of any of the key stakeholders – especially low paid employees.

In other proposals to change the wage fixation process, public authorities with other important economic functions such as the Reserve Bank and Productivity Commission would become directly involved. These proposals require very careful consideration, as there are risks that the other roles of those organisations might be compromised.

Conclusion

ACOSS believes it is essential that the award system continue to play a central role, along with the social security system, in protecting the living standards of low-paid workers and their families. A minimum wage that is not based on an objective assessment of the minimum needs of those who rely on it, and is disconnected from movements in pay for workers higher up the earnings distribution, is vulnerable to erosion.

It is critical that the living standards of low-paid workers not be allowed to fall further below community standards. Over the long term, minimum award wages have fallen substantially relative to average weekly ordinary-time earnings.

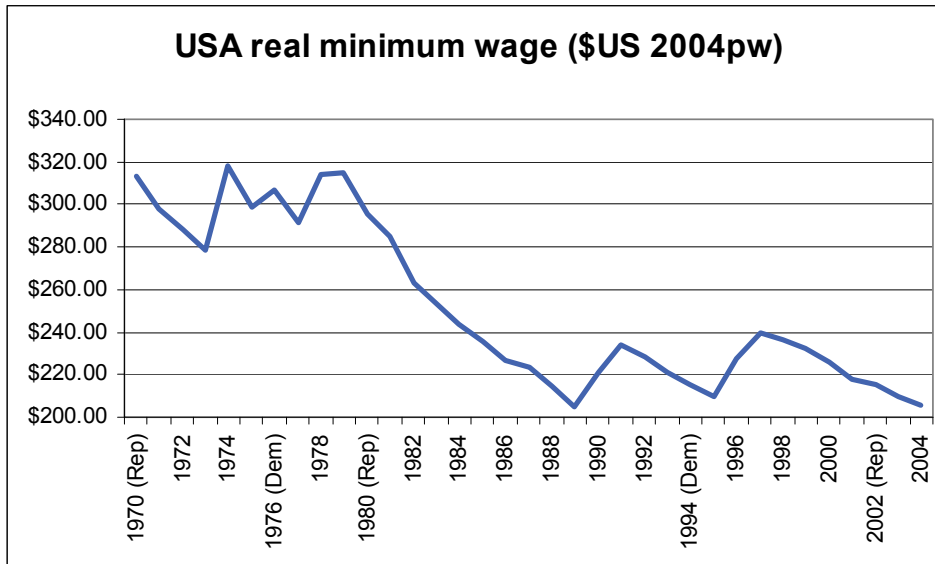
An effective minimum wage "floor" is essential to improve the living standards of low-paid workers and their families and to ensure they do not fall further behind.

In summary, ACOSS respectfully submits that, in the short-term the Commission should increase minimum wages so as to ensure that they do not fall any further behind movements in average wage rates. Over the medium term, we propose that the Commission undertake an inquiry to ascertain an appropriate benchmark for the adequacy of minimum wages.

Attachment:

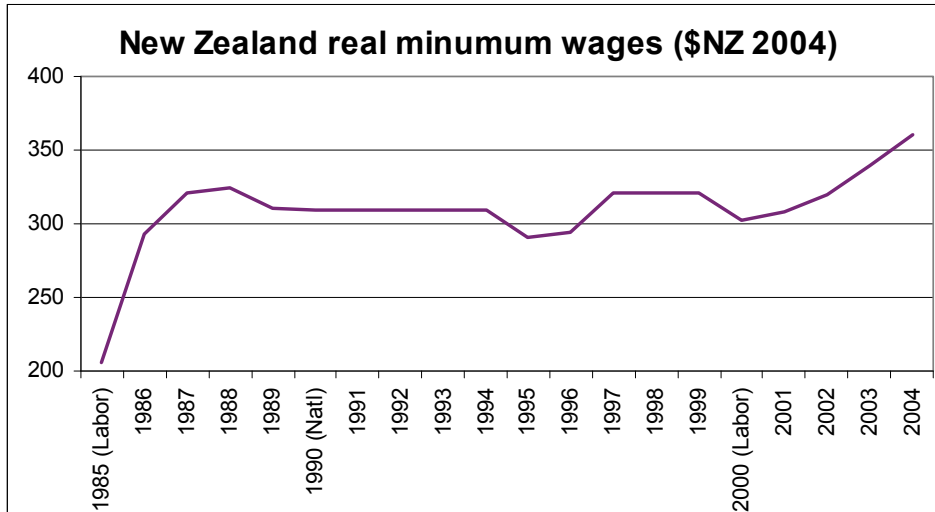
Trends in minimum wages in the United States, New Zealand and Australia

This short paper compares trends in real minimum wage outcomes in the United States and New Zealand (where Governments effectively determine minimum wages) and Australia (where the Industrial Relations Commission - an independent tribunal - fixes minimum wages). The graph below charts real minimum weekly wages (assuming a 40 hour week) in the United States over the past 30 years. Changes of Government there do appear to have had a major impact on growth in real minimum wages.



Sources: US Dept of Labor, History of federal minimum wage rates (1938-1996) and subsequent updates, Bureau of Statistics for CPI. The beginning of each Democrat or Republican administration is indicated at the bottom of the graph.

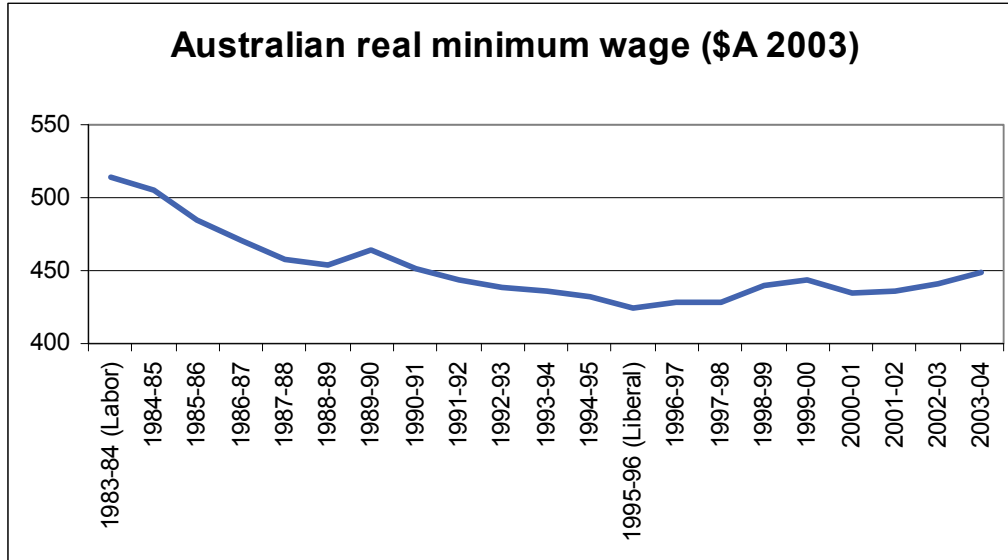
The graph below charts real minimum weekly wages (assuming a 40 hour week) in the New Zealand over the past 30 years. Again, changes of Government appear to be associated with major shifts in real minimum wages.



Sources: Pacheco & Maloney (1999), *Does the minimum wage reduce the employment prospects of unqualified New Zealand women?* in *Labour market bulletin* 1999, Updates from Department of Labour website www.dol.gov.nz; CPI updates from Statistics New Zealand.

Australia's pattern of minimum wage increases also reflects shifts in economic and social policy. However, these policy shifts cut across changes in Government. To a large extent, they reflected a bipartisan policy consensus. Broadly speaking, real minimum wages grew more strongly in the 1990s than in the 1980s. Following the deep recession of the early 1980s, wages policy focussed on reducing unemployment. Accordingly, both minimum and average wages were restrained. This strategy was effective in reducing unemployment, but growth in productivity slowed. Therefore in the early 1990s, the emphasis shifted towards productivity bargaining at the enterprise level. As productivity growth surged, the previous constraints on both average and minimum wages were eased. The Commission responded to these shifts in public policy, but overall there was less volatility in growth in real minimum wages than was evident in either the United States or New Zealand³⁷.

³⁷ By definition, *nominal* wages have been stable in these countries during periods when there was no increase. However, *real* wages (the measure that better reflects actual living standards) fell substantially over some of these periods - for example in the USA over most of the 1980s.



Sources: Dawkins (2000) The labour market, in Reserve Bank, The Australian economy in the 1990s; ABS, Australian Economic Statistics; Industrial Relations Commission website for updates.

There are two conclusions from this analysis, which appear to apply at least to a comparison between the United States, New Zealand and Australia:

- where minimum wages are effectively set by Government, real minimum wages appear to respond to the political cycle
- where minimum wages are set independently of Government, long term movements in real minimum wages appear to be less volatile.