Chapter Three

Australian Democrats' Report

3.1 The *Workplace Relations Amendment (Protecting the Low Paid) Bill 2003* proposes to narrow the adjustment of the award safety net to focus on the lowest paid. The Bill aims to compel the AIRC to give even greater consideration to:

- the needs of the low paid, including their need for employment;
- the employment prospects of the unemployed; and
- the capacity of employers to meet increased labour costs.

3.2 The *Workplace Relations Act 1996* specifies the matters that may be included in over 2 000 federal awards. Presently only about 20 per cent of employees rely on awards as their pay-setting method.

3.3 The wage and salary rates in those awards constitute the federal award safety net, designed to provide employees with fair minimum wages and conditions, and it is the responsibility of the Australian Industrial Relations Commission (AIRC) to maintain that safety net.

3.4 In maintaining that safety net, Section 88B(2) specifies that the AIRC must have regard to:

- the need to provide fair minimum standards for employees in the context of living standards generally prevailing in the Australian community;
- economic factors, including levels of productivity and inflation, and the desirability of attaining a high level of employment; and
- when adjusting the safety net, the needs of the low paid.

3.5 Nevertheless, it is clear that the Government prefers agreement making to safety net adjustments to awards as a more sensitive market mechanism than the method the AIRC employs through setting wage fixing principles under the Act.

3.6 The Government also has a desire to reduce costs to employers by lowering the annual increase awarded by the AIRC.

3.7 Section 88B(2)(b) already factors in a consideration of economic and employment considerations. The Bill goes further. The Bill sits on the premise that the employment prospects of the unemployed are likely to be detrimentally affected by upward adjustments of minimum award wages. With that in mind they wish to constrain potential increases.

3.8 This sets up a potential clash between the Act's requirement that living standards of low wage earners be maintained or improved, and a desire to reduce the cost of labour to maximise employment. If you concentrate on the former the fear is that you can price labour too high, and if you concentrate on the latter the fear is it will be a race to the bottom and poverty.

3.9 The Democrats contend that because Section 88B(2)(a) requires adjustments in the context of living standards, living standards have to be assessed against what a set wage or salary can actually buy, and how that compares with living standards for the community generally, and whether they are improving (or not).

3.10 Such an assessment can only be made in relation to disposable income (not gross income), and to assess net income requires an understanding of the effects of tax and welfare offsets or imposts at particular income, familial, or demographic levels.

3.11 The Democrats have a very clear view. Maintaining or raising living standards of low income wage earners, or moving the unemployed from welfare into work can not be addressed principally through the AIRC and cannot be done in isolation of tax and welfare policy.

3.12 While the Committee Majority report chose not to address this issue at any length, it has to be addressed. The present system has clear limitations.

3.13 Analysis of previous safety net decisions shows that the AIRC have taken into account economic factors, including productivity and employment, and the needs of the low paid.

3.14 Our concern, along with others[1], is that the AIRC will be compelled to accept arguments it has previously rejected as without merit.

3.15 The AIRC do consider the employment prospects of the unemployed when making their decision. The following statement demonstrates this:

> We accept that, whilst there is no automatic relationship between the two, real wage growth can adversely affect aggregate employment growth. The extent of such effect will depend upon the prevailing economic circumstances and the extent of the real wage movement. The limited addition to aggregate wages cost associated with our decision will not have a significant real wages effect.[2]

3.16 The ACTU submission contends there has been no increase in unemployment, in fact to the contrary, as a result of Safety Net increases in 1998, 1999, 2000, 2001, and 2002.

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1 Submission 4 - ACTU pg 3

2 *Safety Net Review-Wages April 1999* PR00 2002 para 108

3.17 The argument to reform the intersection between welfare and tax is in our view a more compelling case for improving prospects for the unemployed.

3.18 In their submission to the Committee, the ACTU showed that the 'gap between the wage rates of award based employees and the community generally, as measured by Average Weekly Ordinary Time Earnings (AWOTE) has been increasing. The Minimum Wage (or C14, the lowest wage rate payable under any award) has fallen below 50 per cent of AWOTE for the first time'.[3]

3.19 I was surprised that one of the arguments put forward against safety net increases across the board, was because a high proportion of employers passed the Safety Net increase on to over award employees, even though there was no obligation on them to do so. It is surely not the fault of the AIRC that employers choose to do this, and perhaps it is more indicative that employers recognise the need for wage increases that are not tied to productivity to keep up with inflation and the cost of living.

3.20 The Democrats also see the merit of a Safety Net in providing a 'no disadvantage test' as a base for enterprise bargaining.

3.21 The Government argues that by implementing the Bill and compelling the AIRC to adhere to new guidelines that this will somehow strengthen its role in encouraging bargaining at the workplace level. There is no evidence to suggest that this would in fact be true, except for the Minister and the Department saying it would be true.

3.22 Agreement making has significantly increased in the seven years of the Act's operation, and there is no evidence its growth has been limited in the manner suggested.

3.23 One of the telling and valid criticisms of the present system has been that it delivers relatively low net income increases to wage earners and relatively high gross costs to employers.[4]

3.24 The Democrats are sympathetic to the argument that the safety net raises the costs of a wide range of wage-related expenses for employers including over-time payments, worker's compensation, leave loadings, penalty rates and superannuation. Evidence suggests that this can have adverse effects on employers either resulting in increased cost to consumers or adversely affecting hiring and investment decisions.

3.25 The Democrats have noted this in several media releases and speeches in relation to minimum wage increases. While the capacity to pay could be more easily absorbed by large business the Democrats are aware that it is predominately small and

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3 Submission 4 - ACTU

4 Hansard EWRE p. 17 Tuesday 27 May 2003

medium sized business that rely upon awards and are thereby more adversely affected by increase wage costs.

3.26 In my view there is not enough evidence to demonstrate that the amendments proposed in this Bill will address the legitimate needs of all stakeholders – employees who deserve a better deal, and employers who are squeezed by rising gross costs.

3.27 While the Democrats support an industrial relations system that maximises and balances productivity, jobs growth and job security while ensuring fair and just pay conditions and treatment; and have always supported the AIRC decisions to increase the wage safety net[5]; we believe that the living standard/employment/costs conundrum can be more effectively dealt with through the tax and welfare system.

3.28 The difficulty with living wage increases is that they increase gross wages and add-on costs. For every living wage increase, an employer is faced with additional superannuation contributions, workers compensation payments and payroll tax.

3.29 The employee does not obtain any immediate benefit from the employer's on-costs. Instead they are also hit with additional taxes, so, in cash terms, they may only end up with half of the real cost to the employer.

3.30 For example, for the employer, the $17 increase is compounded by higher payroll taxes, superannuation, worker's compensation and other on-costs, resulting in an effective $20-$23 increase. For the employee, for every dollar increase in wages, some low-income workers can lose 70 cents in welfare benefits. Since they have to pay 17 cents income tax as well, this can lead to a crippling effective tax rate of 87 cents in the dollar. So in their hands $17 may drop to $8-$10 net.

3.31 In the words of the submission by the Australian Industry Group, 'Safety net wage increases represent a very poor 'bang for the buck' as far as low-income households are concerned'.[6]

3.32 What we need is a system that increases the real disposable income of low-income employees.

3.33 The key area for the Government to be examining is that the minimum living standards are met. Then, that income tests should reward and acknowledge attempts to work and supplement income while, at the same time being withdrawn at an appropriate rate as employment income increases.

3.34 This is a complex issue. At the moment there are 17 different pensions and income support allowances. They all have different income and asset tests. In some cases this is appropriate, as the Government should be providing more incentive for someone on the Newstart Allowance to get off welfare than an age pensioner.

5 As has the Government, interestingly. Hansard EWRE p.3, Tuesday 27 May 2003

6 AiGroup, Submission 18, page 6

3.35 The unemployed are in the unfortunate position of knowing that if they get a job they may be only 13 cents in the dollar better off for their efforts. After taking into account transport costs, clothing and additional food expense, they may not be better off at all.

3.36 The National Centre for Social and Economic Modelling analysis shows that 22 percent of the poorer half of the nation face effective marginal tax rates of more than 60 percent. One in two working sole parents face similarly high effective marginal tax rates. These statistics do not include the high number of people that are discouraged from entering the workforce by these poverty traps.

3.37 Minister Abbott amongst others has been rightly arguing for more effort to be made in this policy field. While the most disadvantaged in our society have a right to be given income support and treated with respect, our tax and welfare systems need to be changed to interact in a way that encourages welfare to work.

3.38 The Democrats are open-minded about considering various options to achieve change.

3.39 One of the promising areas of reform is the concept of the tax credit. Tax credits are designed to soften the impact of high effective tax rates. We know that there are plenty of savings that can be made. These could be redirected into a tax credit system to reduce the high effective tax rates faced by a person moving from welfare to work.

3.40 It is clearly important to consider tax credits as one way of getting more people off welfare. It is hard to believe that Prime Minister Howard has apparently already ruled out this idea, without suggesting an alternative.

3.41 Proposals have been around for many years[7]. One of the so called ‘five economists’ developed a specific tax credit proposal providing a tax-free tax credit of the order of 2 per cent that would be paid as a supplement to the wage of low wage earners in low-income families as an alternative to a living wage increase.

3.42 There is an urgent and large need for a system that delivers significant real disposable income increases for the low and lower paid, to encourage a move from welfare to work, to deliver social equity, and to give working people a chance to get off the floor and aspire to upward mobility for their families.

3.43 The Democrats both before and after the budget explained how the only fair way to provide equal tax cuts to all Australians was to increase the tax-free threshold. This would go a small way to reducing the high effective marginal tax rates.

[7] Refer Keating and Lambert, “Improving incentive: Changing the interface of tax and social security”, *Australian Economic Review*, 281-289.

3.44 Our preference for the recent tax cut would have been to increase the tax-free threshold to $7,500. The Government's tax cuts kept the tax-free threshold at $6,000.

3.45 If, as a society, we decide that to have a bare minimum existence costs, for example $12,000, why do our tax rules operate to tax income earned over $6,000?

3.46 This approach has been supported by Dr Kayoko Tsumori[8]. He states that all participants in Australia's welfare debate, while disagreeing on many issues, agree on at least three key objectives.

3.47 First, any policy aiming to alleviate poverty 'should encourage employers to create jobs and jobless people to take them' because the major cause of poverty is joblessness'.

3.48 Second, those in fulltime work 'should take home enough money at the end of the week to keep their heads above water'.

3.49 Thirdly, it is important to create and maintain work incentives.

3.50 As stated above, a minimum wage increase may have an adverse impact on employment. The earnings credit may have an adverse effect on work incentives[9]. Dr Tsumori states that:

> There is a third option that meet all three criteria: to raise the personal tax-free threshold. The current tax-free threshold is set at $6,000 per annum. By raising it from such a low level, returns to paid work would be boosted. As a result, it would become less necessary to raise minimum wages or to supplement wages with the earnings credit. A higher tax-free threshold would neither affect job creation nor perpetuate poverty. Most of all, it would not discourage personal initiative.

3.51 While some academics have debated the various merits of earned tax credits and increasing thresholds, the Government has been impotent. Content to allow the high effective tax rates to apply to low-income earners moving off welfare, but remaining sympathetic to the interests of those on over $60 000 faced with a marginal tax rate of 48.5%. As ACOSS[10] has recently pointed out, their average tax rate, for someone earning $60 000 is only 26%.

3.52 By contrast a low wage earner on $20 000 has an average tax rate of 12%. So if you triple your income your average tax rate only doubles.

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8 'Is the Earnings Credit the best way to cut dole queues? Centre for Independent Studies, 13 May 2003.

9 Peter Saunders, 'Threshold Issues for a Tax System that creates job', *The Australian Financial Review*, 17-21 April

10 ACOSS Info 347 – June 2003 Page 4.

3.53 The tax and welfare system is unbalanced – too heavy on lower income Australians and lighter on higher income Australians, particularly when you take into account the effect of Tax Expenditures.

3.54 It seems that while the Government attempts to cut tax for high-income earners by reducing capital gains tax and the superannuation surcharge, and providing private health insurance rebates, they are ignoring one of the most important issues facing our society.

3.55 Minister Abbott has himself come out in support of providing assistance to the low paid by addressing poverty traps through the taxation system as an alternative to wage increases.

3.56 Rather than initiate an inquiry to explore the prospects he is instead pursuing an industrial relations avenue that is flawed.

3.57 The Democrats do not believe the Bill is adequate to address the legitimate concerns of all stakeholders and call on the Government to instead focus their energies on reforming the tax and welfare system.

Senator Andrew Murray