

In Confidence

Office of the Minister for Workplace Relations and Safety

Chair, Cabinet Economic Growth and Infrastructure Committee

## **Annual Minimum Wage Review 2016**

### **Proposal**

1. This paper proposes:
  - 1.1 To incrementally adjust the adult minimum wage from \$15.25 to \$15.75 per hour from 1 April 2017; and
  - 1.2 That the starting-out minimum wage and training minimum wage rates remain at 80 per cent of the adult minimum wage, which will adjust these rates from \$12.20 to \$12.60 per hour.

### **Executive Summary**

2. The government's objective for the minimum wage review is to 'keep increasing the minimum wage over time to protect the real incomes of low paid workers while minimising job losses' (CAB (12) 41/5B refers).
3. The current minimum wage rates are \$15.25 per hour for adults and \$12.20 per hour for starting-out workers and trainees. Minimum wages are being paid to around 73,300 employees, making up approximately 2.9 per cent of all employees. Minimum wage workers are disproportionately young people and those working part-time. Women, Māori and Pacific workers, people without formal qualifications, disabled workers, refugees and migrants are also more likely to be paid the minimum wage than other groups of workers.
4. This year's review took place in a strong economic climate, with consistent economic growth and strong labour market performance. The unemployment rate, at 4.9 per cent (September 2016 quarter), is the lowest it has been since the global financial crisis. Economic growth is expected to decrease slightly over the next two years, although remain relatively stable.
5. I have considered advice on minimum wage options for 2017 from the Ministry of Business, Innovation and Employment (MBIE). These options were assessed against the objective for the minimum wage review. Key impacts of the minimum wage options are summarised in Table 1.
6. I propose increasing the adult minimum wage to \$15.75 per hour (option 3 in the review). It is also my intention that the starting-out wage and the training minimum wage remain at 80 per cent of the adult minimum wage, which will increase these rates to \$12.60 per hour.
7. This option reflects a consistent approach that continues the increase in the real value of the minimum wage and increases its relativity to the median wage to 67

per cent (up from 66.8 per cent after the minimum wage increase on 1 April 2016).

8. This year the median wage increased 2.9 per cent to \$23.49 per hour (Labour Market Statistics (Income) June 2016). An increase in the minimum wage of 50 cents could increase annual economy-wide wages by \$65 million. MBIE modelling estimates that the constraint on employment growth is 1,500 jobs.

*Table 1: Summary of the impacts of the minimum wage options*

Minimum wage rate impact measures	Option 1	Option 2	Option 3	Option 4	Option 5	Option 6
Adult minimum wage (hourly rate)	\$15.25	\$15.50	\$15.75	\$16.00	\$16.50	\$19.80
Adult minimum wage (gross weekly income) <sup>1</sup>	\$610	\$620	\$630	\$640	\$660	\$792
Percentage increase	N/C	1.6%	3.3%	4.9%	8.2%	29.8%
Relativity to median wage <sup>2</sup>	64.9%	66.0%	67.0%	68.1%	70.2%	84.3%
Number of people impacted (rounded up to nearest 100)	73,300	89,900	119,500	142,700	212,000	528,700
Estimated restraint on employment	N/C	N/C	-1,500	-3,500	-7,000	-28,000
Estimated economy-wide increase in wages (\$m, annual)	N/C	26	65	113	257	2,331
Estimated inflationary impact/GDP (percentage points)	N/C	N/C	N/C	N/C	0.1%	0.7%
Additional annual costs to the government (\$m) <sup>3</sup>	N/C	\$15.33	\$29.38	\$40.44	\$87.10	\$543.55 <sup>4</sup>

<sup>1</sup> This is calculated on a 40 hour week basis.

<sup>2</sup> The median hourly earnings are \$23.49 per hour (Labour Market Statistics (Income), June 2016).

<sup>3</sup> This is a high level estimate based on the additional costs to the Ministries of Health, Social Development and Education and the Accident Compensation Corporation from higher wage costs for their employees and service providers.

<sup>4</sup> This figure in particular is likely to be underestimated because employees and contractors working for state agencies other than the four surveyed here would be affected by a minimum wage rate increase to \$19.80. This figure should also be considered alongside the increase to ACC's Outstanding Claims Liability which could result in higher ACC levies.

## Background

9. I have a statutory obligation to review the minimum wage rates by 31 December each year under section 5 of the Minimum Wage Act 1983.
10. Cabinet agreed in 2012 to adopt a cyclical process for the review of the minimum wage rate. The process comprises a comprehensive review (as was undertaken in 2011) to be completed every fourth year, with a streamlined process in the intervening three years focusing on fewer key factors and with limited formal consultation. The first comprehensive review under this process was undertaken in 2015.
11. As specified in the streamlined process, MBIE has focused on the following factors in assessing the options for the minimum wage rates for 2017:
  - 11.1 Inflation, using the Consumer Price Index (CPI) as the indicator
  - 11.2 Wage growth, using median wage as the indicator
  - 11.3 Restraint on employment; and
  - 11.4 Other relevant factors, such as the impact on sectors, including the state sector
12. The minimum wage rates normally increase every year after the completion of the annual review. The following table shows the recent changes to the minimum wage rate, compared with the annual increase in the average wage.

Year	Adult Minimum Wage	Starting-out/Training Minimum Wage <sup>5</sup>	% change	Annual increase in average wage <sup>6</sup>	% of the average wage <sup>7</sup>
April 2006	\$10.25	\$8.20	7.9%	5.4%	47.5%
April 2007	\$11.25	\$9.00	9.8%	4.7%	49.8%
April 2008	\$12.00	\$9.60	6.7%	4.7%	50.8%
April 2009	\$12.50	\$10.00	4.2%	5.4%	50.2%
April 2010	\$12.75	\$10.20	2.0%	1.0%	50.5%
April 2011	\$13.00	\$10.40	2.0%	2.6%	50.1%
April 2012	\$13.50	\$10.80	3.8%	3.8%	50.1%
April 2013	\$13.75	\$11.00	1.9%	2.1%	50.0%
April 2014	\$14.25	\$11.40	3.6%	3.5%	50.6%
April 2015	\$14.75	\$11.80	3.5%	2.1%	51.3%
April 2016	\$15.25	\$12.20	3.4%	2.4%	51.7%

<sup>5</sup> This rate was previously known as the Youth Minimum Wage.

<sup>6</sup> Source: Ordinary time hourly wages, Labour Market Statistics, March quarters, Statistics NZ.

<sup>7</sup> Source: Ordinary time hourly wages, Labour Market Statistics, March quarters, Statistics NZ.

## **Comment**

13. In general, minimum wage increases may have the following impacts:
  - 13.1 *Increased earnings for minimum wage workers* (although net household income is also affected by other government interventions, such as taxation and abatement for those receiving income support and tax credits) and, potentially, flow-on impacts for other workers earnings close to the minimum wage.
  - 13.2 *Increased labour costs for employers*, especially for those industries that employ a large number of minimum wage workers such as retail and hospitality. This could result in greater inflationary pressure. An increase in the minimum wage will also have a fiscal impact on the state sector, mainly the Ministries of Education, Health and Social Development and the Accident Compensation Corporation (ACC).
  - 13.3 *Negative employment effects*, including lower job growth and reduced hours, particularly from a significant rise in the level of the minimum wage. The extent of these effects will depend on the size of the wage increase and the economic and labour market context in which it occurs, and are most likely to impact on some demographic groups, such as youth and Māori and Pacific workers.
14. Setting the minimum wage requires balancing the benefits of any changes, such as the protection of the lowest paid, against the costs that any changes might bring, such as negative employment impacts.
15. MBIE advises that a moderate increase is appropriate in the current economic and labour market conditions. A moderate increase means an incremental adjustment that maintains or increases the real value of the minimum wage while minimising constraint on job growth.
16. An incremental adjustment to the minimum wage rate is not expected to have a significant impact on either the demand or supply of minimum wage workers or, more broadly, employment or unemployment. Further, it is unlikely that a modest increase in the minimum wage will have a significant effect on wage growth.
17. Given the uncertainty around many the potential impacts of a minimum wage increase, I consider that a relatively constrained approach continues to be warranted. Amongst all the options I considered, option 3 (\$15.75 per hour) is the preferred option because:
  - 17.1 This is an incremental increase that takes account of current economic and labour market circumstances.
  - 17.2 A moderate increase will have a positive financial and social impact for low-paid workers through an increase in their income. Option 3 impacts up to 119,500 workers directly with a minimal impact on employment growth.
  - 17.3 Options 1 and 2 (\$15.25 per hour and \$15.50 per hour) have no negative impacts on the economy or employment growth, but do not have as significant or widespread positive impacts on low-paid workers.

- 17.4 Option 5 has smaller employment growth impacts than option 6. However, employment impacts from increases in the minimum wage will fall predominately on the low paid and vulnerable sectors of the economy.
- 17.5 Under options 5 and 6 (\$16.50 per hour and \$19.80 per hour), the costs are very likely to outweigh the benefits as employment growth could be significantly restrained. This is inconsistent with the objective of the minimum wage review, which is to protect the real incomes of low-paid workers while minimising job losses.
- 17.6 Although, the decision between options 2 (\$15.50) and 3 (\$15.75) was close, I consider that option 3 is the most consistent with the objective for the minimum wage review and the criteria each option is assessed against. The attached Regulatory Impact Statement and Minimum Wage Review Report 2016 provide greater detail of why option 3 is preferred.
- 17.7 Option 2 (\$15.50) is an increase of 1.64 per cent and would directly affect 89,900 workers. It would increase economy wide wages by \$26 million and increase the fiscal cost to government by \$15.33 million. This option would reduce the relativity to the median wage to 66 per cent. This figure is above inflation (0.4 per cent) however, the Treasury forecast inflation to increase to 1.5 per cent in 2017 which may reduce the value of option 2.

## **Consultation**

18. In accordance with the Cabinet minute (CAB Min (12) 41/5B), consultation has been undertaken with Business New Zealand (BusinessNZ) and the New Zealand Council of Trade Unions (NZCTU). Their views and submissions are analysed in the review process:
  - 18.1 BusinessNZ submitted that a review of the role and effect of the minimum wage should be undertaken in light of the significant movements of the minimum wage over the past 10 years. This review should take particular account of the recent case law which highlights the different environment the minimum wage operates in compared to that of 1945 when initially introduced.
  - 18.2 NZCTU submitted that there should be an immediate increase in the minimum wage rate to \$19.88 per hour which is 66 per cent of average ordinary time earnings or, if that is unachievable, an increase in the minimum wage rate to 66 per cent of the average ordinary time hourly earnings over three years with an interim step to \$16.95 per hour on 1 April 2017.
19. The Treasury, Ministry of Health, Ministry of Social Development, Ministry of Education, Ministry of Pacific Peoples, Ministry for Women, the Accident Compensation Corporation, Te Puni Kōkiri, State Services Commission and the Inland Revenue Department have been consulted in this review. The Department of Prime Minister and Cabinet has been informed of the review.
20. The Treasury, the Ministry of Health, the Ministries for Women, and Pacific Peoples, and the Accident Compensation Corporation advise that they are comfortable with increasing the minimum wage rate to \$15.75 per hour.

21. Te Puni Kōkiri recommends an increase in the adult minimum wage to \$16.50 per hour. Te Puni Kōkiri also provided the following comment:
- 21.1 Te Puni Kōkiri does not support the recommendation for an increase to \$15.75 (Option 3). CPI has increased 47.2 per cent since 2007. Given the significant increase on housing related costs to household expenditure (47.2 per cent increase since 2007), and the wider government work programme to increase housing security, affordability and independence, we recommend setting the minimum wage rate at \$16.50 (Option 5). This would reflect a moderate level (47 per cent) increase to minimum wage rates since 2007.
- 21.2 In addition, Te Puni Kōkiri and MBIE have a number of shared goals with regard to economic development, and we would like to find better ways in the future to provide constructive input and support in the difficult task of modelling and estimating the impact of minimum wage increases.

22 A summary of agency comments is provided in the Regulatory Impact Statement.

### **Fiscal Implications**

- 23 There are state sector employees and contractors who earn at or close to the adult minimum wage, particularly in the public health and compulsory education sectors. Increases in the minimum wage rate are therefore likely to have direct (and also indirect or ‘flow-on’) costs for some state sector employers. The Ministries of Education, Health and Social Development and the Accident Compensation Corporation have been identified as agencies which would be more impacted by changes in the minimum wage. For these four agencies, total annual costs directly related to the proposed minimum wage increase are estimated to be \$29.38 million per annum.
- 24 If the Government reaches a settlement in pay negotiations for workers in aged and disability residential care, and aged and disability home and community support services, the associated wage increase will reduce the impact attributable to changes in the minimum wage with respect to the Ministry of Health. Any impact of these negotiations has not been factored into the cost estimates.
- 25 As well as increasing wage costs, increasing the minimum wage might have other fiscal impacts. Social assistance costs through benefit payments may rise if an increase in the minimum wage increases unemployment. Meanwhile, higher incomes can increase the amount of personal income tax received and lead to the abatement of social assistance, such as Working for Families tax credits. However, these impacts cannot be accurately assessed with the information currently available.

### **Human Rights**

- 26 I recommend that the starting-out minimum wage and the training minimum wage continue to be set at 80 percent of the adult minimum wage. As these minimum wage rates continue to make a distinction on the basis of age, namely those aged 16 to 19 years, or their employment status, it continues to raise an issue of discrimination under section 19(1) of the New Zealand Bill of Rights Act 1990.
- 27 However, this discrimination appears to be justified in terms of section 5 of the New Zealand Bill of Rights Act for the following reasons:

- 27.1 There are negative long-term economic and social effects associated with young people being out of work, especially if they remain unemployed for a significant period of time. The starting-out minimum wage and training minimum wage were designed to help get young people into work and work-based training. They encourage employers to take a chance on a young person, and provide opportunities for 16 to 19 year olds to engage in training in their chosen occupation. This enables young people to earn money, gain skills, and get work experience. It helps mitigate the effects of long-term unemployment by assisting young people into work before they move into a cycle of benefit dependency.
- 27.2 While there has been a stronger labour market performance over the past year, the unemployment rate for the 15 to 19 year old age group is still higher than for other groups (19.7 per cent, September quarter 2016). Labour market conditions and the unemployment rate have not changed significantly enough over the past year to warrant increasing the relativity of the starting-out wage and training minimum wage from the status quo of 80 per cent of the adult minimum wage.

### **Legislative implications**

- 28 Minimum wages are set through an Order in Council made under section 4 of the Minimum Wage Act 1983. To give effect to a change of the minimum wage rate, a new Order in Council needs to be made by the Governor-General, on the recommendation of the Minister for Workplace Relations and Safety. It is proposed that the new order will come into force on 1 April 2017 to provide certainty and consistency to both employees and employers.

### **Regulatory Impact Analysis**

- 29 The Regulatory Impact Analysis requirements apply to the proposal in this paper and a Regulatory Impact Statement (RIS) has been prepared and is attached.
- 30 The Director, Regulatory Systems and the Regulatory Impact Analysis Review Panel, have reviewed the attached RIS prepared by the Ministry of Business, Innovation and Employment. They consider that the information and analysis summarised in the RIS meets the criteria necessary for Ministers to fairly compare the available policy options and take informed decisions on the proposals of this paper.
- 31 I have carefully considered the analysis and advice of officials as summarised in the attached RIS. I am satisfied that, aside from the risks and uncertainties already noted in this Cabinet paper, the recommended option (\$15.75 per hour) provides a fair balance between the protection of the lowest paid workers and employment impacts. The recommendation is the result of my statutory review of the minimum wage rates and is consistent with expectations of the Government Statement on Regulation.

### **Gender Implications**

- 32 Women tend to be overrepresented in a number of demographic characteristics associated with low pay, including working part-time and working in the hospitality and retail sectors (in service and sale occupations). It is estimated that, of those

currently earning the minimum wage, 59.7 per cent are women, so an increase is likely to have a slight positive impact on women.<sup>8</sup> However, Statistics New Zealand calculate that the overall average hourly wage for women is approximately 12 per cent less than the average hourly wage for men (aged 18 to 64 years) and this would not change significantly under my recommended option.<sup>9</sup>

## Publicity

- 33 I intend to make a media statement about the decision on the minimum wage rates for 2017 following Cabinet confirmation. The RIS and Minimum Wage Review Report 2016 will be made publically available through MBIE's website (the RIS will also be available on Treasury's website), subject to any appropriate withholding of information that would be justified under the Official Information Act 1982.

## Recommendations

The Minister for Workplace Relations and Safety recommends that the Cabinet Economic Growth and Infrastructure Committee:

1. **note** that the objective for the minimum wage agreed by Cabinet in 2012 is to 'keep increasing the minimum wage over time to protect the real incomes of low paid workers while minimising job losses' (CAB (12) 41/5B refers)
2. **agree** that the adult minimum wage rate be adjusted from \$15.25 per hour to \$15.75 per hour from 1 April 2017
3. **agree** to maintain the starting-out minimum wage and the training minimum wage at 80 per cent of the adult minimum wage rate, which will mean these each increase to \$12.60 per hour
4. **note** this change to the minimum wage rate will be announced before the end of 2016
5. **agree** to the Minister for Workplace Relations and Safety issuing drafting instructions to the Parliamentary Counsel Office to give effect to these recommendations through an Order in Council.

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<sup>8</sup> Source: Labour Market Statistics (Income) June 2016, Statistics New Zealand.

<sup>9</sup> This calculation excludes all workers that reported an hourly wage below the adult minimum wage.