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Submission on the National Minimum Wage

Presented to the:

Low Pay Commission

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Introduction

The Small Firms Association (SFA) is the trusted partner of small businesses in Ireland, with 8,500 members and six affiliated organisations in all sectors and parts of the country. Its mission is to deliver business-focused advice and insights to member companies, influence government policy to the benefit of small businesses and connect its members in a thriving community.

The SFA has a vision of Ireland as the most vibrant small business community in the world – supporting entrepreneurship, valuing small business and rewarding risk takers. In this context, the SFA welcomes the opportunity to make a submission to the Low Pay Commission on the National Minimum Wage rate, with particular comments on women on the minimum wage, based on our knowledge and experience of the small business community, which comprises over 182,000 businesses and employs half of the private sector workforce.

Overview

Ireland is a nation of small businesses, with over 97% of enterprises employing less than 50 employees and 84% employing less than 10. They have a vital role to play in terms of employment generation, especially in regional towns and villages and rural Ireland. Therefore, decisions on the National Minimum Wage (NMW) rate must be made in the context of the ability of those companies to pay and with an appreciation of the impact on small business establishment, growth and the ability to create jobs.

The SFA is advocating that the Low Pay Commission recommend to Government in its 2016 report that the NMW should remain at its current level. This would provide an opportunity to fully asses the impact of the 1 January 2016 increase on employment levels, inflation, competitiveness and business survival. It would also allow time for Ireland to navigate the current global economic uncertainty – a context that requires extreme caution in domestic economic decisions. A year of wage floor stability would also afford time for the recovery to reach the sectors and regions that are currently lagging. Above all, these companies need to control costs and have a degree of certainty to allow them to rebuild their businesses.

One SFA member put it clearly when she said that "the minimum wage is maxed out at €9.15". This is certainly true in the current domestic and international economic context. As demonstrated below, there is no justification for a further rise in the NMW and all of the evidence points to a need for caution, stability and certainty. Any other course of action will lead to the prevention of job growth and to job losses in small businesses.

Evidence-based policy

The SFA welcomes the concept of an independent evidence-based assessment of the National Minimum Wage. However, the operation and methodology of the Low Pay Commission to date, with particular reference to its 2015 report, falls short of this ideal.

There was insufficient indication in the Low Pay Commission's 2015 report that its recommendations were evidence-based. The existing shortage of detailed data specific to Ireland poses challenges to all parties with an interest in the National Minimum Wage. In this context, it was disappointing that the Commission produced no new evidence/data of its own for the report. At a meeting with the Commission in November 2015, the SFA indicated its willingness to assist the Commission in gathering relevant data via a member survey. The 'Prompt questions' document received by the SFA and others on 1 March 2016 provides a useful template for such a survey, but this was received too late to conduct the survey and include the results in this submission.

From the SFA members that have already come forward to share their views on the NMW, some have said that they don't employ anybody on the minimum wage and others have indicated that they do. In many cases, those on the minimum wage are students or those working on a part-time, temporary or seasonal basis. Many are not the primary earner in their household. Some indicated that inexperienced workers are hired on the minimum wage and moved to a higher rate after six months or so, once they have acquired additional skills.

These findings, however, are not comprehensive. If the Commission are interested in doing an extensive survey and utilising the results in its deliberation between now and its decision in July, we are happy to administer it on your behalf at any point.

The SFA reiterates its position that the recommendations of the Low Pay Commission must be evidence-based. The SFA's 2015 submission clearly demonstrated that there was no evidence for an increase in the National Minimum Wage based on an assessment of inflation, movement in the earnings of employees, levels of employment and unemployment, national competitiveness and exchange rate movements (the review criteria outlined in the National Minimum Wage Act 2000). On this basis, the SFA called for the NMW to be frozen. The Trade Unions, on the other hand, called for a €1 increase in the NMW rate. The recommendation of the Commission was for a 50c increase, with no calculations provided to support why that was deemed to be appropriate. This experience gives SFA members little confidence in the Low Pay Commission as an independent body that bases its recommendations on the evidence available.

Impact of the increase of the NMW to €9.15 per hour

The Small Firms Association disagreed with the Low Pay Commission's recommendation for the NMW to increase to €9.15 per hour. Nonetheless, the Government accepted it and the 5.7% increase came into effect on 1 January 2016. It is too early to provide an empirical assessment of the impact of the changes (in terms of reduction of hours, prevention of recruitment, job losses and business closures) after only two months. However, it is clear from consultations with our members that a number of effects have already emerged.

- *Interaction with the tax system*

The Low Pay Commission's 2015 report states "A moderate increase in the current minimum wage rate without an appropriate adjustment in employer PRSI will have a major impact, particularly on small business costs." It also states "…it is clear that any recommended increase in the NMW must be accompanied by an appropriate adjustment to the PRSI system, to ensure that the entire burden of any adjustment should not fall solely, and unreasonably, on the employer".

Budget 2016 introduced certain PRSI changes, effectively ending the step effect from an employee perspective and shifting the step effect for employers. However, the changes to employer PRSI cannot be considered an 'appropriate adjustment' as called for by the Low Pay Commission. The changes offset less than 10% of the increased labour costs as a result of the NMW increase. The minimal level of the offset has resulted in even greater pressure on companies in labour intensive, low margin sectors, who have very limited scope to either absorb the cost increases or pass them on to customers. Therefore the poor alignment of the minimum wage and the tax system has increased the likelihood of the minimum wage increase costing jobs.

This demonstrates a problem in terms of the Low Pay Commission making recommendations that are contingent on one another and these recommendations being implemented in part by the Government of the day. The Low Pay Commission must be cautious about recommending any change in the NMW that would produce distortions in the tax system or elsewhere, as its remit to recommend accompanying policy changes to resolve these distortions is limited.

- *Knock-on pay claims*

A number of SFA members have reported increasing pressure for knock-on pay rises for those earning above the new NMW rate, in order to maintain their relative position. This occurs even in companies that do not employ anyone on the NMW. Repercussive claims are specifically ruled out by the National Minimum Wage Act 2000, but this does not alter the reality that employers are facing on the ground. A recent SFA survey found that 40% of small businesses cannot afford to give pay increases in 2016, and for those who intend to, this will average 2%. This leaves employers who cannot afford broad-sweeping pay rises at risk of damaging relations with their employees.

Economic context

Ireland faces political and economic uncertainty over the coming months. Internationally, exchange rates, oil prices and interest rates have all been in Ireland's favour in recent months, but these are aspects that are prone to reversal and over which we have little control. Equally, the global economic slowdown, the prospect of Brexit and the associated exchange rate risks are all external threats that could change Ireland's economic outlook in 2016. Policy should take the path of least harm as the economy navigates this volatile period.

In this context, it is vital that Ireland does not allow its underlying competitiveness to be eroded. All businesses compete internationally on costs, whether they export or not. Labour costs are a significant element of this in many sectors. Ireland currently has the second highest nominal NMW in the EU (after Luxembourg) and the sixth highest in terms of purchasing power. The additional burden of other employment legislation is significant and businesses are fearful as a result of pre-election criticism of flexible working conditions from some parties. If the cost of employment in Ireland is significantly higher than our export markets and competitor economies, it puts Irish companies at a distinct disadvantage when it comes to winning and maintaining market share.

Aggregate figures show the economy to be booming but this is primarily driven by strong exports. Only 6.4% of small companies are engaged in exporting – leaving the vast majority of businesses in Ireland dependent on the performance of the domestic economy. Domestically, the recovery has still been slow to reach some sectors and parts of the country, especially for small firms. Total domestic demand is still 7.1% below its peak in value terms, with consumer spending down 4%. Despite this, the wage floor has increased by 6% since the start of the year.

From an examination of the 2012 average gross (pre-tax) profits in small businesses in the sectors with the majority of NMW workers, it is clear that they would not be able to offset NMW increases against profits, as in micro firms (1-10) employees which are 84% of all businesses in Ireland, average pre-tax profits in accommodation and food businesses were €14,549; in retail were €21,470 and other services were €16,582. This means that they are not capable of absorbing labour cost increases without productivity gain and would have no choice but to offset NMW increases against reductions in hours or jobs, job growth or capital or skills investment.

Overall, inflation fell by 0.3% in 2015. The minimum wage is now €1.95 above where it would be if it had been indexed to inflation and the real value of the NMW is 27% higher than when it was introduced. Furthermore, we expect inflation to remain below 1% in 2016. As such, there is little evidence for an increase in the NMW based on the cost of living.

Taking all of these economic factors, it is clear that there is no evidence basis for a further increase in the NMW.

Labour market issues

The labour market in Ireland is shifting in some respects and there is much discussion of the 'war for talent'. It is important to recall, however, that this is a phenomenon that relates predominantly to highly skilled workers. The situation in the sectors that employ the bulk of minimum wage workers (retail, hospitality and support services) is much more sobering. Employment in these sectors was, at best, stagnant in 2015. Employment in retail has returned to 2005 levels, but there has been no significant year-on-year growth since 2007. Since 2005, growth in the wage floor has outstripped turnover growth by a factor of over 30 percentage points – in a sector where labour accounts for 70% of total costs.

In the economy as a whole, unemployment is still high, at 8.8%. While employment is growing at 5% annually in Dublin, the figure is only 2% for the rest of the country. The majority of those now on the Live Register are low skilled and in long-term unemployment. Increasing the NMW acts as a barrier to job creation and, in particular, to helping low skilled and young workers to enter the workforce, as it becomes unaffordable to train them up.

Small businesses have the capacity to continue to generate employment but any increase in the entry level of wages will prevent them from doing so.

Despite a severe productivity problem in domestic-facing sectors, the NMW is over 70% of median earnings in the accommodation and food sector and 57% of median earnings in retail (compared with 45% of median earnings in the overall economy). The closer the minimum wage is to the median wage, the greater the probability that the employer will have to offset additional increased wages with job losses or non-creation of new jobs, as the effect on their overall wage bill is greater.

In the current Irish context, where the trends in different parts of the labour market are so vastly different, the SFA believes that wages should be set in a competitive market. This is the most practical for businesses, taking account of their ability to pay, and will maximise job creation and retention. Increasing the NMW is a blunt tool that is ineffective at combatting poverty and inequality and that generates undesirable side effects such as locking the long-term unemployed out of work. The labour market itself should be used to arrive at a rate that is realistic for both the employer and the employee.

Women on the National Minimum Wage

The Low Pay Commission's 2015 report highlighted that 64.7% of those on NMW are women. We had little feedback on this issue from member companies. Again we believe that the Low Pay Commission should undertake an extensive survey to allow for a more evidence-based approach to assessing these issues.

Conclusion

Small business owner-managers are close to their businesses and their employees. They recognise the value of employee contribution and generally display much lower employee turnover when compared to large business. Small businesses will respond to market trends in wages but they cannot generate employment where unjustified business cost increases are imposed upon them by Government.

There is little evidence for an increase in the NMW economically, given an increasingly uncertain global environment, high unemployment, a deflationary cost of living and real concerns about the viability of minimum wage increases for firms in the regions.

On this basis, the SFA believes that there are substantial grounds for the Low Pay Commission to recommend that the NMW be maintained at its current rate of €9.15 per hour. This would give small businesses, especially those still far from a full recovery, certainty over their labour costs, which is essential in particular to businesses operating in the sectors and regions most affected by the NMW. Maintaining the NMW rate would also insure that job creation efforts are realisable for the low-skilled workers still on the live register. It would give them an entry point into work and upskilling from where they can develop their skills and increase their wages relative to their productivity levels. A further increase in the NMW, on top of the 5.7% increase introduced in January 2016, would be detrimental to small businesses and therefore to job creation and retention in Ireland.

We would welcome the opportunity to meet with the Commission to discuss our submission in more detail and our offer to undertake extensive research remains. For further information on any of the issues raised in this submission, please contact Patricia Callan, SFA Director, on 01-6051602 or patricia.callan@sfa.ie

More information about the SFA is available on www.sfa.ie and on Twitter @SFA_Irl