

# **WAGES AND ALLOWANCES REVIEW 2008**

## **Outline of Submission**



**August 2008**

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## Table of Contents

	<i>Page</i>
1. Summary of Ai Group's position	3
2. Approach that the Commission should take in increasing wages and allowances	3
3. Relevant legislative provisions	5
4. Wage-setting decision of the Australian Fair Pay Commission	6
5. Economic conditions and outlook	7
6. Operative date and the importance of avoiding retrospectivity	17
7. Formula for adjusting wage related allowances	18
8. Adjustments to expense related allowances	18

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## Outline of Submission

### 1. Summary of Ai Group's position

1. The AIRC in accordance with the terms of the *Workplace Relations Act 1996* is conferred with power to vary:
  - Wage rates in transitional awards;
  - Wage-related and expense-related allowances in transitional awards; and
  - Wage-related and expense-related allowances in pre-reform awards.
2. In exercising its powers, the Act requires that the AIRC not vary the terms of awards in a manner that is inconsistent with decisions of the Australian Fair Pay Commission (AFPC).
3. Ai Group is not opposed to the AIRC increasing rates in transitional awards and increasing allowances in transitional and pre-reform awards, consistent with the AFPC's decision.

### 2. Approach that the Commission should take in increasing wages and allowances

4. Ai Group proposes that applications to vary awards, other than those which have been used as vehicles for the Full Bench proceedings, be dealt with by individual Members of Commission via the panel system.

5. Such an approach we submit is in the interests of all parties as:
- The parties to individual awards are better able to address issues relating to their awards;
  - Adequate time and attention can be paid to service and notification requirements;
  - Should the applicant Unions be diligent in filing their applications, ample time will be available for the settlement of orders prior to 1 October 2008;
  - Applications are able to be heard and determined by members of the Commission assigned to the relevant panel who have knowledge about the relevant industry and award; and
  - It avoids the wastage of resources which results from having several members of the Commission engaged in handling matters best dealt with by one member of the Commission.
6. Where the parties to a particular award agree, Ai Group seeks that the orders be settled without the need for a hearing.

### **Rounding**

7. Ai Group supports the rounding of wage increases in transitional awards to the nearest 10 cents. That is, the AIRC should grant a \$21.70 increase to the Federal Minimum Wage and other minimum adult weekly rates.
8. Ai Group submits that no general principle should be adopted for the rounding of allowances. Rather, the method by which individual parties to various awards have historically approached the question of rounding should be adopted.

### 3. Relevant legislative provisions

9. The terms of the *Workplace Relations Act* set out the manner in which the AIRC is required to perform its functions with respect to varying both transitional awards and pre-reform awards.
10. The Act makes it clear that whilst the AIRC is not required to replicate the decision of the AFPC it must ensure that its decision is not inconsistent with the AFPC's decision.
11. In considering applications to vary allowances, the Commission needs to ensure that elements of remuneration which are now incorporated within Pay Scales are not varied in awards and hence would be subject to a double increase. It is not always clear what is and what is not an "allowance".
12. Section 178 of the Act gives some guidance on this issue. In this section the term "basic periodic rate of pay" is defined as follows:

*"Basic periodic rate of pay means a rate of pay for a period of work (however the rate is described) that does not include incentive-based payments and bonuses, loadings, monetary allowances, penalty rates and other similar separately identifiable entitlements".*

13. Basic periodic rates of pay are included in Pay Scales and hence the AIRC has no jurisdiction to vary any elements of such rates of pay in pre-reform awards.

## 4. Wage-setting decision of the Australian Fair Pay Commission

14. On 8 July, the AFPC announced its general wage-setting decision for 2008. The Commission increased the standard Federal Minimum Wage (FMW) to \$543.78 per week (up \$21.66), or \$14.31 per hour (up \$0.57). All Pay Scales were increased by the same amount. The increase represents a 4.1% increase in the standard FMW.
15. The decision takes effect from the first pay period on or after **1 October 2008**.
16. The increase awarded is considerably higher than that sought by Ai Group, although not as high as that sought by the ACTU. In its submission to the Commission, Ai Group proposed an increase of \$0.35 per hour (\$13.30 per week) for all classifications, representing a 2.5% increase. Once tax cuts were taken into account, this amount would have increased to around \$20 per week or 4.1%.
17. In its decision, the AFPC had considerable regard to the financial pressures on low-income households, especially those resulting from movements in consumer prices. It appeared to be concerned to ensure low-income households received a real increase in disposable income, considering the increase together with relevant tax and transfer changes.
18. In considering employment and competitiveness across the economy, the AFPC noted that wage pressures have generally been contained to date and that higher wage growth appeared to have been contained to segments of the economy with skill-shortages or already low unemployment. It noted that wage growth in collective agreements made over the past three years had been steady.

19. It estimated that taking into account direct and indirect effects of the increase, the effect on prices over the medium term was up to 0.4 per cent. It stated that on balance, the effect on aggregate wage and inflation outcomes would be “relatively minor”.
20. As with the 2007 decision, the AFPC had regard to the effect of, and interaction with, changes to the tax/transfer system, noting that the effect on disposable income could be significant. Its modelling showed that all household types modelled would experience a real increase in disposable income in October 2008 compared with the previous year, as a result of the decision.

## **5. Economic conditions and outlook**

21. In performing its functions, the AIRC must have regard to the objects of the Act and *“the state of the national economy and the likely effects on the national economy of any order the Commission is considering, or is proposing to make, with special reference to the likely effects on the level of employment and on inflation”* (s.103).

### **Summary**

22. The current economic and competitive environment necessitates that caution be exercised in determining minimum wage outcomes this year.
23. The June quarter 2008 consumer price inflation data was recently released. Price inflation was higher than expected in the quarter and this implies continued vigilance by the Reserve Bank in monitoring of wages outcomes and inflation expectations.
24. On the other side of the ledger, June quarter 2008’s retail trade data showed a 0.6% decline in sales volumes, which was weaker than expected.

25. On balance, the data continue to suggest that given the current slowing in domestic demand growth and the slowing in global growth, inflation will head, slowly, back to within its target range of 2-3% by mid 2010 in line with the Reserve Bank's forecasts.
26. The world economy is an important area of uncertainty affecting the outlook for Australian economic activity. Global economic growth has slowed but rising commodity prices have induced rising inflationary pressures in the United States, Europe and Japan and the commodity importing emerging economies. Higher risk aversion in financial markets has also constrained credit availability in some economies including the United States.
27. A key uncertainty for the size of the slowing in global growth is how far the downturn in the US, Europe and Japan will affect growth in the emerging economies. There are now signs that the latter, which have driven global activity over recent years, are now seeing slower exports growth.
28. China, a key driver of Australia's recent and near-term growth is facing inflationary problems driven by commodity price inflation and strong economic growth. At the same time, China's exports growth, particularly to the United States, has slowed significantly in line with the slowing of US economic activity.
29. The risks for Chinese and, therefore, global growth are clearly on the downside.
30. Supporting other signs of moderating domestic growth, recent Ai Group surveys suggest that the manufacturing, construction and services sectors saw weaker conditions in recent months. Confirming concerns over inflationary pressures, wages, input and product price growth remain solid.

## Recent economic data

31. Recent partial economic data suggest a further slowing in economic growth while inflation in the June quarter was higher than expected.

- Annual 'headline' inflation accelerated to 4.5% in the June quarter 2008, up from 4.2% in the previous quarter. In quarterly terms, the headline inflation rate was 1.5% up from 1.3% in the previous quarter.
- While headline measures of inflation have accelerated, for policy purposes the RBA focuses on two measures of underlying inflation, the 'trimmed mean' and the 'weighted median'. In annual terms, these measures also accelerated to 4.3% and 4.5% respectively, averaging around 4.4%. This average is significantly above the Bank's 2-3% target range.
- Among other measures of underlying inflation (so-called 'exclusion' measures), the all-groups index excluding volatile items increased by 1.3% in the quarter (up from 1.2% in the previous quarter), with the annual rate rising to 4.2% from 3.6% in the preceding quarter.
- The quarterly increase in 'market goods and services ex-volatile items' accelerated sharply from 0.8% to 1.4%, for annual increase of 4.2%, up from 3.5%.

32. While prices accelerated in the June quarter, retail trade growth weakened further in the quarter and in the month of June.

- In line with ongoing signs of a significant easing in economic activity, seasonally adjusted retail trade volumes, which account for around 16% of GDP, fell by 0.6% in the June quarter 2008, following a fall of around 0.1% in the March quarter.
- In the month of June, seasonally adjusted retail sales fell by 1.0%. This followed a revised increase of 0.9% in May and a revised fall of 0.4% in April.
- Household goods retailing was the only sector to show an increase in sales (0.8%), while hospitality and services remained steady.

- All other areas in the sector experienced falling sales. The strongest falls were in department stores (-5.2%) and clothing and soft good retailing (-5%).
  - Two of the states reported some growth in retail turnover, South Australia (0.3%) and Western Australia (0.2%).
  - The other states reported declines, Victoria (-1.5%), Queensland (-1.3%), New South Wales (-1.0%) and Tasmania (-0.7%).
33. The easing of retail sales growth is in line with other indicators, including consumer credit growth that suggest that consumers are pegging back their spending, rebuilding savings and focusing on reducing debt.
34. In line with slower retailing, housing data is unambiguously weak.
- The seasonally adjusted number of dwelling unit building approvals fell by 0.7% in June following a revised 7.2% fall in May.
  - The trend for total dwelling approvals fell by 0.9% in June - a seventh consecutive month of decline.
  - The fall in total dwelling approvals was driven by a 1.4% decline in the number of private sector other dwellings approved.
  - The number of private sector houses approved was stable in June, following a revised 1.6% fall in the previous month.
  - In seasonally adjusted terms, the value of new residential building fell by 2.7% in June, while, the value of non-residential building fell by 7.5%.
35. Paralleling the decline in building approvals, finance commitments, which tend to be a leading indicator of building approvals, have softened significantly due to higher interest rates and deteriorating housing affordability.
- The value of owner occupied housing commitments fell by 5.7% in May (seasonally adjusted).
  - The number of owner occupied housing finance commitments also fell in May, by 7.9%.

- In seasonally adjusted terms, both the number and value of owner-occupier housing commitments have fallen in four consecutive months.
  - The number of owner occupied dwelling finance approvals was 21.5% lower in May 2008 than at the same time last year. Annual growth in finance for the construction of new dwellings fell to 1.9% in April.
  - The total value of dwelling finance commitments for investment housing fell by 6.8% in May to be 19.2% down on the same time last year.
  - Overall, finance commitments for all dwellings in April decreased by 6.1%, to be 18.3% lower over the year.
36. The latest employment data show a distinct slowing in labour force growth in July. Generally the direction of labour force growth lags other economic data and the slower growth in the most recent month may well herald the start of a period of more disappointing labour market outcomes. In NSW the beginnings of decline are suggested in the seasonally adjusted July data with employment falling by 17,600 and, despite a fall in the participation rate, the rate of unemployment rose to 4.7%.
37. As a further indication that the labour market is beginning to respond to slower economic activity, job vacancy numbers are showing signs of easing growth.
- According to ABS data, there were a total number of 184,400 job vacancies in the three months to May 2008, a 3.6% increase from February 2008 (seasonally adjusted).
  - However, the trend for total job vacancies grew at a slower pace in May 2008, rising by 1.1%. While this marked the eleventh consecutive quarter of trend growth for total job vacancies, it was the softest rate of increase recorded since November 2005.
  - Signs of slower vacancy growth are consistent with the Department of Education, Employment and Workplace Relations (DEEWR) vacancy survey for July 2008. The DEEWR Skilled Vacancies Index (SVI) fell by 0.5% in July with vacancies falling for all three occupational groups: Professionals (down by 0.8%), Associate Professionals (down by 0.5%)

and Trades (down by 0.3%). In annual terms, the SVI is 6.0% lower than in July 2007.

38. Other partial indicators confirm a softening economic outlook.
- The National Australia Bank's monthly business survey for June reported that business conditions deteriorated sharply and unexpectedly with a sustained slowing in sales and profits, which have begun to slow job growth and reduce capacity usage.
  - The NAB's quarterly survey for the June quarter showed a similar pattern of slowing growth. Business confidence fell to its lowest level since the early 1990s recession, while business conditions in the quarter were also sharply lower, consistent in NAB's view with domestic demand growth slowing to 2-2½% by mid 2008.
  - Near and medium term expectations also fell, reflecting weaker investment intentions and softer forward orders.

## **Recent data on industry activity**

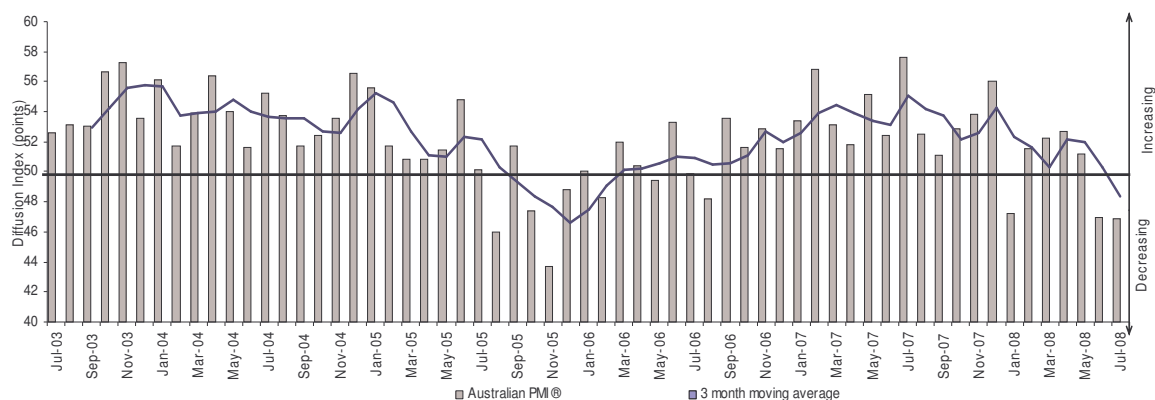
39. Industry activity has continued to weaken in the manufacturing, services and construction sectors over recent months. Manufacturing growth improved in the December quarter of 2007, before easing again into the March and June quarters of 2008, this has persisted into July. Services activity has also cooled in recent quarters, falling back significantly from its earlier solid expansion path. Construction activity declined in the past two months.

### **Manufacturing**

40. The Australian Industry Group - PricewaterhouseCoopers Australian Performance of Manufacturing Index (Australian PMI®) eased in July recording a reading of 46.9, little changed from the 47.0 points in June. The index remains below the key 50.0 level separating expansion from contraction.

41. The slower domestic economy, higher interest rates, and consequent softness in housing activity are driving the weakness in activity, compounded by weaker global growth, rising costs and the high Australian dollar.
42. Production and unemployment fell again in July, though at a slower rate. New orders and stocks both fell solidly, putting downward pressure on production.
43. Supplier deliveries were stable, exports rose moderately following two months of falls.
44. Input costs grew strongly but at a slower rate, while selling prices growth was stable. Wages increases accelerated in July after four months of moderate easing in growth.
45. Manufacturers cited positive effects on activity from solid infrastructure and mining related demand, while on the negative side were weaker orders notably relating to housing construction; raw material costs especially steel, aluminium and petrol; problems with staff retention and the Western Australia gas disruption.
46. Manufacturing activity grew in Western Australia and South Australia but declined in all other states.

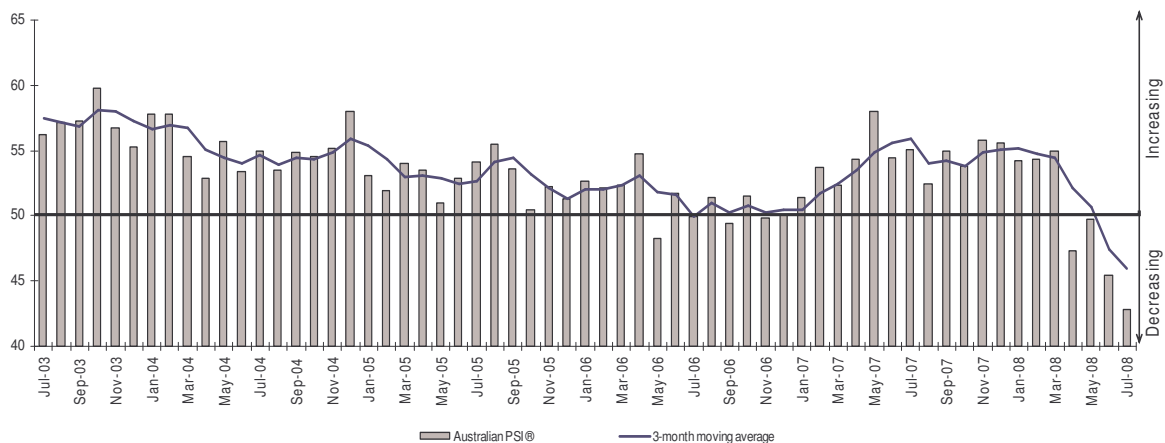
**Chart 1: Australian PMI®**



## Services

47. Services sector activity slumped further in July, with declining levels of consumer and business confidence further restraining household spending and business activity.
48. Firms continue to identify high interest rates and fuel prices as the key factors holding back demand for services.
49. The seasonally adjusted Australian Industry Group/Commonwealth Bank Performance of Services Index (Australian PSI®) fell 2.6 points to 42.8, below the key 50.0 level separating expansion from contraction.
50. New orders and supplier deliveries contracted for a fourth consecutive month, while sales and employment deteriorated at a faster pace.
51. The weakness in activity was broadly-based, although there were signs of resilience in the personal & recreational services and communications services sectors.
52. Activity fell in all states, with the rate of contraction slowing in only Tasmania and Queensland.

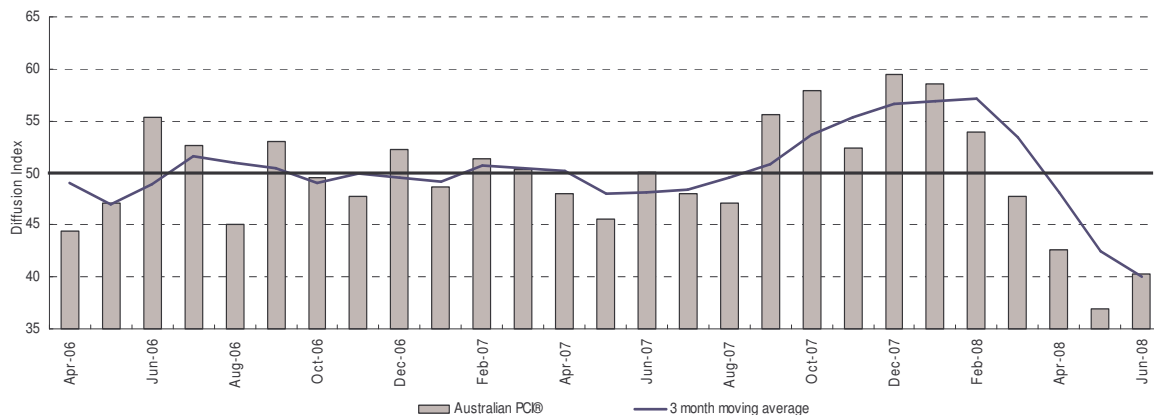
**Chart 2: Australian PSI®**



## Construction

53. The national construction industry declined for a fourth consecutive month in June 2008, although the rate of decline was less marked than in the previous month. The Australian Industry Group / Housing Industry Association Performance of Construction Index (Australian PCI®) registered 40.3 in June 2008, remaining below the critical 50.0 points level separating expansion from contraction.
54. Construction companies linked the reduction in activity to continued weakness in market demand and a further contraction in new business volumes, citing the negative influences of higher interest rates, and weaker consumer and investor confidence. Firms also commented that market uncertainty, and difficulties in raising funds had led to delays in project commencements.
55. For the industry as a whole, both activity and new orders declined further in June (albeit at slightly lesser rates than in May), with the subsequent lower workloads resulting in a reduction in employment for a third consecutive month.
56. The rate of increase in input costs remained at an elevated level in June, as firms reported increased fuel and steel prices.

**Chart 3: Australian PCI®**



## **6. Operative date and the importance of avoiding retrospectivity**

57. Ai Group strongly opposes any retrospectivity in the operative date of the variations.

58. There are compelling and obvious reasons why retrospectivity in respect of operative dates for wage and allowance increases is inappropriate and should only be contemplated in very exceptional circumstances. Such reasons include:

- There are substantial administrative and direct costs associated with back-paying employees to take account of retrospectivity of wage and allowance increases; and
- Nowadays a significant percentage of the workforce is employed by labour hire companies and in other contract labour situations. Typically, the employers in these situations have no ability to recover retrospective wage and allowance increases from their clients.

59. Ai Group submits that the operative date should be 1 October 2008 for any applications in respect of which orders are issued by that date. For any other applications, the date of variation should be no earlier than the date that the order is issued.

## 7. Formula for adjusting wage related allowances

60. For more than 10 years, the method of adjusting wage related allowances in accordance with Safety Net Review decisions has been derived from the Commission's *Furnishing and Glass Industries Allowances decision* [Print M9675; (1996) 40 AILR 3–399].
61. The Statement of Principles arising from the 2005 *Safety Net Review Decision* explains the method of adjustment as follows:

*“Such allowances and service increments should be increased by a percentage derived as follows: divide the monetary safety net increase by the rate of pay for the key classification in the relevant award immediately prior to the application of the safety net increase to the award rate and multiply by 100.”<sup>1</sup>*

62. This method of adjustment was utilised by the AIRC in its 2007 decision. Ai Group submits that the same approach is workable and appropriate on this occasion.

## 8. Adjustments to expense related allowances

63. A well accepted formula tends to apply within each individual award in relation to the adjustment of various expense-related allowances; typically based on movements in the relevant Consumer Price Index.
64. Ai Group can see no reason why the same approach should not generally apply in the present application.

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<sup>1</sup> PR002005 *Safety Net Review – Wages June 2005* – Attachment A, Principle 5, pg. 124