

In Confidence

Office of the Minister for Workplace Relations and Safety

Chair, Cabinet Business Committee

## Increasing the Minimum Wage to \$16.50

### Proposal

- 1 This paper seeks Cabinet agreement:
  - 1.1 To increase the adult minimum wage from \$15.75 to \$16.50 per hour from 1 April 2018; and
  - 1.2 To increase the starting-out wage and training minimum wage rates from \$12.60 to \$13.20 per hour from 1 April 2018 (so that each remain at 80 per cent of the adult minimum wage).

### Executive Summary

- 2 The minimum wage is currently \$15.75 per hour for adults and \$12.60 per hour for starting-out workers and trainees. Adult minimum wages are being paid to approximately 76,400 workers.
- 3 The Government's coalition agreement has a policy to increase the minimum wage to \$16.50 per hour from 1 April 2018. Cabinet noted this on 31 October (CAB-17-MIN-0486 refers).
- 4 This paper provides an assessment of the likely impacts of implementing this policy, and contextualises this in relation to a range of possible minimum wages, as presented in Annex 1.
- 5 This paper proposes that the starting-out wage and the training minimum wage remain at 80 per cent of the adult minimum wage, and will therefore increase these rates to \$13.20 per hour. This paper also notes that officials will prepare advice for abolishing the starting-out wage, in light of the Government's commitment to 'abolish youth rates' **within its first 100 days**, including consideration of any subsequent changes to the training minimum wage.
- 6 Analysis from the Ministry of Business, Innovation and Employment suggests that there are both positive and negative impacts for increasing the minimum wage to \$16.50. I consider that it is appropriate to raise the minimum wage to \$16.50 for a number of reasons:
  - 6.1 This approach meets the Government's commitment to increase the minimum wage to \$16.50, and also reflects a consistent approach to increasing the minimum wage. This consistency gives employers and employees certainty, and minimises potential negative effects of the minimum wage
  - 6.2 MBIE's model estimates there will be no discernible inflationary impact
  - 6.3 A minimum wage of \$16.50 will have a relatively small estimated restraint on employment of 3,000 jobs

Note this is an error. This is not a 100-days commitment

- 6.4 Fiscal impacts to government are estimated to be less than \$20 million annually and are expected to be absorbed within baselines.

## Background

- 7 Following coalition negotiations, Cabinet noted its intention to implement an increase to the minimum wage of 75c (to \$16.50 per hour) as of 1 April 2018 (CAB-17-MIN-0486 refers).
- 8 The following table shows the recent changes to the minimum wage rate, compared with the median wage.

Table 1: Previous and proposed minimum wage increases

Date of new minimum wage	Adult minimum wage		Median wage		Minimum wage % of median wage (June each year)
		% change		%change	
April 2007	\$11.25	9.8%	\$18.00	5.9%	63%
April 2008	\$12.00	6.7%	\$18.56	3.1%	65%
April 2009	\$12.50	4.2%	\$19.51	5.1%	64%
April 2010	\$12.75	2.0%	\$19.95	2.3%	64%
April 2011	\$13.00	2.0%	\$20.02	0.4%	65%
April 2012	\$13.50	3.8%	\$20.78	3.8%	65%
April 2013	\$13.75	1.9%	\$21.48	3.4%	64%
April 2014	\$14.25	3.6%	\$21.92	2.0%	65%
April 2015	\$14.75	3.5%	\$22.68	3.5%	65%
April 2016	\$15.25	3.4%	\$23.22	2.4%	66%
April 2017	\$15.75	3.3%	\$24.00	3.4%	66%
<b>April 2018</b>	<b>\$16.50</b>	<b>4.8%</b>			

## Comment

- 9 In general, minimum wage increases can have the following impacts:
- 9.1 *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.
- 9.2 *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, assessed here by estimates from the Ministries of Education, Health, Social Development and Vulnerable Children Oranga Tamariki, and the Accident Compensation Corporation.
- 9.3 *Increased price of goods and services for consumers*, if employers pass on all or part of their increased labour costs. This can contribute to inflationary pressure.
- 9.4 *Positive economic growth*, through increased spending by minimum wage earners. This effect is harder to quantify, as a counterfactual is not evident. However, some evidence suggests that minimum wage earners are likely to be in low-income

households, and spend a high proportion of their income on goods and services. Higher minimum wages, therefore, increase the purchase and consumption of goods and services in the economy relative to what higher-income households spend their money on (such as savings or investments).

9.5 *Restraint on employment*, including lower job growth and reduced hours, particularly from a significant rise in the level of the minimum wage. This effect can be through substitution of low-wage labour for either capital or for higher-wage, higher-productivity labour. 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. MBIE's minimum wage model estimates the extent of this effect.

9.6 *Increased fiscal costs for government*, through both direct wage costs (employees paid at or near the minimum wage), and indirect costs due to government expenditure on programmes that are affected by the minimum wage. Further discussion of the direct costs to government are below.

10 MBIE has assessed a number of minimum wages to provide context for the impact of increasing the minimum wage to \$16.50. A summary of this assessment is in Annex 1.

11 MBIE's analysis shows that:

11.1 the increase of 75c is broadly consistent with the previous four increases (of 50c) and most businesses and workers expect incremental changes to the minimum wage each year

11.2 there is no discernible inflationary impact of increasing the minimum wage to \$16.50

11.3 an estimated 164,100 people are currently earning wages between the minimum wage and the proposed minimum wage of \$16.50, and many of these would therefore receive an increased wage

11.4 the estimated restraint on employment for the proposed minimum wage is 3,000

11.5 fiscal impacts to government are estimated to be less than \$20m annually.

12 I have considered MBIE's analysis and I remain of the view that an increase of the minimum wage to \$16.50 is appropriate in the current labour market and economic context.

#### *Starting-out wage and training minimum wage*

13 I recommend that the starting-out wage and the training minimum wage remain at 80 per cent of the adult minimum wage, and therefore increase to \$13.20 on 1 April 2018.

14 However, in light of the Government's commitment to 'abolish youth rates,' I have directed officials at MBIE to provide advice on amending the *Minimum Wage Act* to abolish the starting-out wage, including consideration of any subsequent changes to the training minimum wage. Making these amendments in 2018 will provide the chance for adequate consultation to mitigate any possible unintended consequences.

15 I have considered the option of removing the starting-out wage at the same time as increasing the adult minimum wage. However, this would create inconsistencies with the training minimum wage and there is insufficient time to consult with employers and

employees that would be effected. For this reason, amending the *Minimum Wage Act* is the preferable option.

#### *Future increases to the minimum wage*

- 16 The Government has also committed to minimum wage increases, beyond this initial one, to take the rate to \$20 by 2021. It will be helpful, particularly to employers, to signal how these increases will occur. Two key factors that will help employers, particularly those that will likely be affected significantly by these increases are that:
- 16.1 Increases are planned to be spread as evenly as possible over the period (rather than most of the increase happening in a single year)
- 16.2 A review will be conducted each year - if economic conditions are favourable for a larger increase than planned in a particular year, then the increase that year could be larger, however if economic conditions are particularly tight then that year's increase could be smaller.

#### **Consultation**

- 17 Consultation was undertaken with Business New Zealand and the New Zealand Council of Trade Unions, as has been the case for previous reviews of the minimum wage. Neither organisation provided comment on the Government's proposed approach to the minimum wage.
- 18 The Treasury, Ministry of Health, Ministry of Social Development, Ministry for Vulnerable Children, Oranga Tamariki, the Accident Compensation Corporation, Inland Revenue, Department of Prime Minister and Cabinet (Policy Advisory Group), Ministry for Pacific Peoples, Te Puni Kōkiri, State Services Commission, and the Reserve Bank have been consulted in this review. Specific comments from these agencies include:
- 18.1 The Treasury has commented that it is their expectation that agencies manage any increases within existing baselines in the first instance.
- 18.2 The Reserve Bank of New Zealand agreed that this increase is likely to have only a small impact on CPI inflation, but also consider that there is some risk of a larger-than-usual effect on price and wage expectations (potentially generating a ripple effect to other wages above the minimum wage). If this was to occur, this may have implications for interest rates in order to maintain CPI inflation targets.

#### **Financial Implications**

- 19 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, Social Development, and Vulnerable Children, Oranga Tamariki and the Accident Compensation Corporation have provided an estimate of how their costs would be affected by an increase to the minimum wage. For these agencies, total annual costs directly related to the proposed minimum wage increase to \$16.50 per hour are estimated to be \$19.58m per year.
- 20 The estimated cost is lower than the costs for similar increases in previous years. For example, a 75c increase in the 2016 review was estimated to cost \$40.44m per year. One reason for this reduction is the pay equity settlement for aged care support workers earlier in

2017. Due to the increased pay for these workers, the estimated cost of a 75c increase for the health sector fell from \$29.7m in 2016 to \$12.5m in 2017.

- 21 In addition to annual cash costs ACC have estimated a \$40 million impact to ACC's outstanding claims liability (OCL). The OCL is an actuarial estimate of the funds required now to meet the future cost of all existing ACC claims. Increases in the OCL will have an impact on Scheme solvency. Solvency is the measure of ACC's assets to ACC's liabilities by Account. This impact will be recovered over a ten year period through the levy setting process, and appropriations. The Work, Earners', Motor Vehicle Accounts and part of the Treatment Injury accounts are funded by levies. Appropriations cover the Non-Earners Account and the non-earners portion of the Treatment Injury Account.
- 22 As well as affecting wage costs, increasing the minimum wage might have other indirect fiscal impacts. Social assistance costs through benefit payments may rise if an increase in the minimum wage results in a higher level of unemployment. At the same time, higher incomes can increase the amount of personal income tax received and reduce the amount of social assistance due to income abatement. This could offset the fiscal costs for government. However, these impacts cannot be accurately assessed with the information currently available.
- 23 Further, some other government programmes are adjusted based on labour market wage statistics (for example parental leave payment rates are adjusted annually based on changes in average ordinary time hourly earnings). Changes to the minimum wage – particularly larger ones in coming years – may have an impact on these programmes.

## Human Rights

- 24 I recommend that the starting-out minimum wage and the training minimum wage continue to be set at 80 per cent of the adult minimum wage, noting the Government's commitment to abolish the starting-out wage within its first 12 months. As these minimum wage rates 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*.
- 25 However, this discrimination appears to be justified in terms of section 5 of the *New Zealand Bill of Rights Act*.
- 26 There can be 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. Providing the ability to pay young, unskilled, and in-training workers a lower wage than the adult minimum wage is one way to get young people into work and work-based training. This encourages 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. Young people can earn money, gain skills, and get work experience. It mitigates some effects of long-term unemployment by assisting young people into work before they move into a cycle of benefit dependency.

## Legislative Implications

- 27 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. The new order will come into force on 1 April 2018.

- 28 I will bring a paper to the Cabinet Legislation Committee in early 2018 to give effect to the minimum wage increase.

### **Regulatory Impact Analysis**

- 29 A Regulatory Impact Statement (RIS) is required for the proposed changes, and is attached, including an assessment by MBIE's Regulatory Impact Analysis Panel. Treasury advises that in line with the 100 Day Plan implementation arrangements, the regulatory impact analysis focuses only on some of the elements that are normally expected. Treasury would therefore recommend the publication of this Cabinet paper along with the RIS for the information of Parliament and the public.
- 30 The attached RIS prepared by MBIE provides an assessment of the proposed minimum wage of \$16.50, and contextualises this assessment using other minimum wages. MBIE's assessment provides evidence to support the Government's view that increasing the minimum wage to \$16.50 is appropriate in the current labour market and economic context.
- 31 MBIE's Regulatory Impact Analysis Panel has reviewed the RIS and based on the revised expectations for Impact Analyses covering 100 Day Plan priorities has made the following comments:

Given the constraints that have been highlighted in the Impact Statement, the Impact Statement appropriately reflects the analysis and consultation that has been able to be completed. The potential impacts of the proposed approach have been broadly identified, and the analysis is methodical and thorough. Gaps in evidence, risks and downsides are acknowledged. Where stakeholders have provided views these have been summarised. It will be important to ensure monitoring and evaluation processes for the increase in the minimum wage are undertaken in a timely way to inform discussion about the potential effects of future increases.

### **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 by MBIE that 60.6 per cent of minimum wage earners aged 16-64 are women, compared to 49.2 per cent of all wage earners (MBIE minimum wage model, Labour Market Statistics) so an increase is likely to have a positive impact for women.
- 33 However, Statistics New Zealand calculate (as of 1 September 2017) an overall median hourly earnings pay gap of 9.4 per cent between men and women, and it is unlikely that increasing the minimum wage would have any discernible effect on this.

### **Publicity**

- 34 I intend to make a media statement about the decision on the minimum wage rates for 2017 following Cabinet confirmation. The RIS will be made publicly available through MBIE's website and Treasury's website, subject to any appropriate withholding of information that would be justified under the Official Information Act 1982.
- 35 I also intend to communicate the Government's intention for future increases to the minimum wage, following the approach set out in paragraph 16.

## Recommendations

The Minister for Workplace Relations and Safety recommends that the Cabinet Business Committee:

- 1 **note** the Government's coalition agreement policies of increasing the minimum wage to \$16.50 per hour on 1 April 2018, and to be \$20 per hour by 2021
- 2 **agree** that the adult minimum wage be increased from \$15.75 per hour to \$16.50 per hour from 1 April 2018
- 3 **agree** to maintain the starting-out wage and training minimum wage at 80 per cent of the adult minimum wage, which will mean that these each increase to \$13.20 per hour from 1 April 2018
- 4 **note** the Minister for Workplace Relations and Safety will instruct officials at the Ministry of Business, Innovation and Employment to prepare advice on amending the *Minimum Wage Act 1983* to abolish the starting-out wage and make changes to the training minimum wage
- 5 **invite** the Minister for Workplace Relations and Safety to issue drafting instructions to the Parliamentary Counsel Office to give effect to these recommendations through an Order in Council
- 6 **note** this change to the minimum wage rates will be announced before the end of 2017 following Cabinet confirmation
- 7 **note** that publicity will also reflect that the Government's proposed approach for future increases to the minimum wage is to spread increases evenly where possible but still conduct a review each year so that the increases can be responsive to current economic conditions
- 8 **agree** to publication of this Cabinet paper along with the RIS for the information of Parliament and the public

Authorised for lodgement

**Hon Iain Lees-Galloway**

Minister for Workplace Relations and Safety

Annex 1: Summary of impacts for minimum wage options

Impact measures	Increase	Status quo	25c	50c	75c	\$1.20	\$2.25	\$3.25	\$4.10	\$4.45
		\$15.75	\$16.00	\$16.25	<b>\$16.50</b>	\$16.95	\$18.00	\$19.00	\$19.85	\$20.20
Gross weekly income (based on a 40 hour week)		\$630.00	\$640.00	\$650.00	<b>\$660.00</b>	\$678.00	\$720.00	\$760.00	\$794.00	\$808.00
Relativity to median wage (\$24.00 per hour, June 2017)		65.6%	66.7%	67.7%	<b>68.8%</b>	70.6%	75.0%	79.2%	82.7%	84.2%
Relativity to average wage (\$30.36 per hour, June 2017)		51.9%	52.7%	53.5%	<b>54.3%</b>	55.8%	59.3%	62.6%	65.4%	66.5%
Number of people impacted		76,400	92,300	142,400	<b>164,100</b>	210,800	319,600	421,000	502,600	568,200
Estimated restraint on employment		N/C	N/C	-1,000	<b>-3,000</b>	-6,500	-14,000	-21,500	-28,000	-30,500
Estimated annual economy-wide increase in wages		N/C	\$27m	\$74m	<b>\$129m</b>	\$255m	\$708m	\$1,338m	\$2,014m	\$2,333m
Estimated inflationary impact		N/C	N/C	N/C	<b>N/C</b>	0.1%	0.2%	0.4%	0.6%	0.7%
Additional annual costs to government (based on estimated costs for MoH, MSD, MVCOT, ACC, MinEd)		N/C	\$6,326,046	\$12,823,552	<b>\$19,584,248</b>	\$34,679,015	\$73,834,484	\$124,593,606	\$198,240,216	\$239,804,439

Source: Labour Market Statistics (Income) June 2017; MBIE minimum wage model