THE *FAIR WORK ACT* – THE BARRIERS TO PRODUCTIVITY IMPROVEMENT NEED TO BE ADDRESSED

SPEECH TO THE 10th ANNUAL WORKFORCE CONFERENCE

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Workforce has scheduled this Conference at a very apposite time. The arguments in support of amending the *Fair Work Act* to address Australia's dismal productivity performance are getting louder and they are coming from widening quarters.

Of course, changes to the *Fair Work Act* alone cannot deliver the productivity growth that Australia needs. This will require action in a number of areas including in training and education, in infrastructure, in our taxation systems and in our convoluted regulatory systems. However, raising productivity also requires action in individual businesses and where provisions in the Act are presenting barriers to productivity improvement, the Act needs to be amended in ways that preserve fairness for employees, employers and others in the community.

The idea that the *Fair Work Act* represents the perfect balance between all the competing interests and should not be altered is simply not sustainable. It is common for new, major pieces of legislation to lead to unintended consequences and unforseen issues and the *Fair Work Act* is no exception.

The *Fair Work Act* has been in place for over two years and it has been vigorously tested by the Australian Industry Group (Ai Group). We have pursued 13 appeals against worrying bargaining decisions of single members of Fair Work Australia (FWA), with much success, but in a number of areas the legislation has been found wanting.

Recently we conducted a comprehensive survey of our members to obtain their views on the Act. The survey results support the case for change and I will outline some preliminary results later in my speech.

Any country which freezes its workplace relations system in time and decides that no further improvements are desirable or necessary, will subject its citizens to low levels of productivity growth, reduced employment, reduced competitiveness, and harsh effects from globalisation.

Arguments that employers are failing to take advantage of the bargaining provisions of the *Fair Work Act* to increase productivity largely miss the point. Yes, there are occasions when employers and employees will want to negotiate specific provisions aimed at improving productivity but, more often, what leading employers want is legislation and industrial instruments which allow them to focus on productivity improvement every day. They want legislation and industrial instruments which do not impose barriers to productivity improvement such as clauses which impede outsourcing, or restrict the use of contractors, or prevent individual flexibility arrangements being negotiated with employees, and so on.

Ai Group operates in the real world and we are not advocating a wholesale revamping of the legislation but some sensible changes need to be made aimed at removing barriers to productivity growth.

The need for an open and thorough review

Senator Chris Evans, the Minister for Tertiary Education, Skills, Jobs and Workplace Relations has announced a review of the Act from 1 January next year. The review needs to be thorough and open. A timetable and process should be announced without delay so that all interested parties can start preparing their evidence and submissions, and the necessary amendments are made to the Act as soon as possible.

Ai Group intends to play a major role in the review to inform the Government about the experiences of our member companies, and to argue the case for constructive changes to be made.

No doubt there will be a lot of changes proposed by different parties – some will have merit and others will not. We will be urging the Government to pay particular attention to the need for barriers to productivity growth to be removed from the Act. The preservation of workplace flexibility is at the centre of this.

On 26 August 2011, Glenn Stevens, Governor of the Reserve Bank of Australia said:

> *"What people say to me, I cannot verify it obviously, from their individual businesses is that they find it harder to negotiate flexibility. That is something that is said. If that is true that I think is a matter for concern."*[1]

On 4 August 2011, in its draft report on the Australian retail industry, the Productivity Commission said:

> *"Given the existing productivity gap between Australia and countries such as the United States, even greater improvements will be needed to help close this gap. Among other things, this will require greater workplace flexibility so that employers and employees can work cooperatively and creatively together, to deliver the required productivity improvements."*[2]

Earlier this year, on 24 March, in its incoming brief for the Australian Government, The Treasury said:

> *"A close watch will also need to be kept on the labour market: while the evidence to date is that the labour market continues to be flexible, it will be important to guard against any developments that might put flexibility at risk."*[3]

We have kept a close watch on the labour market under the *Fair Work Act*. There is now evidence that some sensible changes need to be made to the legislation to address developments that are putting flexibility at risk.

Closing the cost gap through increased productivity

Australian companies face a major cost gap.

Clearly, the higher dollar is a major factor in this. Recently the Australian dollar has hovered around $US1.06. This compares with a post-float average of around $US0.73. An appreciation of this size means that, even without any changes in actual wages, wages paid in Australian dollars rise by 45% against wages paid in the $US (or in countries whose currency is tightly linked to the $US).

This 45% change in relative wages does not factor in any counteracting changes in wages paid or, critically, productivity. And, when the currency appreciates, the hope of the side comes to rest very heavily on these factors. Here, however, we have bad rather than good news.

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[1] Hearing of the House of Representatives Standing Committee on Economics.

[2] *Economic Structure and Performance of the Australian Retail Industry*, Draft Report, p.286.

[3] The Treasury, Incoming Government Brief, Overview, p.14.

For a number of years relative productivity growth in the manufacturing sector has moved in exactly the wrong direction. Instead of rising faster than in other countries, and helping to offset the negative impacts of the appreciation of the exchange rate on our competitiveness, productivity growth in Australian manufacturing has been slower than in other developed countries.[4] This relative performance has exacerbated the set back to competitiveness due to the higher Australian dollar. As a result we have seen a major cost gap open between Australia and competitor countries.

We need to move quickly to close the cost gap through, firstly, ensuring that wage outcomes are moderate and, secondly, achieving substantial and sustained productivity growth. The signs are not good in either area.

There is no question that, particularly under the current industrial arrangements, productivity gains are harder to win whether in manufacturing businesses or in other industries.

Last week the Managing Director of one of our member companies sent me an email in response to the current public debate about productivity. He explained that his expensive machinery sits idle in the evenings even though he has plenty of demand for his products and had intended to employ workers for an afternoon shift. However, under the *Fair Work* modern award system, the afternoon shift loading applicable to his glass manufacturing workers increased from 15% to 50%[5] and as a direct consequence he has decided to leave his machinery idle after the day shift and to import the glass products he would otherwise have made. He also mentioned a new product that the company has developed. Rather than investing in the capital equipment to manufacture it in Australia, the company has decided to have it manufactured in Singapore.

This experience of being subjected to higher penalty rates is shared by other companies in sectors such as retail, fast food and restaurants.

The Managing Director of another Ai Group member company told me last week that his organisation's plants in Asia make exactly the same products as his Australian plant, and make them to the same standards using workers with similar education and skills. The workers in Australia are paid up to 6-8 times what the Asian workers are paid, and the only way that the Australian plant is going to be able to close the gap is through higher levels of productivity and flexibility.

[4] United States Bureau of Labour Statistics, December 2010.

[5] Phased in via the standard transitional arrangements in modern awards.

An important means of assisting companies to close the cost gap and to achieve higher productivity is to ensure that legislative provisions which promote productivity destroying workplace practices are redressed. I'll come to this issue shortly.

The impact of the *Fair Work Act* on productivity and flexibility – the views of employers

In August, Ai Group conducted a detailed survey of our member companies on the impact of the *Fair Work Act*.

More than 250 employers responded and the survey provides a good insight into the views and experiences of employers – large and small. It will take some time to analyse the results, but even a quick snapshot highlights some critical issues.

Firstly, about 80% of employer respondents said that they were very concerned or somewhat concerned about the wage expectations of their employees over the next 12 months.

Secondly, their views on productivity and flexibility were insightful.

Of those employer respondents who had experienced an increase in productivity since the *Fair Work Act* came into operation, almost none attributed it to the *Fair Work Act*. In contrast, of the employers who had experienced a decrease in productivity, nearly two thirds said that the *Fair Work Act* was an important factor in the decrease.

Similarly, of those employers who had experienced an increase in labour flexibility since the Act came into operation almost none gave any credit to the *Fair Work Act*. Of the employers whose workplaces had become less flexible, over 80% said that the *Fair Work Act* was an important factor in the loss of flexibility.

The survey respondents were asked if they had made an enterprise agreement under the *Fair Work Act*. Of the 82 who had, nearly half (37 employers) reported that the agreement contained new restriction/s.

It appears that the larger the company, the greater the barriers to productivity and flexibility imposed by the *Fair Work Act*. 74% of large employers (500 or more employees) reported that the *Fair Work* bargaining laws had made it more difficult to negotiate flexibility or productivity improvements.

These results point to two things. Firstly, in itself the *Fair Work Act* has not delivered increased productivity or flexibility to Australian employers. Secondly, the Act has introduced barriers to productivity growth and labour flexibility which need to be addressed.

Barriers to productivity and flexibility

Some of the barriers to productivity growth and labour flexibility which need to be addressed through amendments to the *Fair Work Act* are:

1. Provisions which restrict the engagement of contractors and on-hire workers;
2. The lack of a workable form of agreement which provides flexibility to employers and individual employees;
3. Increased union power, including the ability for unions to disturb lawful and fair workplace arrangements which are supported by the majority of employees in a workplace;
4. Ill-conceived transfer of business provisions; and
5. General Protections provisions which are too loose and uncertain.

I will discuss each of these areas in turn.

1. Provisions which restrict the engagement of contractors and on-hire labour need to be outlawed

Prior to the *Fair Work Act* coming into operation, enterprise agreements and awards were not permitted to include provisions which imposed restrictions on the engagement of contractors (individuals or companies) or on-hire labour.

The merits of the former prohibition are obvious. The use of contractors and on-hire labour are two important means by which companies maintain the flexibility to match the supply of labour with demand for their products and services. Flexibility in this area also enables companies to outsource work to contractors who, through specialisation, are often able to carry out the work more efficiently.

The typical clause sought by unions requires consultation with the union before contractors can be engaged plus a requirement to pay "site-rates". In reality this often means that contractors who do not have an agreement with the union do not get any work.

These types of claims are currently being pursued across the construction, manufacturing, transport, aviation, mining and other industries.

It is easy to be critical of an employer who concedes such a claim during enterprise agreement negotiations but faced with damaging industrial action, or pressure to sign union pattern agreements, some employers feel that they have no option but to capitulate.

Ai Group has pursued an appeal in the *ADJ* case.[6] We have argued that the contractor clause in the Communications, Electrical and Plumbing Union's pattern agreement for the Victorian electrical contracting industry breaches the *Competition and Consumer Act 2010* and the General Protections under the *Fair Work Act*. The FWA Full Bench has not yet handed down it decision.

Whatever the outcome in the *ADJ* case, provisions which impose restrictions on the engagement of contractors or on-hire workers need to be expressly outlawed under the *Fair Work Act*.

In the meantime, the Australian Government and State Governments need to use their purchasing power to enforce the Implementation Guidelines for the National Construction Code. The current Guidelines outlaw enterprise agreement clauses which require the names of contractors to be provided to unions. The Australian Government's decision to deem all *Fair Work* enterprise agreements to be Code-compliant, even if they contain clauses which directly conflict with the Implementation Guidelines, has been very damaging and should be immediately reversed. State Governments should follow the Victorian Government's lead[7] and develop their own IR guidelines to preserve the construction industry reforms which have been so successful but which are being eroded day by day.

2. A workable form of agreement which provides flexibility to employers and individual employees is needed

Since 1996, the Australian workplace relations system has included provisions which allow statutory agreements to be reached between employers and individual employees.

[6] Appeal by Ai Group against the decision of Senior Deputy President Acton to approve the *ADJ Contracting Pty Ltd Enterprise Agreement 2010-2014*.

[7] In late June 2011, the Victorian Government announced a review of its *Industrial Relations Principles* for the building and construction industry. The Principles apply to firms tendering for Government work.

For more than a decade Australian Workplace Agreements (AWAs) provided important flexibility to employers and individual employees. Ai Group opposed their abolition, arguing that statutory individual agreements underpinned by a “no disadvantage test” are fair and in fact provide far more protection to employees than common law contracts.[8]

This remains our position. The results of our survey show that most employers want the *Fair Work Act* changed to reinstate statutory individual agreements. 69% of respondents stated that they would like to see some form of statutory individual agreement option introduced into the *Fair Work Act*, with 12% saying No and 19% Unsure. The views were even stronger amongst large employers. Over 80% of the employers with over 500 employees wanted the Act to be amended to permit statutory individual agreements.

To some extent, the Labor Government has acknowledged the need for a form of individual agreement which can override the terms of awards and collective agreements, through its conception of flexibility terms and Individual Flexibility Arrangements (IFAs).

During the development of the *Fair Work* system, the Government stated that IFAs would remove the need for individual statutory agreements such as AWAs because they would provide the ability for employers and individual employees to agree on arrangements which suit their needs subject to the employee not being disadvantaged.

IFAs promised so much but have delivered so little. Timing issues have contributed to some of the problems.

The Australian Industrial Relations Commission (AIRC) developed the model flexibility clause for modern awards in mid-2008 before the *Fair Work Act* had been drafted. The Tribunal adopted a conservative approach in formulating the model flexibility clause, in part because of the lack of certainty regarding the legislative provisions. The Tribunal decided to:

- Allow flexibility in five areas only;
- Not extend flexibility to leave entitlements (because the National Employment Standards (NES) had not been finalised);
- Prohibit IFAs being offered as a condition of employment; and

[8] Advantages of statutory individual agreements to employees are that they would be: Vetted and approved by a statutory body; Subject to a better off overall test; Subject to a maximum nominal term; Easy to enforce; Subject to specific penalties; and covered by the General Protections. These advantages do not apply to common law contracts.

- Enable IFAs to be terminated by an employee with four weeks' notice.

In June 2008, the Full Bench of the AIRC said:

> *"For a number of reasons, it is obviously desirable that there be a review of the operation of the model flexibility clause after it has been operating for a reasonable period. This review would provide an opportunity to assess whether the clause has achieved its purpose of providing flexibility to meet the genuine individual needs of employers and employees."*[9]

Unfortunately, when the Government was drafting the *Fair Work Act* in late-2008 it based the relevant provisions in the Act (concerning flexibility terms in awards and enterprise agreements) on the Tribunal's model flexibility clause for awards. Therefore, the Tribunal's initial, conservative approach has largely been locked-in to the *Fair Work Act*.

If the provisions had not been locked-in to legislation, FWA's 2 yearly review of modern awards, required to commence as soon as practicable after 1 January 2012, would have provided the ideal opportunity to highlight to the Tribunal that the following aspects of the model flexibility clause need to be addressed:

- The four week termination provision prevents an employer using an IFA as part of a wage bargain with an employee. Flexibility should be provided for IFAs to have an agreed nominal term of up to four years, with no ability to unilaterally terminate the IFA during the term.
- Similar to AWAs, employers and individual employees should have the right to incorporate an IFA into the contract of employment at the commencement of employment.
- Leave provisions should be included within the scope of the clause. For example, an employer and an individual employee should be able to enter into an IFA to cash out a proportion of the employee's accrued annual leave on similar conditions to those in s.93 of the *Fair Work Act* (e.g. only accrued leave in excess of four weeks should be permitted to be cashed out).

A further problem is that, at the present time, unions are routinely refusing to sign enterprise agreements unless the flexibility term blocks any meaningful flexibility.

[9] [2008] AIRCFB 550, para [192]

Legislative change is needed to ensure a workable structure for IFAs. The parameters and conditions for individual flexibility need to be set out in the Act, with no ability for awards or agreements to detract from that framework.

3. Increased union power, including the ability for unions to disturb lawful and fair workplace arrangements which are supported by the majority of employees in a workplace

Under the *Fair Work Act*, collective agreements are not separated into union agreements and non-union agreements. The merits of this can be debated but one thing is clear - many employers are encountering problems with unions seeking to use provisions of the *Fair Work Act* to disturb workplace arrangements which are supported by the majority of their employees.

This issue is playing out in various ways:

- Some employers have reached agreement with their employees and sought to put the enterprise agreement to a vote of employees, only to find that at the last minute a union representing only a few employees obtained a bargaining order from FWA delaying the vote.
- An employer (JJ Richards) which did not have an enterprise agreement, nor want one, became subject to an FWA protected action ballot order even though no bargaining had taken place and the union had not obtained a majority support determination to test whether the majority of employees actually wanted a collective agreement.
- Unions with only one or a few members in a workplace have become covered under enterprise agreements, a right which they have been granted under the *Fair Work Act*.
- Unions have used scope orders to force employers to bargain for national agreements and/or agreements across several related companies when the employer has wanted to enter into separate agreements with its employees in particular workplaces. An agreement for a particular workplace allows the employer and the employees to tailor the agreement to their particular needs.

There are other problems being encountered due to the increase in union power granted under the *Fair Work Act*. When the Act came into operation, Ai Group identified more than 60 provisions of the legislation where the role and powers of unions had increased.

Under the *Fair Work Act*:

- Unions are insisting upon extremely generous and highly restrictive provisions in greenfields agreements, which are driving up construction costs. Prior to the *Fair Work Act*, an employer was able to enter into an employer greenfields agreement or an agreement with a union eligible to represent only a minority of employees. The loss of these former options has shifted the bargaining power in favour of unions with very negative consequences for head contractors, who often need to reach an agreement before a project starts to manage their industrial risk, and negative consequences for the community which ultimately pays for the higher construction costs.
- Pattern bargaining is rife in some industries and the unions have been able to include a wide range of highly unproductive and inflexible provisions in pattern agreements and impose these on employers given the breadth of the "permitted matters" under the Act and the ability for parties to include non-permitted matters in agreements.
- Union entry rights into workplaces have been expanded substantially under the *Fair Work Act*. The ability for enterprise agreements in some circumstances to include right of entry provisions granting even more expansive rights has exacerbated the problems.

Not surprisingly, of the respondents to Ai Group's survey:

- 64% expressed the view that union power had increased in the enterprise bargaining process, with only 13% having the opposite view;
- 86% of large employers (over 500 employees) said that union power had increased in the bargaining process;
- 29% of employers with union involvement in their workplace said that the unions had become less cooperative under the *Fair Work Act* with only 4% finding them more cooperative;
- 39% of the employers said that union officials had visited their workplace more often since the Act came into operation, with only 15% experiencing less visits.

4. The transfer of business provisions are ill-conceived

The transfer of business provisions of the *Fair Work Act* are important because they often apply when employers want to restructure their businesses, such as merging divisions, divesting unprofitable operations or outsourcing.

In the late 1990 and early 2000s, there was a huge amount of litigation in the High Court of Australia and Federal Court of Australia relating to the transmission of business provisions in the *Workplace Relations Act*. Eventually the issues were resolved in a sensible and fair manner, but inexplicably the *Fair Work Act* was drafted in a manner which largely swept aside the previous sensible case law.

The laws are operating against the interests of employers and employees. The *Fair Work Act* provides many reasons for a company not to outsource work, even if it would be more efficient to do so. The Act also provides many reasons for employers taking on outsourced work to not employ any employees of the client company even if all parties want the transfer to occur.

Ai Group's survey highlights the problems. 31 respondents had been involved in a transfer of business under the *Fair Work Act*. Of these companies:

- 52% of employers said that the provisions of the Act had a very negative impact or somewhat negative impact (NB. only 1 employer said that the provisions had a positive impact);
- 62% of large employers cited a very negative or somewhat negative impact; and
- 13% said that employees were made redundant who would have otherwise been employed by the new employer.

Sensible changes are needed to the transfer of business laws, including reinstating the High Court's "character of the business test" which requires that two employers have the same character before transfer of business implications arise. The alternative "similarity of work" approach which has been adopted for the *Fair Work Act* was held by the High Court[10] to be problematic and inappropriate.

[10] See *PP Consultants Pty Ltd v FSU* [2000] HCA 59

5. The general protections are too loose and uncertain

The General Protections in the *Fair Work Act* are laws dealing with freedom of association, termination of employment for an unlawful reason, coercion, discrimination, sham contracting and other topics. The laws are extremely broad and are routinely being used by unions and lawyers to threaten employers and to drag them into conciliation proceedings in FWA, often over highly speculative claims.

The laws are so broad that unions and employees who wish to oppose restructuring efforts often allege companies are breaching aspects of the General Protections.

For example, 83 respondents to Ai Group's survey stated that the *Fair Work Act* had made it more difficult for their organisation to make employees redundant with 41% (34 employers) citing the risk of a General Protections claim.

Many of the General Protections claims relate to employees who do not have access to the unfair dismissal laws (e.g. because they have only been employed for a short period of time, or have not filed an unfair dismissal claim within the required 14 day period).

Of the approximately 250 respondents to Ai Group's survey, 18 said that a General Protections application had been made against their company, with 28 stating that they had been threatened with a claim.

Of those subject to a General Protections application:

- 61% chose to pay compensation to settle the claim before it was dealt with in Court;
- 72% expressed the view that the claim had no merit;
- 78% stated that the claim was pursued as a General Protections claim because the provisions are more favourable to employees than the unfair dismissal laws;
- 72% stated that the General Protections provisions are too loose and encourage speculative claims

The above results demonstrate that it is far too easy for unions and lawyers to pursue General Protections claims and subject employers to FWA conciliation processes, even where claims have no merit.

Some sensible changes need to be made to achieve a better balance, including the following:

- For claims relating to termination of employment, applications should be required to be lodged within 2 weeks of the termination and a compensation limit of six months' pay should apply (similar to the unfair dismissal laws);
- For claims which do not involve dismissal, FWA should only be permitted to schedule a conciliation conference if all parties have agreed in writing to a conference being held (prior to the conference being scheduled);
- In determining the reason why an employer took a particular action, only the "sole or dominant reason" should be taken into account; and
- Consistent with standard principles of justice, the reverse onus of proof should be abolished with the applicant required to prove that a breach of the law has occurred.

Conclusion

The *Fair Work Act* has been in place for over two years. It has been rigorously tested and some problems have been identified.

The Government needs to move to address the problems rather than continuing to argue that the Act is working well in the face of evidence that it is not in some areas. The Opposition needs to work with the Government to address the problems. It is vital that the major parties find common ground on workplace relations given the retrograde IR policies of The Greens who now hold the balance of power in the Senate.

The common ground should be the need to reduce barriers to productivity growth and labour flexibility. It is beyond contention that Australia's productivity performance needs to be urgently addressed if Australian companies are to survive, and Australian workers are to enjoy higher wages and higher living standards in the future.