

# **2005 SAFETY NET REVIEW CASE**



**Reply Submission to the  
Australian Industrial Relations Commission  
by  
The Australian Industry Group  
and  
Engineering Employers' Association, South Australia**

***April 2005***

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# 2005 SAFETY NET REVIEW CASE

## Reply Submission

### R1 Introduction

R1. The ACTU's reply submission fails to provide any persuasive arguments to counter Ai Group's key contentions that:

- The economy is slowing, productivity performance is weaker and capacity constraints are emerging and, therefore, the Commission needs to adopt a very cautious approach in determining the level of safety net adjustment this year;
- If the ACTU's claim was granted the consequent inflationary pressures would increase the risk of further interest rate rises, which low paid workers with mortgages, personal loans and credit card debts can ill-afford;
- The ACTU's claim, if granted, would damage the international competitiveness of Australian companies;
- The claim comes at a time when many companies are struggling to cope with huge increases in input prices (eg. steel, fuel) and other cost pressures;
- Many people who are seeking work would be deprived of a job, if the unions' claim was granted, and many existing employees would suffer decreased job security;
- There have been massive increases in tax transfer payments in the past year which have substantially increased the disposable incomes of a high proportion of low paid and other employees and, consequently, the level of safety net adjustment which the Commission would otherwise have awarded should be substantially discounted;

- Safety net adjustments have a disproportionate negative impact on small businesses and care needs to be taken to avoid damaging this vital sector of the Australian economy;
- The ACTU's claim is inconsistent with the objects of the *Workplace Relations Act* in that it would diminish the primacy given to workplace bargaining under the *Workplace Relations Act*;
- An \$11.00 per week safety net adjustment is appropriate.

R2. In several areas, far from countering Ai Group's arguments, the ACTU's reply submission adds further weight to Ai Group's contentions.

## R2 Economic Conditions and Outlook

- R3. Ai Group welcomes the ACTU's acknowledgement in its reply submission that "growth has moderated". Survey data set out below, reinforces that the economy has moved to a lower gear in 2005.
- R4. Having said this, it is disappointing that the ACTU continues to adopt the flawed approach of focussing on economic data that reflect the past. The ACTU needs to be reminded of its statement in last year's submission which emphasised the need to consider the economy at the time "*when any decision in the Case is likely to take effect*"<sup>1</sup>.
- R5. Further, the ACTU persists with its tired old approach of seeing the economy in "straight line" terms rather than a more complex picture of often multi-directional trends. It is the mixed messages that make the task challenging - something the Reserve Bank Governor highlighted in his recent testimony to the House of Representatives Standing Committee on Economics, Finance and Public Administration.
- R6. It is untenable for the ACTU to persist with its position that "*the economy remains strong, growth continues, unemployment remains at historically low levels, inflation remains at the centre of the Reserve Bank's target range, productivity, profits and business investment also continues to grow*" in order to argue for a wage adjustment that will apply for most employees sometime in the third quarter of 2005.
- R7. If we look forward using both available data and current forecasts, we see a picture of:
- An economy growing at a much slower pace;
  - Unemployment no longer falling;
  - Inflation pressures rising;

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<sup>1</sup> ACTU's submission in the 2004 Safety Net Review, p.71.

- Productivity declining;
- Profit growth moderating; and
- Business investment strong but likely to moderate.

R8. Ai Group has compiled a listing of current economic forecasts for 2005 by the financial and private sector forecasting community (see **Table 1** below). They support the proposition of slower growth rather than one of an economy remaining strong. A number of the forecasts also point to higher levels of inflation, with forecast inflation touching the upper-limit of the RBA's band for inflation.

**Table 1 – Current Economic Forecasts for 2005**

Organisation	Growth Forecast	Inflation Forecast
ANZ	2.3	2.1
CBA	2.2	2.6
NAB	2.0	2.4
WBC	2.7	3.0
Access Economics	2.2	2.8
St George	2.6	2.9
Macquarie	2.5	2.9

Sources: ANZ, March 2005; Access Economics, March 2005; CBA, April 2005; NAB, March 2005; St George, Macquarie, April 2005; Westpac, April 2005

R9. Contrary to the ACTU's proposition,<sup>2</sup> there is nothing in the economic literature that suggests it is impossible to have slower growth and rising inflation (leading to interest rate pressure), the ACTU seems to have forgotten that Australia in the late seventies went through a period of stagflation (declining growth and rising inflation).

R10. While Ai Group does not suggest we face a similar period of stagflation, the emerging data points to higher inflationary pressures in a period of slowing growth. This comes from inflationary pressure from skills shortages, infrastructure bottlenecks, higher fuel costs, and rising upstream prices. Indeed, the RBA Governor noted in its testimony to the House of Representatives Standing Committee on Economics,

<sup>2</sup> ACTU Reply Submission, p.7

Finance and Public Administration (EFPA5) that *“this combination of weaker than expected GDP growth and higher than expected inflation is a disappointing one”*.

- R11. Further, as the recently released Access Economics Business Outlook for March quarter 2005 states (p.vi):

*“Australia’s growth party is over. Rates are rising even though output growth hasn’t been lower since 1992. Growth has slowed as, first, China-driven demand for commodities and years of infrastructure neglect has left demand crashing up against supply constraints in mining, resource manufacturing and commercial construction. But, second, a slowly deflating housing price bubble is undercutting demand in retail, housing construction and real estate, while the soaring \$A has hurt demand for non-resource manufacturing. Demand weakness in these sectors is being ignored by the Reserve Bank, which is raising rates as it only sees the first problem – supply weakness. That is highly risky amid a deflating housing bubble. So output growth will stay below trend through 2005, and unemployment will soon stop falling, while the current account may be slow to improve.*

*The Reserve Bank fears inflation as rampant demand has seen the current account blow out and driven unemployment down. They see that spilling over into inflation next because upstream prices are rising rapidly, oil is frisky, and as more income keeps getting tipped in by the surging commodity cycle. But we are less sure – only some exporters have pricing power, and we see demand gains fading fast in sectors affected by a fading housing price bubble. And, with the \$A on the rise, that may keep inflation under 3%, and it may keep any lift in wage inflation relatively modest”*.

- R12. The assessment present by Access Economics is supported by recent survey data collected by Ai Group.

## **Quarterly Survey of Australian Manufacturing**

R13. The latest Australian Industry Group - PricewaterhouseCoopers quarterly Survey of Australian Manufacturing showed that while growth in production steadied in the March 2005 quarter, it was nevertheless the weakest March quarter in four years.

R14. In the March quarter 2005, the net balance of firms reporting higher production increases rose to a seasonally adjusted +12% from +10% in the previous three months (a positive net balance indicating growth).

R15. Production increased in nine sectors, up from seven in the previous quarter – although this was primarily underpinned by the largest increase in stocks in the history of the survey. As well, the improvement was driven largely by the food & beverages and textiles sectors.

R16. Growth in sales and new orders strengthened moderately, but is expected to ease in the June quarter. Production growth in the next three months is projected to be the weakest since the September quarter of 2001. Other key findings were:

- Among the States, growth strengthened in NSW and Tasmania, but slowed in Western Australia and contracted modestly in Victoria and South Australia;
- Export growth picked up slightly, following a small contraction in the December quarter 2004;
- Sales and new orders improved, in contrast to weaker growth in both supplier deliveries and employment;
- Profits fell for the third consecutive quarter, although at a slightly more moderate pace than in the December quarter;

- Raw material costs continued to increase at the same high rates as in the previous two quarters. Selling prices also increased, but at a slower pace than previously;
- Stocks increased at the fastest pace on record, while order backlogs fell for the third consecutive quarter.

## **Australian PMI™**

R17. A further deterioration in exports and weakening new orders held back manufacturing growth in March according to the latest Australian Industry Group - PricewaterhouseCoopers Australian Performance of Manufacturing Index™.

R18. Despite rising by 1.8 points to 52.6, the March Australian PMI™ was still well below the peak of late 2004 and down on the 55.4 recorded at the same time last year (**Chart 1**). Readings above 50 indicate growth and the distance from 50 reflects the strength of that growth.

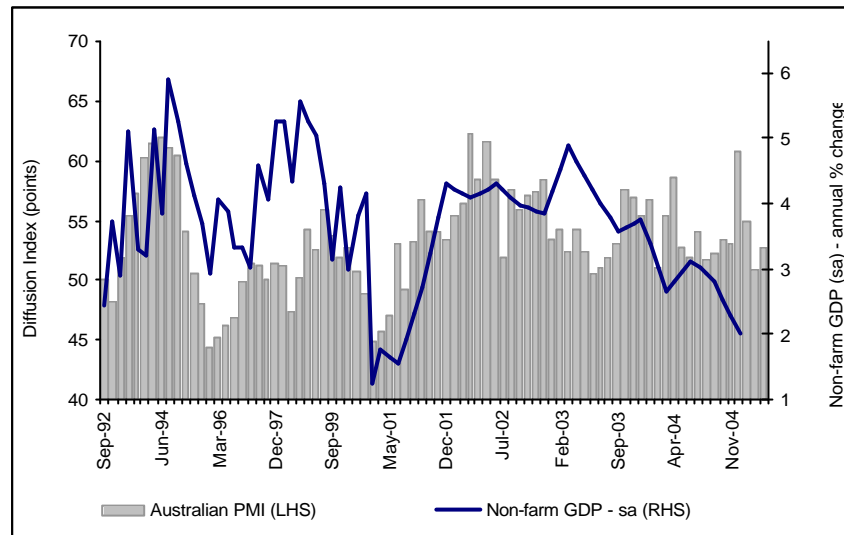
R19. The export sub-index recorded a new low of 41.0 points in March, following a then series low of 46.6 in February. As well, the new orders index declined by 0.4 points to 52.0.

R20. Among the remaining Australian PMI™ components, growth in deliveries weakened while finished stocks posted a small decline. Employment and production improved – the latter however, recording growth well below the corresponding period in 2004.

R21. The input cost index recorded its largest monthly rise since June 2004 (up 4.4 points to 77.9). In addition to input cost pressures, skills shortages and import competition also featured among company responses in terms of the main factors affecting activity.

R22. The Australian PMI™ points to annual manufacturing growth of around 2% and non-farm GDP growth of over 2.5%.

**Chart 1 - Australian PMI™ and Non-farm GDP**



## Australian PSI™

R23. The services sector recovered slightly in March, following a drop in activity last month, with the seasonally-adjusted Australian Industry Group – Commonwealth Bank Performance of Services Index (Australian PSI®) rising 2.7 points to 51.4 (**Chart 2**).

R24. The result has brought the Australian PSI® reading back above the critical 50 point mark that separates expansion from contraction indicating a moderate recovery in services sector conditions. This follows the decline to 48.7 in February.

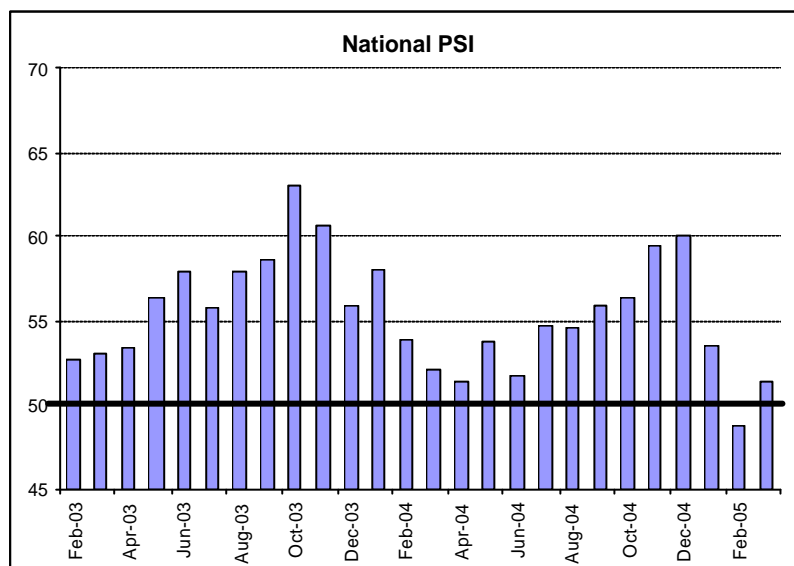
R25. Despite this improvement, however, the March index provides further evidence that growth in services sector activity has slowed from the strong rates reported in late 2004.

R26. Sales fell for the second consecutive month in March, with growth in the overall Australian PSI® underpinned by a rise in new orders and employment; a modest rise in inventories; and, a slower rate of decline

in supplier deliveries.

R27. Services sector activity expanded in eight of nine sectors, led by transport & storage and a recovery in retail trade. Growth slowed in finance & insurance; accommodation, cafes & restaurants; and property & business services. Wholesale trade was the only sector to report a contraction in activity.

**Chart 2 Australian PSI™**



## **R3 The Needs of the Low Paid and Changes to the Social Safety Net in the Past Year**

### **Ai Group's Submission**

R28. Ai Group showed that low-income households with dependent children have benefited substantially from changes in the social safety net since the Commission last adjusted minimum wages. We argued that the large improvements in households' disposable incomes have improved the capacities of these households to meet their needs.

R29. Ai Group also showed that over this same period the social safety net has improved for low-income households without dependent children. These households have become eligible for a 50 percent increase in the superannuation co-contribution payment.

R30. Ai Group proposed that the Commission take these changes into account and discount the increase in safety net wages it would otherwise grant. Ai Group submitted that an increase in minimum wages of \$11 per week would be an appropriate increase after the changes in the social safety net were taken into account.

### **The ACTU's Submission in Reply**

R31. In the section of its Submission in Reply headed "Budget 2004-05 and Other changes to the transfer system" (paragraphs R8.48 to R8.66), the ACTU raises a number of points in relation to these arguments. The ACTU:

- claims that the methodology underlying Ai Group's calculations of increases in income support payments gives a "false impression" of

the actual increase in income support since the Commission last increased minimum wage levels;

- makes a number of comments in relation to the substantial increases in the social safety net for families with dependent children;
- makes some observations in relation to regular, inflation-related changes to the social safety net; and
- raises a number of points about changes to the superannuation co-contribution payment.

### **Summary of the importance of the ACTU's comments**

R32. As elaborated below, none of these points provide reason to reject the arguments put forward in Chapter 4 of Ai Group's Submission. In some cases the ACTU's comments refine and add weight to Ai Group's position.

R33. The points raised by the ACTU do, however, highlight a substantial shortcoming in the ACTU's approach to the interrelationships between the broader social safety net and minimum wages.

R34. In its original submission to the current case (at 7.70), the ACTU suggested that minimum wages and the social safety net should be viewed complementarily. Nevertheless, faced with constructive suggestions about how the Commission might take changes in the social safety net into account when determining adjustments to minimum wages, the ACTU has no suggestions as to how this complementarity might be put into practice. Instead, it appears intent simply on deflecting attention away from the very substantial changes to the social safety net since the Commission last examined minimum

wage levels.

## **How changes in the social safety net should be measured**

- R35. The ACTU (at R8.55 and R8.56) puts forward an argument that Ai Group's calculations of changes to the social safety net give a "false impression of the actual increases in income support."
- R36. Instead the ACTU proposes that in considering whether and by how much to adjust minimum wage levels in 2005, the Commission should also take into account the impact on income support payments (and tax liabilities) of the amount by which minimum wages were adjusted in 2004.
- R37. The ACTU's suggestion overlooks the fact that the substantial changes to the social safety net that are under consideration in 2005 were all put in place *after* the Commission decided to increase minimum wages in 2004. The changes in the social safety net calculated by Ai Group already incorporates the 2004 wage increase because the point of reference is the level of wages after the 2004 wage increase is included.
- R38. Ai Group submits, therefore, that, in contemplating adjustments to wages in 2005, the relevant consideration is how income support entitlements and income tax liabilities have changed since the decision to adjust minimum wages in 2004. If this approach is taken the Commission will avoid the double counting that would be implied if previous adjustments in wages were also taken into consideration.
- R39. The Tables in Annexures, 5, 6 and 7 of Ai Group's Submission show changes in the social safety net since the last wage increase. They do not give a false impression of the extent of the changes to the social safety net. They reflect actual changes in the social safety net since the

minimum wages were last adjusted and with reference to the income levels of minimum wage earners resulting from that decision.

## **The ACTU's various comments in relation to households with children**

### ***i) Household Composition***

R40. It is clearly true that not all low-income earners are members of families with dependent children and eligible for Family Tax Benefit (FTB). This was a point made very clearly in Ai Group's original Submission.

R41. In that Submission Ai Group did not provide estimates of the numbers of households in this category because the ACTU itself had provided estimates of different household types in its original Submission (paragraphs 7.62 to 7.66). In its Submission in Reply (at R8.66), the ACTU provides a different estimate from another source:

*"As Richardson and Harding find of the typical low wage earner: One third have dependent children." (sic)*

R42. The ACTU (at R8.49) also claims that some families with dependent children receive benefits such as Youth Allowance and not the FTB. This raises two points; one is a question of definition and the other is the importance of elements of the social safety net not included in Ai Group's Submission.

R43. In Centrelink's *Guide to Australian Government Payments* (1 January – 19 March 2005) the basic conditions of eligibility for FTB (Part A) state that the recipient:

*"Must have a dependent child aged under 21; OR  
A qualifying dependent full-time student aged 21 to 24."*

*“Note: A child or student cannot be a dependant if:*

- they are receiving a pension, Labour Market related payment such as Youth Allowance; OR*
- aged 5-15, not studying full-time and their annual income is \$10,948 or more; OR*
- aged 15 – 24 and their annual income is \$10,948 or more or they are receiving a Prescribed Education Scheme payment such as ABSTUDY.”*

R44. Ai Group’s claims in relation to households with dependent children coincide with the conditions governing eligibility for FTB. Clearly only families with dependent children or students are eligible to receive FTB and only families in receipt of FTB have been affected by changes to FTB arrangements.

***ii) Entitlement to other forms of income support***

R45. The second point arising from the ACTU’s comments is more interesting. In pointing to benefits such as Youth Allowance, the ACTU implicitly proposes that the Commission look more comprehensively at all elements of the social safety net including payments such as Youth Allowance. When one or more family member receives payments such as Youth Allowance (which is paid at a rate higher than payments in respect of dependent children or students under Family Tax Benefit Part A), this should also be taken into account when considering the capacity of this household to meet its needs.

R46. It should be noted that families are often eligible for FTB in respect of dependent children despite the fact that another family member does not qualify for FTB because they are themselves eligible for Youth Allowance or some other form of income support.

R47. In Ai Group's Submission there was only limited coverage of the income support system and changes to that system over the past year. Ai Group's submission only looked at the changes in the income support system relevant to a set of one and two child households eligible for FTB and single people only eligible for the superannuation contribution payment.

R48. This limited coverage understates the full extent of the changes to the social safety net. Ai Group welcomes this important contribution by the ACTU. Although the ACTU does not propose that the Commission take into account any changes to the social safety net, the clear implication of this point is that that the Commission should consider the full range of changes to the social safety net.

*iii) Rent Assistance*

R49. The ACTU notes (at R8.57) that Ai Group's illustrations of changes in disposable income for households with children apply only to those eligible for Rent Assistance. The ACTU claims there are only 347,847 such families.<sup>3</sup> Ai Group appreciates this contribution by the ACTU and at **Annexure A** we provide data that calculates the impacts of changes to the social safety net for families with children and who are not eligible for Rent Assistance. Taken together households receiving FTB with Rent Assistance and households receiving FTB without Rent Assistance total about two million households.<sup>4</sup>

R50. The illustrations in **Annexure A** of increases in the social safety net for households with dependent children but not eligible for Rent Assistance confirm the very substantial increases in the social safety

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<sup>3</sup> This number of households, sourced from the Department of Family and Community Services' 2003-04 Annual Report, understates the actual number of households who are eligible for Family Tax Benefit and Rent Assistance because it only includes those households who receive these payments fortnightly. It does not include households who receive this form of income support as lump sum payments paid either by Centrelink or the Australian Taxation Office.

<sup>4</sup> Department of Family and Community Services, Annual Report 2003-04, Vol. 2.

net for households with children since the Commission last adjusted minimum wages.

**iv) Household needs**

R51. The final point made by the ACTU in relation to Ai Group's illustration of the substantial increases in disposable income for households with children is the failure of Ai Group to show "how these payments satisfy their (i.e. households') needs" (R8.58).

R52. It is true that Ai Group's submission did not show how increases in household disposable income (and therefore access to a greater range of goods and services) assists households satisfy household needs. It may be that even substantial increases in disposable income do not make a contribution to household needs at all. Higher disposable income may, for instance, be used to finance higher levels of gambling; to buy more cigarettes or to purchase a range of "luxury" goods and services that could not properly be classified as relevant to the satisfaction of "needs".

R53. While these lines of argument may raise many significant points, Ai Group cannot see their relevance in the present context. Increases in disposable income arising from changes in the social safety net assist households meet their needs in exactly the same manner as increases in disposable income arising from rises in minimum award wages – they create the potential for the higher level of disposable income to be spent on the satisfaction of household needs.

## **Regular, inflation-related adjustments to income support payments**

- R54. In Ai Group's Submission the argument was put that regular, inflation-related adjustments to income support payments and income tests should be taken into account when assessing the capacity of households to meet their needs. The ACTU make some comments about this argument (at R8.52 to 8.55).
- R55. There were two elements to Ai Group's argument. First, inflation-related adjustments to income support payments are relevant to the capacity of households to meet their needs. In many cases income support is a very large component of disposable income. Ignoring an inflation-related adjustment to income support payments is equivalent to ignoring an inflation-related adjustment to wages. Second, the *combination* of inflation-related increases in income tests and income support payments often results in an increase in income support that is greater than the inflation rate. This is demonstrated in Annexure 5 of Ai Group's submission.
- R56. At paragraph R8.53 the ACTU suggests that inflation-related increases in income support *payments* serve the purpose of preserving the real value of such payments. At paragraph R8.54 the ACTU quotes a claim from a Centrelink publication to the effect that inflation-related change in income test *thresholds* has the effect of maintaining the real value of the income test area.
- R57. Ai Group does not dispute these points. Rather, it is the *combination* of the change to income tests and payments that gives the result illustrated in Annexure 5. The combination of these two changes results in an increase in income support entitlement in excess of the amount required to preserve the real value of income support payments.

- R58. In Table R8.1, the ACTU calculates the impact of a larger-than CPI increase in wages (i.e. the large increase in minimum award wages handed down in the 2004 Safety Net Case) on an illustrative change in income support arrangements (drawn from Ai Group's illustration in Annexure 5). When compared with the table in Ai Group's Annexure 5, the ACTU table shows that when private incomes rise by an amount that is greater than inflation, eligibility for income-tested income support payments will be lower than would have been the case had private incomes not risen (or had risen by a lesser amount).
- R59. While this illustration is useful in pointing to the substantial erosion of entitlements to income support payments as a result of large increases in minimum award wages, it is not relevant to the arguments presented by Ai Group in support of including regular, inflation-related changes to income support arrangements in the consideration of changes of the social safety net.

### **Increases in superannuation co-contribution payments**

- R60. The ACTU makes a number of points (at R8.59 to R8.63) touching on Ai Group's submissions in relation to the 50 percent increase in the superannuation co-contribution payment announced in the 2004-05 Budget.
- R61. The ACTU point out that eligibility is not the same as participation; that even where households do receive a benefit from the co-contribution scheme this does not improve their disposable income; and that Ai Group's submission did not provide data on who took advantage of the scheme.
- R62. The first two of these points were clearly covered in Ai Group's original submission (at 77 and 81-2) and are not disputed.

R63. Ai Group appreciates the contribution the ACTU makes in pointing out that 450,000 individuals took advantage of the scheme in 2003-04. Using the figures supplied by the ACTU (R8.61), even if these individuals did not increase their level of personal contributions following the 50 percent increase announced in the 2004-05 Budget, they would be eligible for around \$280 extra in financial assistance under the enhancements to the social safety net announced in the 2004-05 Budget. Assuming an effective marginal tax rate of 35.5 percent, this is equivalent to a wage increase of around \$403 or around \$7.75 per week.

R64. The ACTU claim (at R8.59) that Ai Group did not offer evidence to support the claim that the extra superannuation co-contribution payment should be taken into account in evaluation of changes to the social safety net, is not credible. Paragraph 82 of Ai Group's submission contains the following balanced assessment:

*“The overall inter-temporal financial position of low-wage households without dependent children (including in relation to their capacity to meet their future needs) has been roughly preserved in real terms by the increase in the superannuation co-contribution payment. Nevertheless, the capacity of families without children to take advantage of the superannuation scheme has decreased due to the impacts of inflation.”*

R65. The improvement to the superannuation co-contribution scheme is an important addition to Australia's social safety net. There does not seem to be any reason to exclude this element of the social safety net from consideration when examining the needs of the low paid as long as future needs are regarded as important.

R66. Ai Group regards the future needs of low-income people to be important and views improvements to the social safety net in the form of improved returns to saving by low-income people as important enough to be considered by the Commission in its consideration of the needs of the low-paid. By their nature, improvements to the social safety net in the form of encouragements to saving do not improve current-year disposable income. That is no reason to regard them as insignificant.

R67. Indeed, given that the ACTU does not propose the Commission takes account of *any* changes in the social safety net in the current case, even though many of these changes have been substantial, it is difficult to take seriously their dismissal of Ai Group's argument that this particular change in the social safety net should be taken into consideration by the Commission.

## **R4 The Impact of Increases in Minimum Award Wages on Low Skilled Employment Opportunities**

R68. The central arguments in chapter 5 of Ai Group's submission were that:

- The underutilisation of casual and part-time workers and the high incidence of "hidden unemployment" add important dimensions to the consideration of the impacts of minimum wages on the employment opportunities for the low-skilled.
- The ACTU's use of evidence about the aggregate level of employment, particularly during a period of cyclical buoyancy of the labour market, to challenge arguments about a structural feature of the Australian labour market is inappropriate.
- The widely accepted nexus between high minimum wage levels and poor employment opportunities should be considered by the Commission in its deliberations particularly in relation to the needs of the low paid.

R69. The ACTU does not address the first of these arguments. In so doing it continues to put aside for the purposes of the Safety Net Review Case the concerns that it is prepared to express in other forums about the casualisation of the workforce and the desire many casual workers have for more hours of employment.

R70. In addressing the Ai Group's argument that evidence about aggregate labour market performance at a time of cyclical buoyancy is inappropriate in the context of assessing arguments about a particular structural feature of the labour market, the ACTU (at R4.3) states:

*“The ACTU recognises that observations regarding aggregate economic performance differ from issues of structural integrity of the economy. However, the ACTU continues to claim that a proper inference can be drawn from the facts. The facts speak for themselves. Unemployment is down, employment levels are up whilst Safety Net Adjustments have provided reasonable increases.”*

R71. The ACTU does not challenge Ai Group’s argument and in fact appears to recognise its validity. However, it then proceeds to re-use aggregate labour market evidence after contributing the dubious cliché - “facts speak for themselves”.

R72. Ai Group submits that facts rarely, if ever, speak for themselves. Facts are prone to be selected, ignored or misrepresented to suit particular arguments. This is very conspicuously the case with the ACTU’s arguments in relation to the association between high minimum wages and unskilled employment opportunities.

R73. For example, the ACTU (at R4.5) asserts that:

*“The International Monetary Fund’s theory is essentially that high minimum wages or increases in the minimum wage will result in higher levels of unemployment. We fail to see why it is not relevant to direct the Commission’s attention to the economic reality that the opposite has occurred in recent years in Australia.”*

R74. The ACTU’s claim that the IMF put forward an argument about aggregate levels of unemployment is clearly a misrepresentation of the IMF’s view that Australia’s minimum wage “has contributed to a relatively high unemployment rate *for low-skilled workers*”<sup>5</sup> (emphasis added).

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<sup>5</sup> International Monetary Fund, Country Report No. 04/353, Australia: 2004 Article IV Consultation – Staff Report; Staff Statement; and Public Information Notice on the Executive Board Discussion, November 2004.

- R75. Another misrepresentation of facts occurs at R4.5 where the ACTU assert that Ai Group (at paragraph 111 of Ai Group's submission): "concludes that the IMF study is of very limited use."
- R76. The study referred to in paragraph 111 of Ai Group's submission is very clearly not the IMF study. Ai Group's comments on the IMF study were concluded in paragraph 107 with the observation that comments by the ACTU "provide no reason to reject the IMF's statement." Ai Group's discussion then turned to a discussion of another study.
- R77. The ACTU misrepresents Ai Group's comments in relation to the other study as if they applied to the one by the IMF.
- R78. The ACTU is highly selective with its facts about labour market outcomes for low-skilled workers. As shown in Ai Group's submission (123-130), while the ACTU is prepared to be an enthusiastic supporter of current labour market outcomes during Safety Net Review Cases, in other forums it expresses a concern that low-skilled casual workers are unable to find the quantity of work they would prefer. This is despite the current cyclical buoyancy of the aggregate labour market. The ACTU's submission in reply omits reference to this discussion.
- R79. The ACTU also omits from its discussion of the association between Australia's high minimum wages and the employment opportunities for the low skilled, the valuable contribution by Fred Argy<sup>6</sup> in expanding the concept of joblessness to include discouraged workers and the unsatisfied demands for extra work of many casual and part-time workers.
- R80. The ACTU does not take this contribution on board and persists in characterising the argument in terms of the impacts on the official level

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<sup>6</sup> Fred Argy, 2005, "An Analysis of Joblessness in Australia", *Economic Papers*, Vol.24, No.1, pp. 75-96. See also Ai Group Submission Annexure 8.

of unemployment and the number of people in employment. For example, the ACTU states in its conclusion (R9.9):

*“There is no credible evidence before the Commission that granting the ACTU’s claim will result in job losses. The ACTU’s submissions should be preferred.”*

- R81. The conclusion that the association between Australia’s high minimum wage levels and poor employment opportunities for the low skilled would manifest itself in job losses is clearly a misrepresentation of the arguments before the Commission.
- R82. As pointed out by Ai Group (at 117), job losses are one possible manifestation of the association between minimum wages and employment outcomes for the low skilled. Others include slower than average growth of employment opportunities for the low-skilled; the inability of low-skilled casual and part-time workers to find the amount of employment they would prefer and high concentrations of unemployment among lesser skilled workers.
- R83. The ACTU also comments on the epistemological observations in Ai Group’s submission (116 to 122). Ai Group canvasses the difficulties in “proving” associations between economic variables particularly those that are subject to a variety of influences.
- R84. Ai Group put forward the moderate suggestion that, notwithstanding the difficulties in establishing incontrovertible proof, there is a clear logic to the association between high minimum wage levels and poorer employment opportunities for low skilled workers than would otherwise occur. Ai Group submitted that this logic itself is not damaged by the difficulties of establishing proof and that the Commission should nevertheless give weight to the logic of the association.

- R85. The ACTU's rhetorical response (at R.33): "[t]he Commission is urged to abide by a doctrine" is a another misrepresentation, this time about the modest suggestion that the Commission should give weight to an argument.
- R86. The unconstructive tone of this section of the ACTU's Submission in Reply continues with the suggestion that had Ai Group had its way
- "... Christopher Columbus would have been burnt at the stake as a heretic for claiming the world was round when the widely suggested logic was that the world was flat. The economic facts do not support the Ai Group's theory."*
- R87. The difficulty for the ACTU (apart from the narrow selection of facts it is prepared to entertain), is that analogies of this sort appear much more applicable to its own position than to that of those it is opposing. This is particularly the case considering the degree of misrepresentation; the shortage of sensible argument and the extent of recourse to rhetorical flourishes evident in this section of its argument.
- R88. Of course, despite all the filibustering and in sharp contrast to Columbus, the ACTU shies away from taking up the challenge put forward in Ai Group's submission (at 122) of taking on the burden of proof and showing the rest of the world that Australia's high levels of minimum wages *do not* impact adversely on the employment opportunities for the low skilled.

## **R5 Interactions Between Wages, Taxation and Income Support**

### **Ai Group's Argument**

- R89. The major argument in Chapter 6 of Ai Group's Submission is that there is a substantial discrepancy between the quantity of resources required to give effect to minimum wage increases (i.e. the total costs to employers) and the amount that families receive in the form of higher disposable income.
- R90. This discrepancy is expressed in the benefit to cost ratios calculated in Annexure 9. Ai Group claimed that, as a rough guide, adjustments to minimum wages are associated with benefit to cost ratios in a range centred around 50 percent. In other words, on average for every dollar of extra costs borne by employers, award workers receive 50 cents in disposable income.
- R91. This argument, together with the fact that many low-income earners are members of middle or high income families as well as the likelihood that increases in minimum wages is associated with poorer-than otherwise employment opportunities for the low skilled, provides the basis for the claim that minimum wage increases are a relatively inefficient means of addressing the needs of the low paid.
- R92. By way of clarification, Ai Group does not suggest that increases in minimum wages play no role in assisting low-income households meet their needs. Nor is there any suggestion that no wage increases should be granted (Ai Group is proposing an increase of \$11 a week).

## **Comments by the ACTU**

R93. The ACTU (at R8.41 to R8.47) raises a number of detailed issues relating to the measurement of benefit to cost ratios. As discussed below, none of these provide grounds to question the rough guide that the average benefit to cost ratio of minimum wage adjustments is in the order of 50 percent.

### **Effective marginal tax rates calculated in Table 3 of Annexure 9**

R94. The ACTU (at R8.42) questions the 36.5 percent effective marginal tax rate applying to single people with incomes in the range between \$550 to \$700 as shown in Table 3 of Annexure 9. No other effective marginal tax rates calculated by Ai Group are questioned.

R95. The 36.5 percent effective marginal tax rate over this range of incomes is the sum of:

- The 30 percent rate in the personal income tax scale;
- The 1.5 percent Medicare Levy
- The 5 percent shade out of entitlement to the superannuation co-contribution payment.

R96. As set out in the 2004-05 Budget Papers (Budget Paper No.2, p12), entitlement to the superannuation co-contribution payment is reduced when income rises above \$28,000 at 5 cents for every extra dollar of income and is phased out completely when income reaches \$58,000.

R97. Once a person's private income exceeds \$537 per week, entitlement to the co-contribution payment reduces for every extra dollar they receive. This shows up in the table for incomes over \$550 a week.

## **Over emphasis on sole parents**

R98. The ACTU (R8.43) suggests that Ai Group implies that sole parents comprise 33 percent of the workforce because the table relating to sole parents in Annexure 9 is 33 percent of the total number of tables in that Annexure.

R99. There is no such implication at all. The tables in Annexure 9 illustrate benefit to cost ratios with reference to a limited, though important, range of household circumstances. These are a single-income family with two children renting privately; a sole parent household and a single person household. There is no suggestion that this sample is exhaustive or that these three illustrations cover equal number of households. They merely set out a range of circumstances.

## **On - cost proportions**

R100. At R8.45 the ACTU uses Australian Bureau of Statistics (ABS) data relating to on - costs. It suggests an on-cost ratio of 11.9 percent for Small Businesses and 13.4 percent for all businesses. This can be contrasted to the range of on-costs of between 15 and 25 percent illustrated in Annexure 9.

R101. The question is whether these two ranges are measures of the same thing. As it turns out they are not. The Ai Group percentages are the percentage by which total costs of remuneration exceed wage payments. This is the relevant measure in the assessment of the extra non-wage costs arising from additional wage costs. The ABS percentages, however, measure a different ratio. Referring to the same survey report relied on by the ACTU, the ABS makes clear that it measures the ratio of on-costs as a proportion of "employee earnings". The category of employee earnings is much more than wages. It

includes:<sup>7</sup>

*“gross wages and salaries, the value of salary sacrificed (excluding fringe benefits tax), the ungrossed value of fringe benefits provided by employers through arrangements other than salary sacrifice, and severance, termination and redundancy payments.”*

R102. A given level of on-costs expressed as a percentage of this larger category will inevitably be a lower percentage than if the same level of on-costs is measured as a percentage of the smaller category of wages only.

### **Benefit to cost ratios**

R103. The ACTU use of the ABS data does not, therefore, provide any reason to suggest the range of the ratio of on-costs to wages used by Ai Group is inappropriate. The above discussion does, however, suggest that the ratios used by the ACTU are too low.

R104. As a consequence of these comments, there is no reason to substitute the ACTU's estimates of benefit to cost ratios (as set out in Tag R8 of the ACTU Reply Submission) in favour of those originally provided by Ai Group.

R105. In view of this there is also no reason to reject Ai Group's rough rule of thumb that the benefit to cost ratio of increases in minimum award wages is around 50 percent.

### ***Further illustration***

R106. By way of further illustration of the wedge between the costs to employers and the benefits received by employees, Ai Group provides

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<sup>7</sup> Australian Bureau of Statistics, Labour costs, 1301.0 – 2005.

for the Commission's information a set of tables at **Annexure B**.

R107. These tables show the degree to which disposable incomes increase and the degree to which employer costs rise due to increases in minimum award wages.

R108. The impacts of a range of alternative increases in the basic minimum wage of \$467.40 per week are included in illustrations.

R109. The tables in **Annexure B** illustrate the key points by isolating for illustrative purposes three different household types.

R110. These illustrations lend support to Ai Group's argument that the average benefit to cost ratio of changes in minimum award wages is around 50 percent.

## **R6 International Comparisons and Labour Costs**

R111. In Chapter 7 of Ai Group's submission, the pressures of international competition are referred to and these are supported by comparative data relating to the level of gross wages of average production workers in all OECD countries.

R112. The ACTU does not question that Australian businesses are currently under extreme pressure from competitors located in the rapidly emerging nations in Asia. This is notably the case of businesses in the manufacturing sector that are subject to intense pressures from the rapid growth of manufactured exports particularly from China. These pressures have been compounded by the very large appreciation of the Australian currency in recent years.

R113. The ACTU (R2.111 to R2.116) does raise several important points about the use of the gross wage data as calculated in the OECD *Taxing Wages* publication.

R114. Ai Group has no question with the ACTU's contributions about the use of this data as a less-than-definitive measure of comparative wages. Ai Group does nevertheless maintain that OECD data is useful as a general guide to comparative gross costs of employment (including employment-related taxes). We note that, in addition to the points raised by the ACTU, the data reproduced in the Ai Group submission (at 165) do not include the Australian superannuation guarantee which is a further cost related to employment in Australia.

R115. The data presented by Ai Group may not be a perfect measure of comparative costs of employment but it does provide a starting point from which more definitive comparisons can be made. The starting

point provided suggests that, for the category of the “average production worker”, the costs of employment in Australia are comparatively high even by OECD standards.

## **R7 Disproportionate Negative Impacts of Safety Net Adjustments on Small Business**

R116. In Chapter 8 of its March 2005 Safety Net Review Submission, Ai Group set out some important facts which highlight the disproportionate negative impact of safety net adjustments on small businesses, including but not limited to the following:

- A much higher proportion of award reliant employees are engaged in small businesses;
- The award-reliant employees engaged by small businesses are paid substantially less than the award-reliant employees engaged by larger businesses;
- On average, small businesses are much more likely to be impacted by safety net adjustments than larger businesses;
- Small businesses have less capacity to pay safety net wage increases than larger businesses;
- Over the past 15 years there has been a continuing relative decline in the profit share of the unincorporated sector which largely consists of small businesses.

R117. Nothing in the ACTU's reply submission detracts from the validity of the above statements. The ACTU has adopted a creative approach to interpreting ABS statistics which, when properly interpreted, clearly support Ai Group's assertions.

R118. When Ai Group filed its March 2005 Safety Net Review submission the latest statistics relating to the award-reliance of employees engaged by employers of different sizes were set out in ABS Cat. No. 6306 released on 26 March 2003. On 23 March 2005, the ABS released an updated version of this statistical report.

R119. **Table 2** and **Table 3** below update Table 4 and Table 5 from pages 64 and 65 of Ai Group's earlier submission. In the tables below, both the 2003 and 2005 results are displayed.

**Table 2 – Proportions of Award-reliant Employees by Employer Size**

Size of Employer	Proportion of Award-only Employees (%)	
	2003	2005
Under 20 employees	26.1	27.5
20 to 49 employees	32.4	30.9
50 to 99 employees	27.2	31.5
100 to 499 employees	22.2	20.7
500 to 999 employees	19.8	17.4
1000 and over employees	5.2	4.5
<b>Total</b>	<b>20.5</b>	<b>20.0</b>

Source: ABS Cat. No. 6306.0

**Table 3 – Average Weekly Total Earnings of Award-reliant Employees by Employer Size**

Size of Employer	Average Weekly Total Earnings (\$)	
	2003	2005
Under 20 employees	387.00	407.50
20 to 49 employees	401.70	465.20
50 to 99 employees	421.50	431.90
100 to 499 employees	466.10	477.10
500 to 999 employees	460.50	502.90
1000 and over employees	480.80	498.40
<b>Total</b>	<b>419.90</b>	<b>444.60</b>

Source: ABS Cat. No. 6306.0

R120. It can be seen from **Table 2** above that the latest statistics continue to show that a high and growing proportion of award-reliant employees are engaged by companies with up to 99 employees (89.9% in 2005,

up from 85.7% in 2003) whereas only a very small proportion of award-reliant employees work for companies with 1000 or more employees (4.5% in 2005, down from 5.2% in 2003.)

R121. **Table 3** above highlights that award reliant employees engaged by small businesses continue to receive much lower average weekly total earnings than those employed by larger businesses.

R122. As argued at paragraph 174 of Ai Group's March 2005 submission and as confirmed by the latest statistics - on average, small businesses are much more likely to be impacted by safety net adjustments than larger businesses.

R123. The AIRC should reject the ACTU's creative interpretation of the unpublished statistics set out in Table R5.1 of its reply submission. Clearly, award reliant employees are far more likely to work for smaller businesses than larger businesses. For example, 68.9% of such employees work for businesses with up to 99 employees and only 6.1% work for businesses with 1000 or more employees.

R124. At paragraph R3.4 on page 56 of its submission, the ACTU uses the following definitions of business size:

Small	0 to 19 employees
Medium	20 to 99 employees
Large	100 plus employees

R125. The ACTU appears to have created its own definitions for the convenience of its arguments.

R126. Small businesses are defined differently in various laws, codes, statistical reports and other instruments. In many cases business size is not defined with reference to employee numbers but rather with

reference to turnover, income, value of assets or some other measure. Where employee numbers are used to define the size of a company, significant differences exist with regard to the definition of a small business, as highlighted below:

<i>Corporations Act</i>	Fewer than 50 employees
<i>ABS Small Business in Australia</i> (ABS 1321.0)	Fewer than 20 employees
<i>ABS Employed Wage and Salary Earner</i> (6248.0) and <i>The Labour Force</i> (6203.0)	Fewer than 100 employees (manufacturing); and Fewer than 20 employees (other industries)
<i>ABA Banking Code of Practice</i>	Fewer than 100 employees (manufacturing); and Fewer than 20 employees (other industries)

R127. Regardless of what definition of “small business” is used, it is clear from Table R5.1 in the ACTU’s reply submission that the smallest businesses (those with under 20 employees) have the largest proportion of “award only” employees (39.4%) and the largest businesses (those with 1000 or more employees) have the smallest proportion of “award only” employees (6.1%).

R128. The small business sector is the largest employer in Australia, with well over three million people employed within 1,162,000 small

businesses.<sup>8</sup>

R129. The ACTU's statement at paragraph R3.7 of its reply submission, that wage costs were not identified as a barrier during the Senate Inquiry into Small Business is misleading. The Senate Committee reported that: *"The cost of employing staff was raised as a deterrent to employment by a number of witnesses"*<sup>9</sup>. The costs referred to by the ACTU at Paragraph R3.7 – that is, superannuation, penalty rates and payroll tax – are directly related to wage costs.

R130. Given the disproportionate negative impact of safety net adjustments on small businesses, care needs to be taken by the Commission in determining the level of minimum wage adjustment to avoid damaging this vital sector of the Australian economy.

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<sup>8</sup> *Small Business Employment: Research Note*, Department of Parliamentary Library, September 2002.

<sup>9</sup> Final Report, p.49

## **R8 The ACTU's Claim is Inconsistent with the Objects of the Act**

R131. As set out in paragraph 193 of Ai Group's March 2005 Safety Net Review Submission, safety net adjustments need to be pitched at a level below average enterprise agreement outcomes to avoid diminishing the primacy which is given to enterprise agreement-making under the Act. The ACTU's proposed increase of 5.7% for employees on the Federal Minimum Wage is inconsistent with the objects of the Act.

R132. In response to this point, the ACTU has taken exception to Ai Group's rounding of 5.7% to 6%<sup>10</sup>. Ai Group is happy to concede that the non-rounded figure of 5.7% is more accurate.

R133. The ACTU also seeks to assign great weight to the fact that an employee at Level C1b of the *Metal Engineering and Associated Industries Award* would receive an increase of only 2.6%. As the ACTU is well-aware, employees in this classification are engineers or scientists with a considerable amount of experience and expertise. There are relatively few employees classified at Level C1b compared to the number of employees classified at lower levels. Also, very few experienced engineers or scientists receive the award rate of pay or have their salaries adjusted via safety net wage increases.

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<sup>10</sup> ACTU Reply Submission, Para R5.12.

## **R9 Conclusion**

R134. The level of increase proposed by the ACTU is unaffordable and would damage the Australian economy with consequent negative effects for employers and employees.

R135. Over the past year, the low paid – particularly those with children – have received massive increases in income support payments. This should be taken into account by the AIRC and the amount that the Commission would otherwise have awarded should be substantially discounted.

R136. In weighing up all the relevant issues, an \$11.00 per week safety net wage increase is appropriate.