TASC Presentation to the Oireachtas Joint Committee on Enterprise, Trade and Employment

'The Minimum Wage'

20 July 2010

1. Introduction

1.1 We appreciate the Chairman's invitation to TASC to appear before the Oireachtas Joint Committee to discuss the minimum wage.

1.2 The context for TASC's presentation is the recent call by the Restaurant Association of Ireland (RAI) for a cut in the JLC wage rates[1] and our response in '*Square Deal? The Real Cost of Making a Meal in the Restaurant Sector* (TASC, 2010). Another contextual point is the call from some quarters for a reduction in the minimum wage by one euro. The TASC response is evidence-based and demonstrates that a focus on cutting wages will not address the current problems being experienced in the sector.

1.3 TASC argues that positive action needs to be taken to restore the demand in the economy that is necessary for protecting employment and creating job growth.

1.4 TASC does not accept that lowering either the minimum wage rate or the JLC rates will accomplish this goal. On the contrary, the overall effect will be to reduce the level of consumption in the economy.

1.5 Furthermore, a cut in either of these rates will negatively impact the public finances through decreased income tax, income levy and PRSI receipts and through a decreased consumption tax take.

1.6 Reducing the rates will not impact to any significant extent on Ireland's competitiveness; exporting companies tend to pay their workers well in excess of minimum wage rates.

1.7 Finally, TASC argues that lowering these rates will have a dramatically negative effect on low paid workers.

[1] Minimum rates of pay and other conditions of work, for workers in certain sectors are determined by Joint Labour Committees (JLCs). Currently, there are 13 JLCs in existence. Each JLC is composed of representatives of workers and employers in the sector concerned.

2. The negative impact on the real economy

2.1 The ongoing economic crisis has led to a general collapse in demand in the economy.

2.2 The collapse in demand, in turn, is responsible for the particular difficulties of those sectors, usually non-exporters, which hire minimum wage earners.

2.3 Consumer spending has fallen at over six times the eurozone rate[2] and the last thing we should be doing in this context is further cutting demand. On the contrary, we need to increase consumption; we need to encourage spending to boost demand in the economy.

2.4 Eurostat figures show that the great majority of advanced countries have actually increased their minimum wage rates during the current crisis[3]; they did this precisely because they understood the need to maintain demand.

2.5 Low paid workers are almost pure transmitters of demand. These are people who already spend all or almost all of their money.

2.6 Reducing the minimum wage by one euro would result in a lower level of spending throughout the economy. This reduced spending will hit all firms including those that employ low income workers.

2.7 For those firms that do not employ minimum wage rate workers or JLC rate workers, there would be no upside to the reductions; these firms will have reduced income, without a corresponding significant reduction in their cost base. This will distort the economy in favour of low paying sectors and exacerbate the job crisis in all non low-wage sectors.

3. The negative impact on the public finances

3.1 Lower wages will result in lower tax revenue (income tax, income levies, employers' and employees PRSI) at a time when the ESRI (2010) is forecasting a general government deficit of over €31billion in 2010.

3.2 TASC calculates that the direct cost to the exchequer caused by reducing the JLC rate of €9.27 to the statutory minimum wage rate of €8.65 is €1,143 per worker[4]. Please refer to Annex 1 for a breakdown of this figure.

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[2] Between 2008 and 2010, Irish consumer spending is estimated to fall by 10.2 per cent (DoF, 2009; page 10) and consumer spending in the EU is expected to fall by 1.6 per cent (European Commission, 2010a; page 27).

[3] European Commission (2010b) figures are available for 22 advanced economies. Of these, sixteen have increased their minimum wage rate since 2008, three have decreased the rate since 2008 and three have left it unchanged.

[4] See Annex 1. Calculations based on the Deloitte Tax Calculator and on Correspondence with the Department of Social Protection.

3.3 The public finances will be further negatively impacted through a reduction in VAT receipts as the annual net income of an employee working a 39 hour week would fall by €645. As low income earners have a very high marginal propensity to consume, almost all of this €645 would ordinarily be recycled as consumption spending.

3.4 In terms of the effect on exports, it is important to realise that export-oriented firms tend to be more productive and already pay significantly above the minimum wage. It follows that reducing the minimum wage is not one of the policy measures which would have a positive significant impact on Ireland's international competitiveness.

4. The negative impact on individual workers

4.1 The minimum wage was introduced in recognition of the vulnerability of low income workers. That vulnerability has not decreased in the intervening period.

4.2 Twenty-one of the 27 EU countries have a statutory minimum wage and most of the remaining countries have *de facto* minimum wages through collective agreements.

4.3 TASC argues that minimum wage laws help boost overall wage equality between women and men as the majority of minimum wage workers are women.

4.4 The minimum wage also acts as a bulwark protecting young people, migrants and other vulnerable groups against exploitation by employers.

4.5 A decrease of just one euro in the minimum wage represents a critical sum for low income families and is equivalent to a cut of over eleven and a half per cent. Such a cut would be well in excess of deflation. Other income sources, for example, child benefit, and pay in the form of the income levy (equivalent to €351 annually) have already been cut. At the same time, food prices in Ireland are the second highest in the European Union according to Eurostat (2010a), further compounding the tremendous pressure on living standards for low income workers.

4.6 A 39-hour working week on the minimum wage currently provides an income of €337 euro. According to research undertaken by the Vincentian Partnership, in 2009, a two parents and two children[5] family with one person working needed an income of €578 per week to have a minimum essential standard of living. Reducing the minimum wage by one euro per hour would see this weekly income fall to just €298 euro or 51 per cent of this Vincentian minimum standard of living.

4.7 The OECD has conducted comparative research on international levels of earnings inequality and found that in 2008, Ireland had the highest level of earnings inequality in the original EU 15

[5] Aged 10 and 15.

(OECD, 2008). Minimum wage earners did not benefit equally from the boom. Although the minimum wage was increased by 40% over the last ten years of the boom, this was lower than the average increase in weekly earnings for non-minimum wage earners (CSO, 2010).

5. Labour Costs in Ireland

5.1 The relevant cost to the employer is not the wage rate. What is relevant is the overall labour cost made up of wages and taxes.

5.2 The hospitality sector is the largest employer of low- wage workers and labour costs in Ireland are already relatively low in this sector.

5.3 The OECD's tax database shows that employer's PRSI is low in Ireland compared to other OECD countries; it also shows that the hospitality sector has the 3rd lowest labour cost in the EU15 (TASC, 2010).

5.4 The last year the minimum wage was increased in Ireland was 2007. The EU Klems (2009) database shows labour costs per hour for hospitality workers in 2007. These were

€12.84 in Ireland;

€14.85 in the United Kingdom;

Labour costs averaged €15.56 in the EU-15 as a whole;

Only Greece and Portugal had lower labour costs per employee than Ireland.

The RAI has put forward the argument that reducing enforceable pay scales in the restaurant sector will allow for a reduction in prices which will increase customer levels. However, research[6] shows that a reduction of JLC pay scales to the statutory minimum wage (a wage cut of seven per cent) would facilitate a minimal reduction in price. Abolishing JLC pay scales for general workers would mean a reduction of 61 cents per customer for a meal costing €60 for two; for a meal costing €100 for four people, the reduction would be 51 cent per customer. It is unlikely that these minimal price reductions would increase customer demand.

5.5 It should also be pointed out that those firms that are unable to pay the minimum wage are already able to avail of the 'inability to pay' clause in the existing law.

[6] The TASC report uses Fáilte Ireland research (2009) on the cost of food preparation to demonstrate the impact of cutting wages on the cost of meals. The research was based on a limited sample and TASC has undertaken additional analysis using CSO data that further supports the argument that cutting wages will have no significant impact on reducing the cost of making a meal in an effort to stimulate demand. See Annex 2.

6. Measures to support the hospitality and retail sectors

6.1 TASC argues that action needs to be taken to sustain employment in low wage sectors including the struggling hospitality and retail sectors.

6.2 Wages are just one portion of overall labour costs, which in itself is just one part (approximately one third) of overall business costs.[7] TASC argues for a full review of non-wage primary costs including utility bills; commercial rates and other input costs.

6.3 To take one example, food prices in Ireland are the second highest in the EU 27 and the natural inference from this is that there is a lack of competition at one or more points in the supply chain.

6.4 These non-competitive points in the supply chain must be identified and investigated, and steps taken to restore competition. The very existence of such an investigation may itself result in downward pressure as companies and sectors respond to increased transparency of goods pricing.

6.5 Other policy options relating specifically to the restaurant sector that merit examination include a temporary reduction in VAT and Excise taxes, the introduction of consumer vouchers and measures to boost tourism.

7. Summary of main points

7.1 Lowering the minimum wage will ultimately have a negative impact on Irish businesses because it will lower aggregate demand in the economy. Specifically, this reduced spending will directly lead to business closures.

7.2 A reduction of JLC pay scales to the statutory minimum wage (a wage cut of seven percent) would facilitate a minimal reduction in price and fail to increase consumer demand in the restaurant sector.

7.3 Labour costs are already low by EU-15 standards. At the same time the 'inability to pay' clause in minimum wage legislation protects those enterprises that are in legitimate trouble.

7.4 It is clear that Irish prices are seriously out of line with our European counterparts and TASC would encourage the Oireachtas Joint Committee to conduct a comprehensive investigation into the causes underlying these price rigidities.

7.5 To help struggling businesses, TASC would encourage the Oireachtas Joint Committee to investigate high food prices and enact new legislation to allow for tenants and landlords to enter into negotiations over current rent levels.

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[7] See Annex 2.

7.6 A reduction in the key JLC wage rates will reinforce earnings inequality and will negatively impact on the quality of life of low income workers and their families.

7.7 Finally, lowering the minimum wage will lead to further damage to the public finances and at the same time will hamper Ireland's growth potential. We need to get people spending again, and attacking the take home pay of low income earners will have precisely the opposite effect as they have the highest propensity to consume. The return of consumption will be based on wage growth, not on wage cuts.

My colleagues and I are happy to take questions.

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Annex 1:

Cost to the exchequer of changes to the minimum wage rate

	A	B	C
Hourly rate	**€7.65**	**€8.65**	**€9.27**
Weekly rate	€298.35	€337.35	€361.53
Hours	39	39	39
Weeks	52	52	52
Gross annual income	€15,514.20	€17,542.20	€18,799.56
20% income tax	€3,103	€3,508	€3,760
Tax credits, relief, etc	€3,660	€3,660	€3,660
Income tax payable	€ -	€0	€100
Income levy	€ 310	€351	€376
Health levy	€ -	€0	€0
Employee's PRSI	€ -	€0	€488
Annual net income	€15,204	€17,191	€17,836
Employer's PRSI - 8.5%	€1,318.71	€1,491.09	
10.75%			€2,020.95
Total cost to employer	€16,833	€19,033	€20,821
Exchequer gain	€1,629	€1,842	€2,985

Impact on the Exchequer = Income Tax + Income Levy + Health Levy + Employee's PRSI + Employer's PRSI

A = €7.65 per hour = €0 + €310 + €0 + €0 + €1,318.71 = €1,629

B = €8.65 per hour = €0 + €351 + €0 + €0 + €1,491.09 = €1,842

C = €9.27 per hour = €100 + €376 + €0 + €488 + €2,020.95 = €2,985

The table above shows the direct cost to the exchequer from reducing the JLC rate from €9.27 down to the minimum wage rate of €8.65. The cost is €1,143 per worker. This is €613 in employee payments with the rest (€530) coming from employer's PRSI. The employee will see a reduction in annual net income of €645.

The table above also shows the direct cost to the exchequer from reducing the minimum wage rate from €8.65 down to €7.65. The cost is €213 per worker. This is €41 in employee payments with €172 coming from employer's PRSI. The employee will see a reduction in annual net income of €1,987.

Annex 2:

Impact of reductions in wages on restaurant prices

Horwath Bastow Charleton and the CSO are the two main sources of data and analysis of the restaurant sector. The Horwath Bastow Charleton study, in relation to labour costs, is similar to the findings of the CSO's Annual Services Inquiry (2007). In that year, the CSO found the following:

Turnover (excluding VAT) in Restaurant Sector	Personnel Costs (including PRSI)	Personnel Costs as a % of Turnover
2,314,674	743,652	32.1%

The Fáilte Ireland publication estimates labour costs at 30.5 per cent of sales price.[8]

Reducing the JLC rate to the minimum wage would mean a reduction of 6.7 percent in the personnel costs of the affected employers. If we take an across the board cut of Personnel Costs of 6.7 percent (this is an over-estimate of the impact of abolishing the JLC because an across the board cut would assume that managers and other categories not covered by the JLC would also find their remuneration similarly reduced), we find that the amount reduced as a percentage of turnover (receipts) would come to 2.2 percent.

If this saving were fully applied to a reduction in turnover (this would mean that profit levels would remain the same) - then we find the following for the meal prices used in the TASC Report.

	Two People - €60	**Four People - €100**	**One Person – Lunch €10**
TASC (using Horwath Bastow Charleton data)	61 cents	51 cents	20 cents
CSO data	64 cents	54 cents	22 cents

The difference is minimal and confirms the incremental impact as stated in the TASC report. Cutting wages will have no significant impact on prices as a means of stimulating demand.

[8] Fáilte Ireland, Study to Evaluate the Cost of Food Preparation and Service Activities in the Hospitality Sector – May 2009.