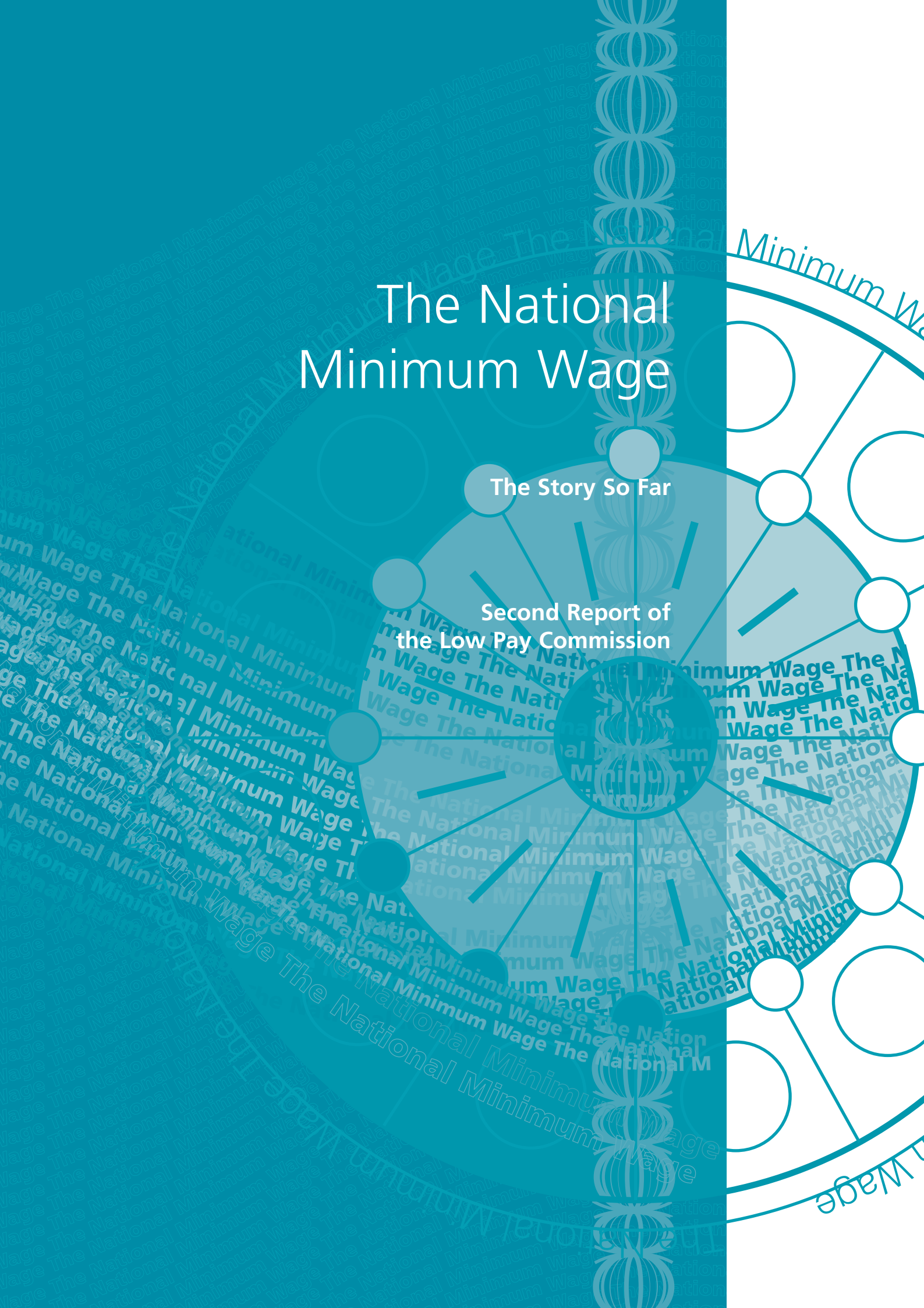


The National Minimum Wage

The Story So Far

Second Report of
the Low Pay Commission





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Second Report of the Low Pay Commission

Presented to Parliament by the
Secretary of State for Trade and Industry by
Command of Her Majesty
February 2000

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Chairman's Foreword

Based on the recommendations in our first report, the Government introduced the UK's National Minimum Wage on 1 April 1999. This was a major intervention in the labour market, yet nine months after its launch our judgment is that it has been introduced successfully. To borrow a phrase from an American study, 'the sky hasn't fallen', or, as a national newspaper put it, 'minimum wage, minimum fuss'.

When the Government announced its response to our first report, it asked us to evaluate the introduction of the minimum wage, and report our findings by December of this year. This request enabled us to set in train a full evaluation strategy well before the introduction of the minimum wage, establish baselines, agree a research programme, and begin a process of discussion and consultation which we maintained throughout the implementation period. We now have a great deal of evidence on which to base our conclusions and recommendations.

The success of the introduction of the National Minimum Wage stems in part from the prudent nature of our initial recommendations, which were based on what we believed the economy and businesses could manage, and also what we knew would benefit large numbers of low-paid workers. But it is also the result of much hard work from all those who were determined that the introduction of the minimum wage should be a success, including the Government, trade associations, unions and voluntary organisations. Great credit is also due to the employers and workers in individual businesses who had to adapt pay and working practices to ensure that workers received at least the minimum wage.

Women in low-paid work have benefited most from the National Minimum Wage, and we are pleased to see in early data that the policy has made a significant in-road in the gap between men and women's pay. More broadly, when combined with the Working Families' Tax Credit, the minimum wage makes an important contribution to tackling in-work poverty for families with children.

The Government asked us to look specifically at 21 year olds. At the time of our first report, the data and evidence could lead to a number of possible judgments. But the data for this report are far clearer: for most 21 year olds the lower statutory minimum is irrelevant, as they already receive at least the full National Minimum Wage. We are confident in recommending that 21 year olds should be covered by the full rate.

We have scrutinised the immediate impact of the minimum wage. But a full assessment cannot be undertaken now. More time is needed before national earnings data are available to help evaluate its full impact. Similarly, although our evidence suggests that compliance is reasonably high, it is too soon to offer a definitive assessment. The Government will need to continue to monitor and improve compliance levels.

In this report we have stuck to our terms of reference. We were not asked to make recommendations on uprating, or on the coverage of younger workers other than 21 year olds, and so we have not done so. But the Commission is clear that for the National Minimum Wage to continue to be a useful labour market instrument, it cannot be left at its initial rate. The level must be reassessed, so that employers can plan ahead, and low-paid workers can continue to benefit.

A handwritten signature in black ink, appearing to read 'A. Bain'. The signature is fluid and cursive, with a large initial 'A' and a long, sweeping tail.

December 1999

The Commissioners

from left to right standing:

Rita Donaghy
William Brown
George Bain
Paul Gates
Bill Callaghan

from left to right seated:

David Metcalf
Lawrie Dewar
Stephanie Monk
John Cridland



Professor George Bain (Chairman)

President and Vice-Chancellor,
The Queen's University of Belfast

Professor William Brown

Professor of Industrial Relations,
University of Cambridge

Bill Callaghan

Chief Economist, Trades Union Congress
(until 30 September 1999);
Chair, Health and Safety Commission
(from 1 October 1999)

John Cridland

Director of Human Resources Policy,
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Scottish Grocers' Federation

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General Secretary,
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Professor of Industrial Relations,
London School of Economics

Stephanie Monk, C.B.E.

Director of Human Resources,
Granada Group plc

Executive Summary

Introduction

- 1 Following our initial recommendations, the Government asked us to monitor the implementation of the National Minimum Wage and report again in December 1999. In particular, it asked us to review the position of 21 year olds. It then issued Regulations and guidance and launched an extensive advertising campaign. These helped businesses and workers prepare for implementation on 1 April 1999.
- 2 Building on our work for the first report, we commissioned twenty-three research projects, undertook large-scale surveys of companies in low-paying sectors, considered all available data and held two seminars. We took written and oral evidence and visited all parts of the UK. Our regular and open contacts with employers, workers and their representatives have been key to our work.

Findings

Impact

- 3 Several years will be needed to assess the full effects of the National Minimum Wage. But already it is clear that a large number of people have benefited. Two-thirds of beneficiaries are working women and, of these, two-thirds are part-time workers. Well over one and a half million workers were entitled to higher pay by April 1999 because of the minimum wage, and our initial assessment is that the substantial majority of these workers, in the formal sector at least, are now receiving their entitlement.
- 4 The National Minimum Wage was set cautiously so as not to undermine competitiveness. Its introduction added only around 0.5 per cent to the national wage bill, with no measurable impact on overall employment. The absence of general pressures to restore wage differentials, and the way in which firms have managed the change, mean that additional costs caused by the National Minimum Wage have been manageable for most businesses.

- 5 Employment continued to grow in low-paying sectors in the quarter following the introduction of the minimum wage, and there are no signs of a significant minimum wage effect in the unemployment figures. Our research programme and consultation show that any job losses have been small. We found many different ways in which firms were adapting to the legislation other than shedding labour. In the longer term, there is a particular need to monitor whether there are changes in the structure of employment.
- 6 Both employers and workers have adjusted well to the introduction of the minimum wage. Small businesses have been most affected, yet have successfully managed the transition. Each sector has had to adopt its own strategies to cope with the additional pay costs and, for some sectors or types of businesses within them, the adjustment has been considerable. Nevertheless, for the vast majority of employers, the transition has been successful and, consequently, most low-paid workers are receiving their full entitlement.

Defining Workers, Pay and Working Time

- 7 While in general the definitions of a worker, pay and working time have performed well, a small number of anomalies have emerged. More guidance is needed on voluntary workers and on people undertaking therapeutic activity. Coverage of students should be more consistent. The level of the accommodation deductor needs to be kept under review, and the broader question of non-standard work (such as sleeping over) should be reviewed in the longer term as the National Minimum Wage settles in.

Young People and the Development Rate

- 8 The Development Rate for young workers has meant a pay rise for very many young people while not affecting their employment opportunities. Most 21 year olds are already earning at or above the level of the full minimum wage. To include them in the upper threshold, therefore, makes sense. The data also suggest that a level of £3.20 per hour for 18–20 year olds would pose no significant problems for employers. The six-month Development Rate for older workers has the

potential to improve their employment prospects. But more work needs to be done to ensure this potential is realised.

Compliance and Enforcement

- 9 The National Minimum Wage should be largely self-enforcing, and the initial publicity was successful in raising awareness among employers and workers. Early indications are that the vast majority of businesses are meeting their obligation to pay the National Minimum Wage, but not all workers entitled to it are receiving it. The Inland Revenue has made a successful start to enforcement, adopting a pro-active stance towards non-compliance. There are further practical steps which might be taken to increase compliance by raising awareness and improving enforcement procedures.

Conclusion and Next Steps

- 10 The National Minimum Wage has been introduced successfully, with no significant adverse effects on the economy. Large numbers of low-paid workers have benefited, particularly women, and the National Minimum Wage, together with the Working Families' Tax Credit, will benefit low-income families. Low-paying sectors have adapted well. This success needs to be built on. Levels of compliance should be improved, and the minimum wage will need to be updated.

Recommendations and Suggestions

Younger Workers

Recommendations

- The Government should include 21 year olds in the coverage of the full National Minimum Wage from June 2000. (para. 6.21)
- The Government should amend the regulations so that National Traineeships are treated in the same way as Modern Apprenticeships. (para. 6.43)

Compliance and Enforcement

Recommendations

- The Government should continue to publicise the National Minimum Wage widely and, in particular, promote it effectively among the ethnic minority communities. (para. 7.27)
- The Government should fund a small number of community-based pilot projects in areas where workers are likely to be at most risk of non-compliance. (para. 7.39)

Suggestions

- In the medium term, the Government could consider the Inland Revenue working in partnership with employer and worker organisations to enforce compliance on a sectoral basis. (para. 7.37)

Definition of Workers, Pay and Working Time

Recommendations

- The Government should issue further detailed guidance on the definition of worker which is geared specifically to the needs of the voluntary sector. (para. 5.7)
- The Government should review the guidance on benefits for workers with disabilities who are in receipt of 'therapeutic earnings', with the aim of making it more coherent and accessible. (para. 5.12)
- The relevant departments and agencies should work together to produce, and widely disseminate, clear guidance on what constitutes worker status for individuals undertaking therapeutic activity to ensure that they are not adversely affected by confusion about the legal position. (para. 5.16)
- The Government should address anomalies in the coverage of students to make the treatment of postgraduates and, where feasible, students on EU/EEA higher education courses the same as undergraduates. (para. 5.23)
- The accommodation deductor should be retained at its present rate and its level considered again when the National Minimum Wage is reviewed. (para. 5.37)
- The Government should investigate whether the regulations relating to the deductor could be simplified to make compliance easier for employers. At the least, simpler guidance should be issued. (para. 5.37)
- The Government should produce specific guidance to emphasise the difference between 'sleepovers', where the assumption must be that the worker would not normally be wakened and where an allowance is usual practice, and 'on-call' and 'standby' arrangements, where a worker is required to be at the workplace outside of normal working hours with the expectation that he or she will be required to work, for which the National Minimum Wage is payable. (para. 5.41)

- The Government should ensure that the regulations on travelling time properly reflect the policy intention, which is set out in the guidance: the National Minimum Wage must be paid ‘when a worker ... is travelling in connection with his work during normal working hours or the normal range of hours that the worker does’, and, if necessary, amend the regulations at a suitable opportunity. (para. 5.46)

Suggestions

- The Government should consider the coverage of seafarers in any future review of marine policy. If it is to be reviewed, we would welcome consultation. (para. 5.24)
- The application of the ‘fair estimate’ and ‘daily averaging’ agreements should be kept under review with the aim of ensuring necessary protection is provided to workers while minimising burdens on business. (para. 5.44)

Government Funding

Recommendations

- The Government should ensure that adequate funding is made available to meet the additional costs caused by the introduction of the National Minimum Wage in social care. (para. 4.43)
- Where necessary, the Government should fully meet the additional costs caused by the introduction of the National Minimum Wage to the Supported Employment Programme. (para. 5.9)

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1 Introduction

Following our initial recommendations, the Government asked us to monitor the implementation of the National Minimum Wage and report again in December 1999. In particular, it asked us to review the position of 21 year olds. It then issued Regulations and guidance and launched an extensive advertising campaign. These helped businesses and workers prepare for implementation on 1 April 1999.

Our Task

- 1.1 Following our first report, which recommended the rate and definition of the UK's first National Minimum Wage, the Government gave us new terms of reference. These required us to monitor and evaluate the introduction and impact of the National Minimum Wage, particularly the effect on:
 - pay, employment and competitiveness in low-paying sectors and small firms;
 - particular groups of workers, such as young people, women, ethnic minorities, homeworkers, people with disabilities and voluntary-sector workers;
 - pay structures, including the effect on differentials and different pay systems; and
 - training.
- 1.2 We were specifically asked to recommend whether 21 year olds should be covered by the adult rate. In making our recommendations, we were asked to consider:
 - the wider economic and social implications;
 - the likely effect on employment and inflation;
 - the impact on costs and competitiveness of business, particularly in the small-firms sector; and
 - the potential costs to industry and the Exchequer.
- 1.3 We were asked to report to the Prime Minister and the Secretary of State for Trade and Industry by December 1999.

Preparing for the National Minimum Wage

- 1.4 In our first report we made twenty-four recommendations: thirteen on the definition; four on training and development; two on the rates of the wage; and five on implementation and enforcement. In June 1998 the Government accepted in principle all these recommendations, but some subject to further consultation in preparation for the Regulations. For example, it consulted on the treatment of pieceworking and the application of the accommodation offset.
- 1.5 There were two recommendations in particular which the Government accepted in principle but decided not to implement exactly as recommended. We recommended that 'an initial Development Rate of £3.20 per hour should be introduced in April 1999' and that 'the appropriate Development Rate in June 2000 should be £3.30 per hour'. The Government decided to phase in the Development Rate in two stages, with an initial rate of £3.00 introduced in April 1999, rising to £3.20 in June 2000. In addition, it decided that the Development Rate for younger workers should apply to all 21 year olds as well as those aged 18–20. At the same time, it announced that we would be asked to review the position of 21 year olds again in a second report. We also recommended that the 'appropriate rate for the National Minimum Wage should be £3.70 per hour in June 2000'. The Government commented that any future uprating would be subject to the Commission's evaluation and the economic circumstances of the time.
- 1.6 The National Minimum Wage Act received Royal Assent on 31 July 1998. But much hard work was needed by the Government, employers and advisory bodies to ensure that the National Minimum Wage could be implemented successfully on 1 April 1999.
- 1.7 The Department of Trade and Industry (DTI) had the task of translating our recommendations into legislation. The draft Regulations attracted substantial comment during consultation, much of which was reflected in the final Regulations. Examples of this responsiveness included the additional provisions governing salaried workers, exemptions

for au pairs and other family workers, and the decision not to proceed with provisions governing pay records. The pay-slip statement on the minimum wage, which had become impracticable and burdensome in the format proposed by the draft Regulations, was also dropped.

- 1.8 Following publication of the Regulations, the DTI issued guidance on the minimum wage aimed at workers and employers. While its lateness prompted criticism from some leading business organisations, the guidance has proved useful in explaining the very detailed Regulations.
- 1.9 Implementation of the minimum wage was accompanied by high-profile publicity. The Government invested £5 million in press, television and radio advertising. This was supplemented by a great deal of positive press interest. The publicity initiatives were very successful in raising public awareness. The Government's evidence to the Commission reports that a post-implementation poll revealed that 80 per cent of employers and 72 per cent of workers – an increase from 30 per cent before implementation – knew the principal rate of the National Minimum Wage.
- 1.10 Trade associations, unions and other organisations played an important part in preparing businesses and workers for the implementation of the minimum wage. Trade associations provided extensive guidance and support for members. The National Hairdressers' Federation, for example, held a series of meetings throughout the UK. Articles on the National Minimum Wage were published in various trade publications. Trade unions raised awareness of workers' entitlement through helplines, promotional material and meetings. Voluntary organisations also helped awareness. The National Group on Homeworking distributed posters, leaflets and advice in a range of languages.
- 1.11 We know that many businesses prepared well for the minimum wage. Evidence from our research and visits showed companies anticipating the National Minimum Wage in their wage agreements well before its introduction. But some businesses were not so well prepared. Research showed that, in Autumn 1998, hospitality employers, typically owners of small single units, were vague about implementation plans, leaving compliance to the last minute. Nevertheless, in general,

preparation was effective and resulted in a smooth launch on 1 April 1999.

Conclusion

- 1.12 Having generally accepted the recommendations in our first report, the Government produced Regulations – on which it consulted – and guidance, and undertook an extensive advertising campaign. Businesses and workers’ organisations made significant preparation for the implementation of the National Minimum Wage. This meant that employers and workers were well prepared for its introduction.
- 1.13 In this report we examine the subsequent impact of implementation on businesses and workers and describe how they have managed the transition. We also discuss issues that they have raised with us. But first we outline how we undertook our task, building on the strong relationships which we established during the preparation of our first report.

2 What We Did

Building on our work for the first report, we commissioned twenty-three research projects, undertook large-scale surveys of companies in low-paying sectors, considered all available data and held two seminars. We took written and oral evidence and visited all parts of the UK. Our regular and open contacts with employers, workers and their representatives have been key to our work.

- 2.1 The work undertaken in the preparation of our first report provided us with a good basis for our work on the second. As for that report, our recommendations are based on research and extensive consultation.

Research

- 2.2 Although time was short, we commissioned a substantial amount of original research. We publicised our requirements through the internet and professional publications, and were encouraged by the enthusiasm and desire to contribute shown by the research community and others. A group of Commissioners met under an independent chairman from the DTI to assess forty research bids. Twenty-three projects were eventually undertaken.
- 2.3 The projects were broad in scope, looking at the impact of the National Minimum Wage on the particular areas that the Government asked us to address in our terms of reference.
- **Pay structures** were considered by Incomes Data Services Ltd. and the Economic and Social Research Council (ESRC) Centre for Business Research (Hughes, Wilkinson and Bullock, 1999); both adapted their existing surveys to gather material for us.

- In order to assess the **impact on business**, Cardiff Business School (McNabb and Whitfield, 1999) analysed the Workplace Employee Relations Survey to expose the supply and demand factors characterising firms affected by the minimum wage. Leicester City and County Councils, the Leicestershire Training and Enterprise Council and the Lincolnshire Economic Development Services' Research Unit supplemented regular surveys of businesses with questions designed for us.
- Industrial Relations Services Ltd. and researchers at the Manchester Metropolitan University (Lucas and Langlois, 1999) surveyed and interviewed employers, and the Low Pay Network analysed information from their own telephone helplines, Jobcentres, and the Careers Service to provide us with information about the pay and prospects of **young workers**, and firms' employment practices for young people.
- The National Group on Homeworking analysed the pay and working conditions of **homeworkers**.
- The Association for Supported Employment surveyed its members and others in order to provide us with information about the experiences of **people with disabilities**.
- **Volunteers** and workers in voluntary organisations were covered by a project organised by the National Council for Voluntary Organisations.
- The **retail, textile, hospitality and health care industries** were specific low-paying sectors for which we commissioned projects. Researchers at Templeton College, Oxford (Undy, Kessler and Thompson, 1999) conducted sixty-six case studies in the clothing, knitwear and footwear sectors, and Leeds University Business School (Gray and Heyes, 1999) examined pay differentials and earnings distribution in textile and clothing companies in West Yorkshire. Lucas and Langlois carried out two pieces of research: on companies in the clothing and hospitality sectors, and companies in the hospitality and retail sectors. Industrial Relations Services Ltd. also focused on the hospitality and retail sectors in their second project. Finally, Pay and Workforce Research surveyed the pay rates of care-home support workers.

- Many of these projects, but in particular Pay and Workforce Research and Hughes et al., considered the impact of the National Minimum Wage on **small firms**.
- Finally, we commissioned a number of projects from Citizens Advice Bureaux in England and Wales, Northern Ireland and Scotland, the Low Pay Unit, Leicester City Council Low Pay Campaign, and the Humberside Law Centre on **compliance and enforcement** of the minimum wage.

2.4 These projects deployed a broad range of research techniques, including case studies, surveys and secondary analysis of existing datasets. They were conducted by researchers from diverse backgrounds: academics and professional researchers, as well as pressure groups, Citizens Advice Bureaux and groups backed by local authorities which work with the low paid. The findings have informed our deliberations and are reflected throughout this report. Following the publication of our report, we will make the research publicly available. In addition, much of it will be published in full by the researchers. A complete list of the projects we commissioned is at Appendix 5.

2.5 The Commission itself undertook a large survey of firms in the low-paying sectors and regions. Trade associations in the retail, hospitality and business services sectors, as well as the Yorkshire and Humberside Low Pay Unit and Leicester City and County Councils, helped us to identify appropriate firms. Questionnaires were sent out in December 1998 to assess the readiness of companies for the National Minimum Wage and the extent of changes they thought they would have to introduce. We had over two thousand replies in total, a response rate ranging from 15 per cent in some sectors to 37 per cent in others – well above the norm for this sort of survey. In September–October 1999 we sent a follow-up questionnaire which looked at the actual impact of the minimum wage on businesses, and especially on workers aged 18–21, to smaller employers in low-paying sectors. The response rate (60 per cent) was very high. We are grateful for the assistance of all the companies that completed these questionnaires and to the organisations which helped us to identify recipients; they have provided us with valuable data which are reflected in this report.

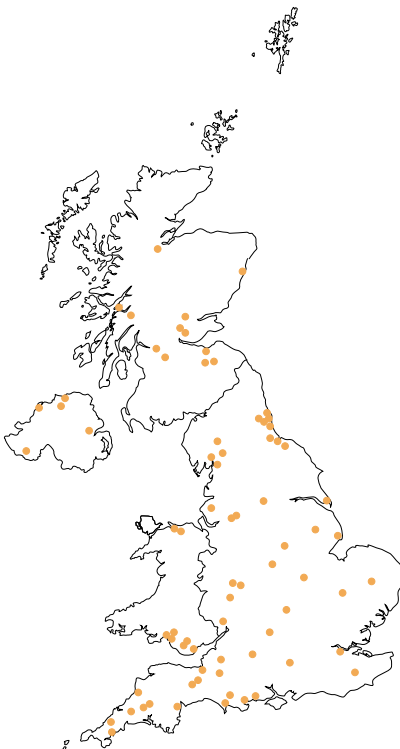
- 2.6 We reviewed all available official data. As our first report made clear, there are problems using the data currently available. Building on previous work by the Office for National Statistics to reconcile the two main data sources, the New Earnings Survey and the Labour Force Survey, we continued to make progress with it in developing better estimates of the incidence of low pay. In the Commission's Occasional Paper 1, we summarised the latest data and suggested possible improvements which could be made to the two main survey sources. But we do not have a complete quantification of low pay. The latest data, in any case, only cover the period around the minimum wage's implementation. In Chapter 3 we explore what can be learnt from available data on the initial impact of the National Minimum Wage, and we give further details in Appendix 2.
- 2.7 In preparation for this report we held two seminars. The first, in December 1998, discussed the impact of the minimum wage on household incomes, taking into account changes to National Insurance earnings limits and the Working Families' Tax Credit. Leading academics gave and discussed papers. The seminar enabled us to clarify our thinking in the light of these changes. It also reinforced our conviction that although the minimum wage cannot itself solve the problems of low pay and poverty, it is an important instrument for making a significant difference to the incomes of the low paid. The papers from this seminar have been published as the Low Pay Commission's Occasional Paper 2.
- 2.8 The second seminar, in September 1999, discussed minimum wage systems in three other countries – France, the Netherlands and the United States of America (US) – with experts from each of these countries. We were particularly interested in the components of minimum wages and enforcement practices in these countries. The papers given at this seminar are published as the Low Pay Commission's Occasional Paper 4. We are grateful to participants from both seminars.
- 2.9 We also compared minimum wages in other countries and discussed the experience of France, Spain and the US with those responsible for monitoring the minimum wages in those countries. We have followed proposals for introducing minimum wages in the Republic of Ireland and Jersey. Further information about international comparisons can be found in Appendix 7.

Consultation

- 2.10 Building on the evidence collected for our first report, we requested evidence from nearly four hundred employer organisations, trade associations, unions, voluntary organisations, pressure groups and academics. We asked them to address, in particular, the impact of the minimum wage on the economy, pay structures, particular groups of workers, training and the treatment of younger workers. We also asked for general comments on the introduction and implementation of the National Minimum Wage.
- 2.11 In all, we received almost two hundred pieces of evidence. Most of these were generally supportive of the level of the minimum wage, although a number of unions argued strongly that it had been set too low. We were impressed by the detailed and well-considered nature of the evidence that we received. Many organisations had based their evidence on independent surveys they had conducted. Some employers expressed concern over the future of the minimum wage. But all the evidence dealt positively with the initial impact. The result is a substantial independent body of knowledge. As for our first report, the evidence, unless it was given in confidence, will be made available to libraries.
- 2.12 Our website enabled people to view our terms of reference and list of publications. Between April and September, the website registered over 100,000 hits. These included around 14,000 user sessions, not only from the UK, but also Australia, Japan and the US. As a result, we received many e-mails, some submitting evidence.
- 2.13 As well as written evidence, we took oral evidence from the CBI and the TUC. We also had meetings to discuss two key issues. To learn about the impact on young people and training, we met young people themselves and the TUC's Youth Forum, the National Union of Students and the British Youth Council. We also met the trade associations which represent those sectors in which young people most often find employment: the Brewers and Licensed Retailers Association, the Hairdressing Employers Association and the National Hairdressers' Federation. To consider the impact of the accommodation offset, we met the British Activity Holiday Association, the British Hospitality Association, the Youth Hostels Association and the GMB. We are very grateful to those who took part.

- 2.14 For our first report we undertook an extensive programme of visits which enabled us to listen to those likely to be affected by the minimum wage. We continued this process as part of the consultation for this report, again aiming to cover all parts of the UK. Prior to implementation, we visited businesses to see how they were preparing for the minimum wage. After implementation, we focused on those sectors most affected, groups of workers cited in the terms of reference, and specific issues which had been raised with us.
- 2.15 We particularly wanted to meet and discuss the impact of the minimum wage with small firms. We held meetings with groups of small firms, and we also saw many small firms individually during our visits. We held discussions with the Federation of Small Businesses and their members in England, Scotland, Wales and Northern Ireland. We contributed to publications aimed at small businesses such as the NatWest Small Firms Bulletin and the *Pub Business* magazine, and we participated in an active internet discussion on the Enterprise Zone website which targets small businesses.
- 2.16 Our visits took us to the North East, the South West and the Midlands of England, as well as Northern Ireland, Scotland and Wales. We tailored our programme to address the issues raised with us as time went on. The level of the accommodation offset was one such issue; we met many organisations in the hospitality industry throughout the programme, including both large and small hotels in city centres and remote locations, people running activity holidays and workers' representatives. We also visited intentional communities. We met representatives from the brewing and licensing industry. We met organisations which train and place in work people with learning difficulties. We met voluntary bodies which rely on volunteers and some which employ workers. We discussed the Development Rate for 18–20 year olds with young people who were working to help fund their education, those trying to acquire the skills that would enable them to find permanent jobs, and agencies trying to provide them with work and training. As there are differences in the provision of education and training between the various parts of the UK, we also discussed this in Northern Ireland, Scotland and Wales as well as England.

Figure 2.1



- 2.17 We met workers who had benefited from the minimum wage, and those assisting the low paid from trade unions, Citizens Advice Bureaux, Low Pay Units, and those specifically targeting ethnic minorities and particular groups such as homeworkers. We tried to meet employers from all the low-paying sectors and, in particular those from the textile industry, care homes, childcare, food processing and catering, retail, business services and tourism. A full list of those we met, and who agreed to be listed, is given at Appendix 1.

Conclusion

- 2.18 From the very start of our work for this report, we were helped by those employing or working with the low paid. Trade associations and trade unions, Citizens Advice Bureaux, Low Pay Units and Training and Enterprise Councils were all open and enthusiastic about providing us with information and discussing our work with their members and constituents. We were invited to participate in conferences, seminars and conventions and were encouraged by the response we received to our seminars, articles and questionnaire. Unions disappointed at the level of the wage, nevertheless co-operated with us and supported our work. Similarly, employer bodies which disliked some of our recommendations were always helpful and constructive. We contributed to their work in small ways – for example, by giving talks at local meetings and writing articles for trade journals – but we benefited in large ways, through our better understanding of businesses and workers.
- 2.19 We have a wealth of information from our research, evidence and visits. And we have benefited from the enthusiasm and co-operation of employers, unions, academics, and others; their willingness to work alongside the Commission has been key to our work. Together we have developed the material on which we have formed our judgment.

3 Assessing the Impact

Several years will be needed to assess the full effects of the National Minimum Wage. But it has clearly already brought substantial benefits to large numbers of people, especially women and part-time workers. Inevitably, even a prudent rate has caused difficulties for certain businesses. But our judgment, nine months after its introduction, is that the long-term costs to business and the economy are likely to be small, and may well be difficult to identify from other developments in the labour market.

- 3.1 Several years will be needed to assess the longer-term effects of the National Minimum Wage. Nine months after its introduction, however, there is a growing body of evidence that the prudence shown in choosing the rate has helped to ensure minimal adverse impact on the economy. The early message has been 'so far, so good'.
- 3.2 Evaluating the National Minimum Wage has not been straightforward. Where to draw the baseline is, for example, unclear. There was substantial adjustment prior to its introduction, and research we commissioned from Incomes Data Services Ltd. (IDS, 1999) suggests that some firms had been making adjustments to their pay structures for up to two years in anticipation of the minimum wage. In other cases, our research shows that firms have taken until after the implementation date to comply with the new requirements (National Association of Citizens Advice Bureaux (NACAB), 1999). We have therefore needed to be flexible in our view about where to draw the baseline.
- 3.3 Within our timescale, the amount of official data available is limited. The New Earnings Survey (NES) is the primary source of earnings information, but it is conducted annually and the April 2000 survey will be the first to be entirely free of pre-implementation data. The latest official data on employment available for this report are from the Labour Force Survey (LFS) for Summer 1999 and cover one quarter after the date of introduction. We have therefore sought to gather more up-to-date information by supplementing official data sources

with a research programme, a full consultation exercise, and a survey of low-paying firms six months after implementation.

- 3.4 The implementation of the new policy has been eased by the economic environment. The economy has been stronger than forecasters predicted, and employment has continued to grow as the minimum wage came into force. Recent policy reforms have also had beneficial effects. The new Working Families' Tax Credit complements the National Minimum Wage in promoting work incentives, while reductions in employers' National Insurance Contributions may have enabled firms to absorb higher wage costs more easily. The New Deal has contributed to falls in youth unemployment. The Working Time Regulations were introduced in October 1998. These broader developments make it difficult to identify the effects of the minimum wage.

Beneficiaries

- 3.5 Our work shows that the National Minimum Wage has already helped a large number of workers. National earnings data which fully reflect the implementation of the minimum wage will not be available until Autumn 2000. Existing data are also subject to revision. In this report, therefore, rather than second guess future official statistics, we present our judgment of the number of workers helped by the minimum wage. This judgment is based on a wide and varied range of research and an extensive consultation programme, together with an early appraisal of the emerging data.
- 3.6 Last year we estimated that around 1.9 million workers would be entitled to higher pay because of the National Minimum Wage. These estimates were based on Spring 1998 data and assumptions about earnings movements over time. We used the Office for National Statistics (ONS) methodology, which makes adjustments for known biases in the two main sources of earnings statistics, the NES and LFS, and took the mid-point of the range as the best estimator. The details of these estimates and assumptions were set out in our Occasional Paper 1, which we published to alert users of the data to the remaining problems, and to encourage the ONS to make further improvements.

- 3.7 In the light of ongoing development work, the ONS now advises that the best estimate of low-pay incidence is more likely to be towards the bottom of its existing range and closer to the NES estimates. This advice means that the number of workers entitled to higher pay in April may have been lower than originally estimated. The revised ONS advice, and our original assumption about earnings growth, suggest that the number of workers entitled to higher pay because of the minimum wage was around 1.7 million. Our own analyses of the data, outlined in Appendix 2, confirm that the figure is well over 1.5 million. Moreover, these estimates do not incorporate recent employment growth in low-paying sectors which means that the number of workers benefiting from the minimum wage continues to grow.
- 3.8 How many workers have benefited so far? Our assessment is that the substantial majority of workers directly entitled to higher pay are now receiving at least the minimum wage. The April 1999 NES data, for example, which represent a pay period very soon after the introduction of the minimum wage, show very substantial changes to the bottom of the earnings distribution. In the year to April 1999, the proportion of employees earning below the minimum rates fell from over 5 per cent to below 2 per cent.
- 3.9 Our work suggests that compliance is now significantly higher than indicated by the April 1999 NES. The pay period for some employees in the survey may partly relate to March, while many pay settlements incorporating the minimum wage were awarded on or around 1 April. Hence a large number of workers may not have received their first post-settlement pay packet until later. In addition to some well-publicised cases of delayed payment, our own research and consultation provided clear evidence of employers who did not implement the minimum wage until later in the year.
- 3.10 While compliance in the formal sector is likely to have increased significantly since April 1999, it is likely to be less for the economy as a whole. The NES undersamples low-paid workers and those in the informal economy where compliance is likely to be lower. The best alternative official source of earnings data for employees outside the NES is the LFS. The latest LFS data for Summer 1999 show little evidence

of a minimum wage effect; a large number of workers are shown still to be below the minimum rates. The current ONS advice, to use the lower bound of its adjusted range, places less weight on the LFS data. This, together with the evidence we have gathered through research and consultation, leads us to believe that there are problems with using the LFS to measure compliance with the minimum wage.

- 3.11 In any case, official data sources are not ideal for making precise estimates of compliance. Ongoing development work may, in time, improve the quality of information from the LFS. But measurement errors and resulting imprecision are inherent in all household surveys and the LFS data cannot provide any real indication of compliance. We note that similar surveys in countries with long-established minimum wages, such as the US and France, show large numbers of workers below any minimum rates. Compliance in both these countries, however, is regarded as close to universal. Furthermore, not all employees over the age of 22 are legally entitled to the full minimum wage. The minimum rate for workers on accredited training schemes with a new employer is £3.20 per hour, and part of the cost of accommodation for live-in employees can be offset against the minimum wage. These individuals cannot be identified in existing surveys, which is a further reason why official data cannot be used as an absolute measure of compliance.
- 3.12 Our own research reveals that, even in the less formal sectors of the economy, substantial numbers of workers are now receiving the minimum wage. While both research from NACAB and the Government's evidence show a large number of complaints about underpayment, levels are well below those associated with other breaches of employment law. Compliance has also improved as awareness of the minimum wage has increased. It has taken time for workers to secure their rights. The Government's evidence shows that compliance has improved as enforcement procedures have bedded down. Where complaints have been made, the vast majority of employers have chosen to comply before an enforcement notice is served. Formal enforcement procedures will have increased compliance further.
- 3.13 In summary, we conclude that workers throughout the economy have benefited from the minimum wage. Our

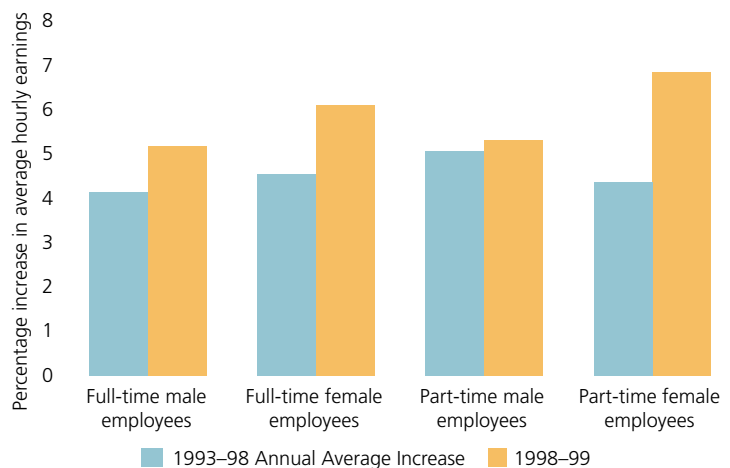
judgment is that well over 1.5 million workers were entitled to higher pay as a direct result of the legislation. A clearer picture of the number of beneficiaries will emerge when the Spring 2000 data are released, and we hope to publish our own interpretation of any new data in due course. In the interim, we are clear that the substantial majority of workers, in the formal sector at least, are now receiving their entitlement. We also note that those who are not yet receiving their full entitlement are more likely to be part-time or casual workers, working a relatively small number of hours. Hence the proportion of hours paid at the minimum wage or higher is likely to be greater than the proportion of jobs.

Women

3.14 The National Minimum Wage has been of particular benefit to female workers. In the year to April 1999, the gap in the average hourly pay of women relative to men narrowed by a full percentage point, the largest amount for almost a decade. The average hourly pay for part-timers increased significantly more rapidly than for full-timers, in contrast to recent trends (see Figure 3.1). We used the NES to examine employees whose pay was raised to the minimum rates or higher in the year to 1999. This shows that over two-thirds of the beneficiaries were women, of whom two-thirds worked part-time.

Figure 3.1

Percentage Increases in Hourly Earnings by Sex and Employment Status



Source: NES, April 1993, 1998, 1999

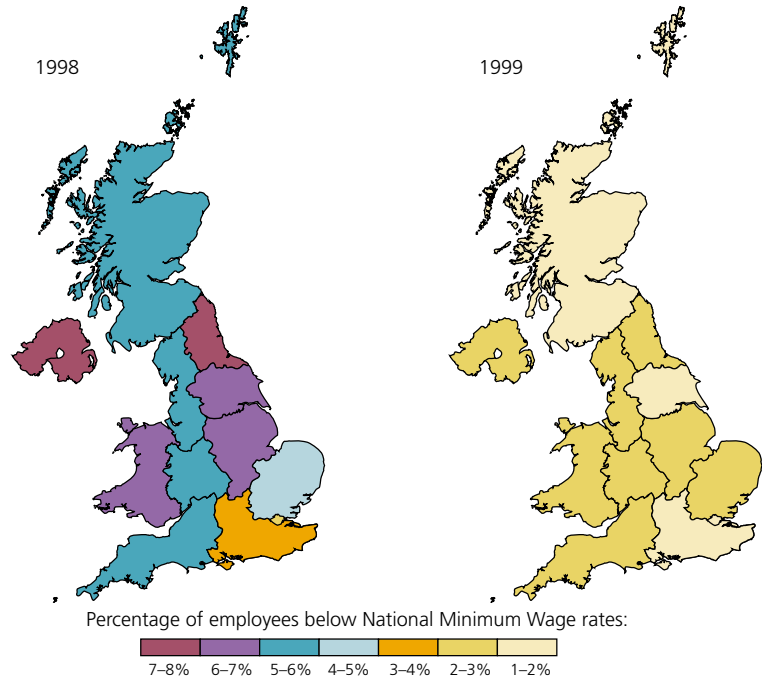
- 3.15 The full impact of the National Minimum Wage depends on the complex interaction between pay and benefits. For example, a lone mother previously working sixteen hours a week for £2.75 an hour would have seen her basic weekly pay rise from £44 to £57.60 because of the National Minimum Wage. Her weekly take-home pay, together with Child Benefit for two children and Family Credit, would rise from £148.10 to £161.70 with the National Minimum Wage. The introduction of the Working Families' Tax Credit, with its more generous income tapers and help with childcare costs, increases her weekly income substantially to £226.10.
- 3.16 The Working Families' Tax Credit was introduced only in Autumn 1999, and more time will be needed to assess its full effect. In any future report we will want to look in detail at the interaction of minimum wage levels with other income and outgoings to assess their impact on women's earnings and family income more broadly.

Regions

- 3.17 Official data show that every region has benefited substantially from the National Minimum Wage. Figure 3.2 shows the fall in the number of employees earning below the minimum rates by region in the year to April 1999. The largest falls were in the lowest-paid regions such as the North East, hence the incidence of low pay across the regions has become more evenly spread as a result of the National Minimum Wage. The incidence of low pay is still lowest in London, though it is now closer to the UK average.

Figure 3.2

Proportion of Employees Below Minimum Rates by Region



Source: NES, April 1998, 1999. Note: England is split into Government Office Regions.

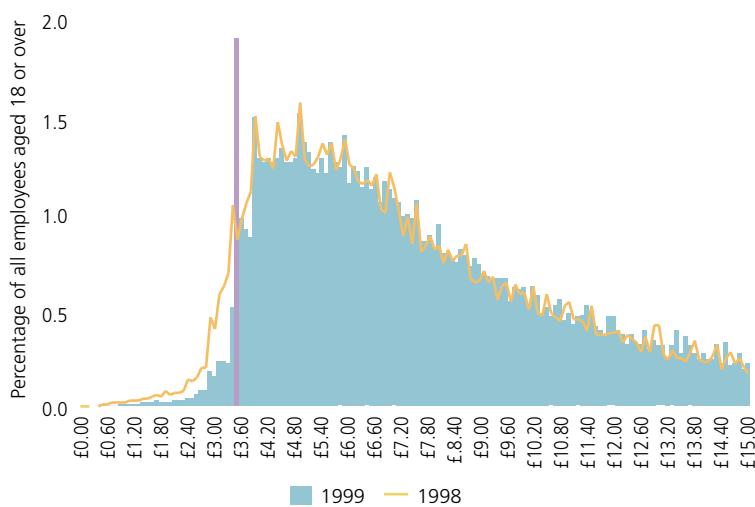
Earnings Distribution

- 3.18 For many years up to the mid-1990s, wage inequality had widened in the UK. Indeed, the need to secure greater equity in the workplace, and ensure that the lowest paid have a greater share in economic development, was a key aim of the new policy. How far wage inequality has been reduced, and at what cost, are therefore important questions about the impact of the minimum wage. We have examined official data to see how the pattern of earnings in the UK has altered during the implementation of the policy. There appear to have been some very significant changes.
- 3.19 Analysis of the NES, detailed in Appendix 2, shows that median hourly earnings for those employees earning below the minimum rates in the 1998 sample who were also in the 1999 survey, rose by around 20 per cent during the year – with a mean of around 30 per cent. Figure 3.3 shows that a large spike has emerged at the floor of £3.60 at April 1999. There are also spikes just above the minimum rate, and IDS have reported evidence of a ‘mezzanine’ effect around £4.00 per

hour as a result of the National Minimum Wage (IDS, 1999a). Such features are likely to have been present in some measure prior to the minimum wage, but we are aware of employers who choose to make specific adjustments because they wish to pay above the legal minimum.

Figure 3.3

Hourly Earnings Distribution

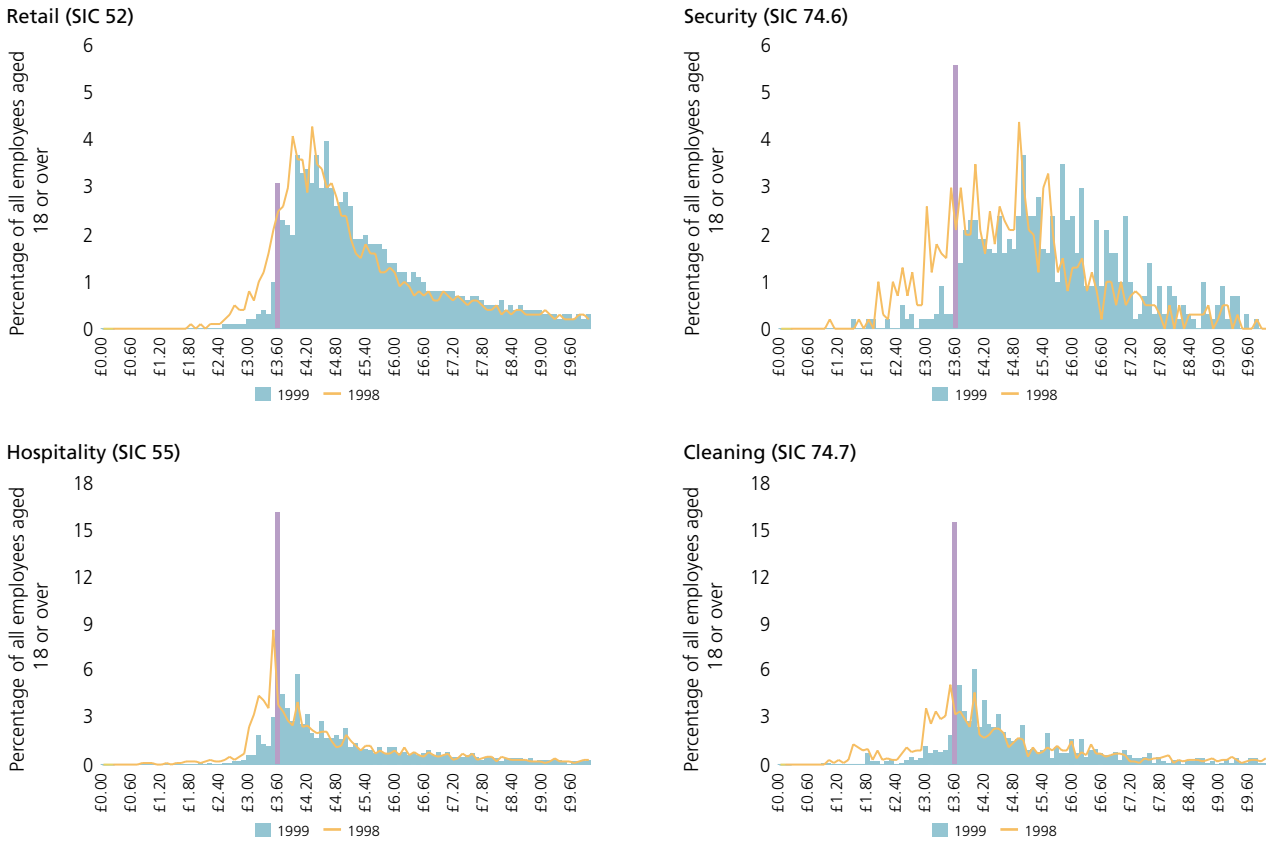


Source: NES, April 1998, 1999

- 3.20 A minimum wage effect on the earnings distribution is even more evident in the low-paying sectors. Figure 3.4 shows the latest figures for the distribution of earnings in retail, hospitality, cleaning and security. In retail there has been a shift in the earnings distribution to the right of £3.60, while the adjustment is even more apparent in hospitality and cleaning, where 16 per cent of employees earned £3.60 an hour. The earnings distributions for other low-paying sectors show similar movements in the period up to implementation (see Appendix 2).

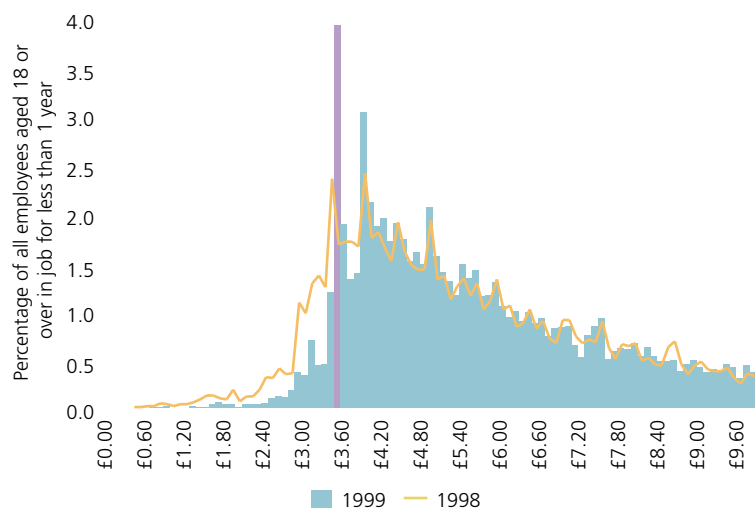
Figure 3.4

Hourly Earnings Distribution in Low-paying Sectors



Source: NES, April 1998, 1999

3.21 Further signs of an impact of the National Minimum Wage are evident in data on the pay of people entering new jobs. We examined the distribution of earnings for employees who had been in a job for less than a year using the April 1999 NES (see Figure 3.5). The data show a clear spike around the new minimum rates for these entry jobs, with around 4 per cent of employees earning £3.60 an hour. We also used the panel element of the NES to examine the earnings progression of individuals who were below the National Minimum Wage at April 1998. Of these, over three-quarters were being paid the National Minimum Wage or higher at April 1999, and almost a quarter needed a pay rise to comply with the legislation.

Figure 3.5**Hourly Earnings Distribution of New Jobs**

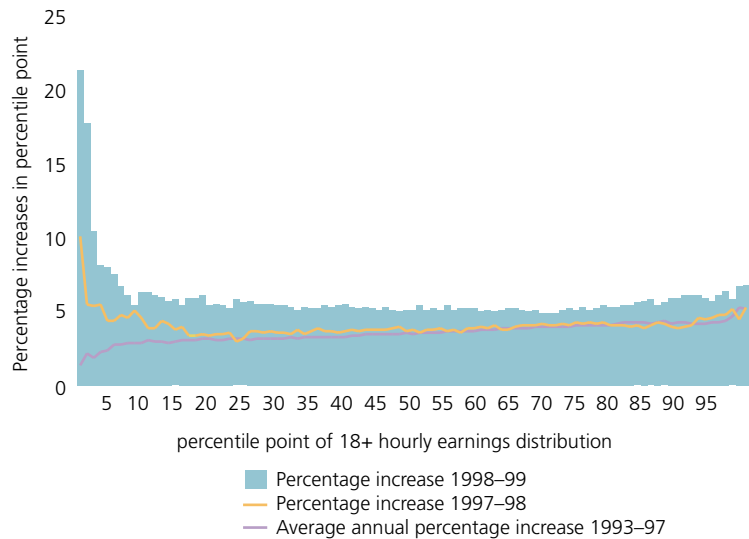
Source: NES, April 1998, 1999

Pay Differentials

- 3.22 A major consideration in making our recommendations was that the National Minimum Wage should be set at a level which limited the reassertion of pay differentials by higher-paid workers. Hence we went to considerable lengths to investigate the likely consequences for pay differentials. We probably need to observe at least another round of pay settlements before assessing the full effect. The early signs, however, are reassuring and support the judgment of our first report that 'the effects would generally peter out in the bottom half of the earnings distribution'.
- 3.23 Figure 3.6 shows the increases in pay across the earnings distribution for the year to Spring 1999 and earlier periods. The latest figures show that the highest percentage gains in pay went to workers at the very bottom of the distribution. This reverses the trend over the last two decades when larger gains in pay generally went to the highest paid. The figure also shows that above-average gains were experienced only up to the lowest twentieth percentile of the earnings distribution, which has a value just under £5 per hour. Thus it is clear that the impact of the National Minimum Wage has so far been largely confined to the very bottom of the earnings distribution.

Figure 3.6

Percentile Increases in Hourly Earnings



Source: NES, April 1993, 1997, 1998, 1999

- 3.24 The view that pay restoration has been extremely limited is also supported by findings from our research programme. IDS, for example, reports that it has ‘not encountered much obvious discomfort regarding differentials which could not be addressed in a straightforward way’ (IDS, 1999b). There appears to have been some erosion of differentials between the lowest-paid workers and those immediately above them where strata of responsibility are narrow, but employers do not appear to be restoring the differential. Thus, for example, at Wolverhampton and Dudley Breweries the lowest grade rate, which is for bar staff, saw an increase of 14 per cent but the supervisor rate was increased only by 4.8 per cent from April 1999.
- 3.25 The absence of pay restoration has also been confirmed by our consultations. For example, on a visit to the South West we were told by representatives of the care sector that the main impact upon differentials had been in the £3.60 – £5 per hour range. Further evidence of limited knock-on effects was also presented in the TUC evidence which indicated that ‘some firms have used the introduction of the NMW to amend pay structures, perhaps amalgamating the bottom rungs, while others have squeezed differentials at the bottom of the ladder rather than passing the NMW increases on up’.

- 3.26 We undertook a survey of businesses, drawn mainly from the retail, hospitality and business services sectors, to investigate the impact of the National Minimum Wage on differentials. This drew a response from over two thousand firms. Over four-fifths of these firms said that the pay of employees over £3.60 per hour would be unaffected. In a follow-up survey, primarily of small firms in hospitality and retail conducted in September–October 1999, we asked the firms which said they would be directly affected by the National Minimum Wage about the pressures for pay restoration. A third of respondents who said they would be directly affected indicated that they had increased pay for those above the minimum rates. The effects were concentrated towards the bottom of the earnings distribution; around three-quarters of firms which raised pay above the minimum rates did not do so above £5 per hour, and over 85 per cent did not do so beyond £6. These results are consistent with international evidence which suggests that minimum wages cause substantial compression of the earnings distribution.
- 3.27 Looking at the latest pay agreements, there are differences between firms. In particular, there are different approaches between businesses where pay is determined through collective bargaining and those where it is not. Appendix 4 includes some examples of differential increases under collective agreements and also within non-negotiated awards. With collective bargaining now covering only a minority of employees (Workplace Employee Relations Survey, 1998), especially in the sectors most affected by the National Minimum Wage, and with the lowest-paid workers being less likely to be union members, the pressure to restore pay differentials may be muted. Even in those low-paying sectors covered by collective agreements, some unions have said they do not intend to push for restoration of differentials.
- 3.28 In organisations with collective bargaining which had rates below the National Minimum Wage, there were generally higher increases for lower-paid than higher-paid staff. Where organisations had no union involvement in pay determination, the only change to the pay structure tended to be the increase for those below the National Minimum Wage; other grade rates generally remained unchanged. For example, at Thomas Cook junior staff were raised to a minimum of £7,020 per year

Low Pay Commission Research

We commissioned Incomes Data Services Ltd. to prepare four quarterly reports from April 1999, monitoring changes in pay structures among the low paid. Questions on the National Minimum Wage were added to their regular monitoring procedures, and an additional survey was undertaken covering sectors where low pay is prevalent. It found 'little evidence of much knock-on effect further up pay structures as a result of the introduction of the NMW'.

IDS, April, July, October, December 1999. Quarterly Report to the Low Pay Commission on the National Minimum Wage.

(£3.60 per hour); but other pay rates remained unchanged, although there were few, if any, staff below this salary.

- 3.29 Even where employers have reported an impact on differentials, further investigation indicates that only small numbers of employees have so far been affected. In some cases, the lowest grade rate minimum was below the minimum wage but there were very few workers in that grade. There have also been major changes in grading and pay progression systems in recent times which may explain the lack of restoration. IDS pointed out in its research for the Commission that traditional fixed differentials are increasingly outmoded and mainly limited to manufacturing (IDS, 1999c). Many grading structures are now very flat with pay progression more likely to be based on individual merit, rather than some fixed hierarchy of pay steps. So far, differential restoration seems to have been very limited.

Low Pay Commission Research

We commissioned Paul Edwards, of the Industrial Relations Research Unit, Warwick University, to examine managerial responses to the National Minimum Wage. He produced a report based on case studies conducted by Warwick University and Cardiff Business School masters' students. The report concluded that the firms studied seemed to have absorbed the costs of the National Minimum Wage relatively easily, but further development of skills and productivity needs to be tackled.

P. Edwards, 1999. *Minimum Wages and Work in Low-wage Sectors: Six Studies.*

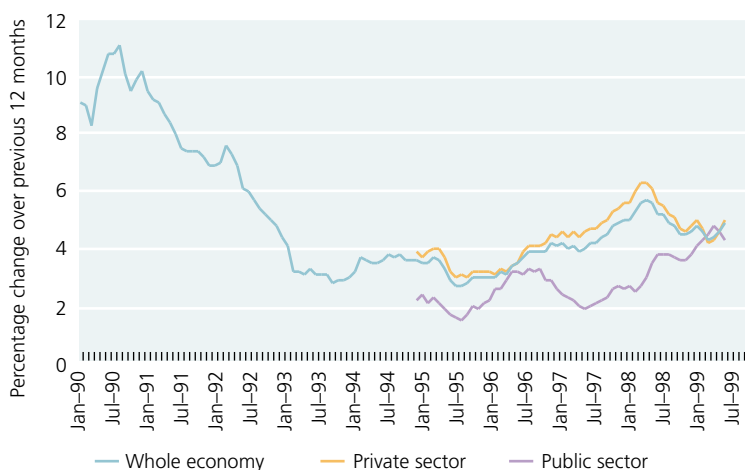
Competitiveness

- 3.30 The National Minimum Wage was set cautiously so as not to undermine competitiveness. Nevertheless, we are conscious that its impact on economic performance will depend on a number of critical factors. Our research has identified highly-varied responses under similar conditions, and for businesses to adapt successfully they need to take a constructive approach to the legislation (Edwards, 1999).

Business Costs

- 3.31 The impact of the minimum wage appears to be widespread among businesses. Secondary analysis we commissioned on the 1998 Workplace Employee Relations Survey suggests that around one-third of establishments had employees who would have been entitled to higher pay by the National Minimum Wage (McNabb and Whitfield, 1999). We are aware that the legislation has been a particular challenge for firms where profitability is low or the scope for innovation is limited, but the absence of general pressures to restore wage differentials, and the way in which firms have managed the change, mean that the costs have been manageable for most of them.

- 3.32 Various special surveys quantify the costs incurred by low-paying firms. A survey we conducted in September–October 1999 covered over 350, mainly small firms in retail and hospitality, whose pay bill costs had risen because of the minimum wage. Among the firms whose pay bill had risen, 87 per cent reported that the rise had been under 10 per cent; half the firms in retail stated that their pay bill costs had risen by 5–10 per cent, while the corresponding figure for hospitality was a third. A national survey by the British Chambers of Commerce estimated that employment costs had risen by an average of 6 per cent among those firms directly affected by the National Minimum Wage. They concluded that ‘most firms have been able to afford to lower their profits to cope with the NMW’.
- 3.33 While official data can be examined in order to assess the overall costs to business, interpreting the figures is not straightforward. We do not know what wage growth would have been in the absence of the policy, nor are official data sufficiently accurate to assess very small effects. Nevertheless, if the National Minimum Wage had had a substantial impact on business costs, we should have seen an irregular rise in the average earnings index (AEI) during its introduction. This has not happened. Figure 3.7 shows that the growth in the AEI during Spring 1999, the period when many employers were adjusting to the forthcoming legislation, was below the level a year previously. There was a slight rise in the March figure which the ONS attributes largely to bonus payments, while the growth actually fell in April.

Figure 3.7**Average Earnings Growth**

Source: Average Earnings Index, ONS.

Low Pay Commission Research

We commissioned Robert McNabb and Keith Whitfield, of Cardiff Business School, to use the 1998 Workplace Employee Relations Survey to examine the characteristics of firms directly affected by the National Minimum Wage.

They found that low pay was more prevalent in small and medium-sized establishments, though the link between work unit size and low pay is more complex than previous research suggested. Low pay was also more prevalent where there was no collective bargaining, and where there was a high degree of competition in the product market.

R. McNabb and K. Whitfield, 1999.
Low Pay in Britain: Analysis of the 1998 Workplace Employee Relations Survey.

- 3.34 The AEI omits firms with fewer than twenty employees and so does not pick up the earnings of many of those affected by the National Minimum Wage. But the NES shows that average earnings growth in the year to April 1999 was similar regardless of whether businesses employed more or fewer than twenty employees. The Monetary Policy Committee had assumed that the National Minimum Wage would add around half a percentage point to average earnings in the six months following its introduction. It has noted, however, that nominal pay growth declined during the period when the National Minimum Wage was introduced, and that the slowdown in recent private-sector earnings growth may indicate a weaker-than-expected initial impact of the minimum wage. Based on current data they have lowered their estimate of the impact of the minimum wage on earnings growth by one-third (Bank of England, *Inflation Report*, November 1999).
- 3.35 In our first report, assuming the maximum of two million beneficiaries, we estimated the first-round direct cost of the National Minimum Wage on the UK wage bill to be 0.6 per cent. We know that many firms have taken measures to control pressures on their wage costs, and our own survey shows that two-thirds of affected firms had done so. We have already explained that the potential number of beneficiaries is slightly lower than the original estimate, and compliance is building up. These developments lead us to conclude that the overall direct impact on the wage bill has so far been around 0.3 per cent, a figure which is likely to increase as compliance levels improve.
- 3.36 The indirect impact of the National Minimum Wage has similarly not been large. We have assessed the impact of pay rises for those at the bottom of the earnings distribution on the overall wage bill (see Appendix 2). Based on evidence from official data and our consultation, our judgment is that the impact of the National Minimum Wage on the overall UK wage bill, covering both the direct and knock-on effects, has so far been around 0.5 per cent.

Productivity

- 3.37 While many of the UK's best companies match the performance of their overseas counterparts, productivity lags behind other major economies in a number of low-paying sectors (O'Mahony et al., 1996). Hence the overall impact of the National Minimum Wage on productivity is likely to be small, and extremely difficult to measure. The Federation of Small Businesses in Northern Ireland told us that the minimum wage had damaged incentives for some firms using piece rates. In contrast, we have evidence of companies which have made a virtue of necessity and taken steps to improve productivity. Other employers have also noted the protection given by the legislation from low-wage competitors. Large firms in security, for example, have favoured a National Minimum Wage because it reduces low-paying operators' ability to pitch for business based on unfair employment practices.
- 3.38 We commissioned the Economic and Social Research Council (ESRC) Centre for Business Research to examine the impact of the National Minimum Wage on employer responses among small and medium-sized enterprises (Hughes et al., 1999). From a survey of over 1,500 enterprises between June and October 1999, they found that a sizeable minority of firms had attempted to improve their competitive performance, and a significant minority had invested in capital equipment to raise productivity. In general, there was more emphasis on cost advantage than product and service design. In cleaning and security, however, firms with a high proportion of low-paid workers were placing a stronger emphasis on improving product and service quality. The research concluded that this may be because there were fewer opportunities for non-wage competition in sectors where low wages were endemic.
- 3.39 In our own post-implementation survey of firms directly affected by the minimum wage, we found evidence of firms responding positively. Of these, three-fifths said they had made some changes to the way work was organised, one-third had increased their use of new technology, and one-third had improved the quality of service they provide (Figure 3.8 overleaf). For many firms the changes were slight, though half of the firms had taken significant action to improve efficiency.

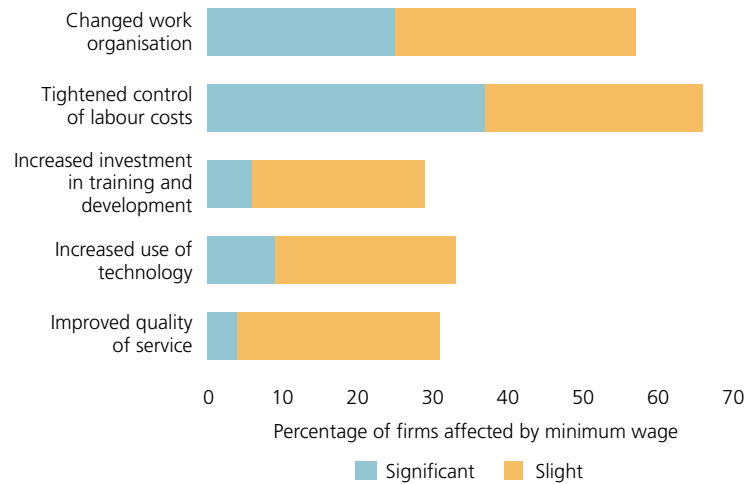
Low Pay Commission Research

We commissioned the Economic and Social Research Council's Centre for Business Research at Cambridge University, to examine the impact of the National Minimum Wage on employer responses to training strategies, labour substitution, internal wage differentials and competitive positioning. Over 1,500 responses were received from a survey conducted between June and October 1999. The interim study reported no evidence of substitution of younger workers for other age groups; small positive effects on training were found for small and medium-sized firms but not for micro-firms; a sizeable minority of firms had responded to the minimum wage by attempting to improve competitive performance.

A. Hughes, S.F. Wilkinson and A. Bullock, 1999. *Assessing the Impact of the National Minimum Wage on Small and Medium Size Enterprises.*

Figure 3.8

Action Taken to Improve Efficiency as a Result of the National Minimum Wage



Source: Low Pay Commission Survey, September-October 1999.

3.40 A number of examples of improved productivity emerged on our visits programme. One major manufacturer told us that the prospect of the minimum wage had prompted it to move earlier from traditional individual piecework to more efficient and flexible team-working piecework. In South Wales a retail company said that managers would be focusing more on improving the efficiency of existing staff as a key to success. A hotel in the South West had been led to reappraise the efficiency of split shifts. While such evidence is anecdotal, it does suggest a variety of positive responses which firms have adopted.

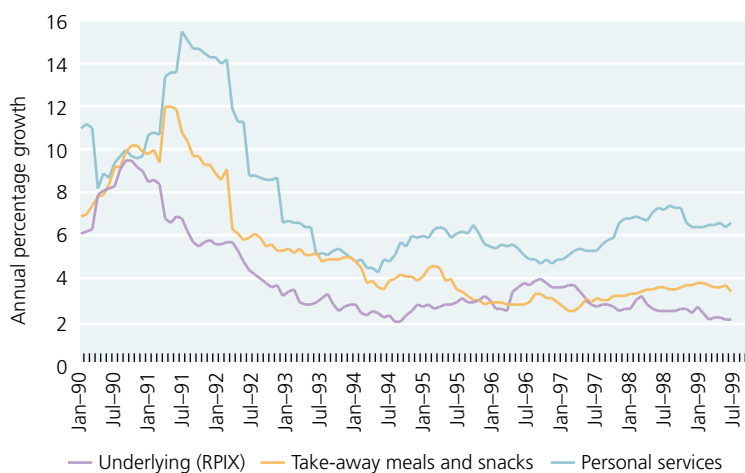
Prices

3.41 In our first report we concluded that the National Minimum Wage was likely to cause a small, temporary effect on prices, but that it was 'unlikely to cause a lasting increase in inflationary expectations'. From our evaluation, it is clear that, faced with pressures on their pay bill, employers in low-paying sectors have found a wide range of ways to adapt. So far, the effect on prices appears to have been extremely small, even when focusing on the products of low-paying sectors.

3.42 External factors, such as the strength of sterling and global economic weakness, have helped subdue inflation during the period when the National Minimum Wage was introduced. Moreover, we would expect its impact on prices to be spread over time because of employer anticipation, the time taken for compliance to develop, and time lags between rises in labour costs and adjustment in prices. We cannot, however, detect any impact on the aggregate Retail Prices Index in the first few months of the National Minimum Wage. In the six months following its introduction, underlying inflation has remained below its target of 2.5 per cent (see Figure 3.9). Last year, the Bank of England estimated that the minimum wage would have a small, temporary effect on inflation, adding 0.4 per cent to prices over two years. In its November 1999 *Inflation Report*, it lowered the estimate of the impact on earnings growth by one-third, which would also indicate a weaker-than-expected impact on the price level.

Figure 3.9

Retail Price Growth



Source: Retail Prices Index, ONS

3.43 We examined the Retail Prices Index by sector. Indices for products associated with low pay, such as take-away meals and personal services, show no signs of significant price rises in the six months since the policy was implemented. We came across specific employers – for example, in hairdressing, small hotels and care homes – who attributed price rises to the National Minimum Wage. Several activity holiday centres in

the South West, for example, said they were raising prices. A number of employers also noted that the costs of contracted-out services, such as cleaning and security, have risen. So far, these effects have not been sector-wide.

- 3.44 The impact of the National Minimum Wage on prices has been concentrated on particular employers, and has been spread over time. More time is needed for the full effects to appear. For these reasons it is difficult to detect an effect in monthly economic data, even when looking at indices for low-paid products. We consider that factors other than the minimum wage will continue to dominate the general inflation outlook.

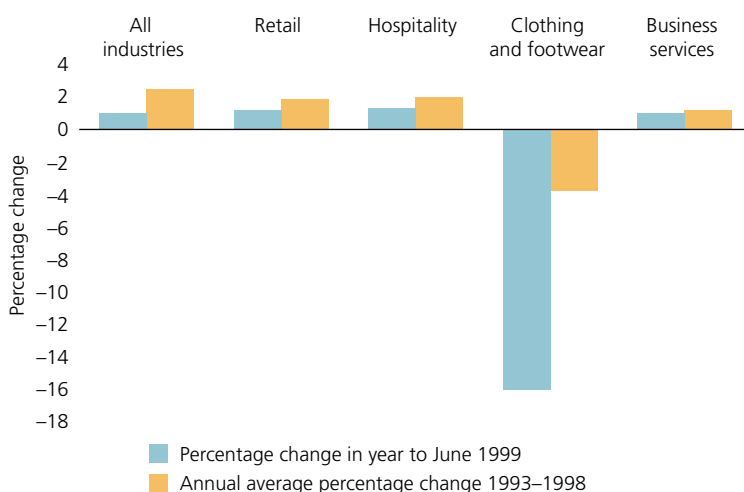
Employment

- 3.45 In our first report, we noted that the National Minimum Wage might well cause re-organisation within sectors and businesses, and that some jobs were likely to transfer to more efficient firms. Nevertheless, the links between the minimum wage and employment are by no means automatic, and we have observed many different ways in which firms are adapting to the legislation other than shedding labour.
- 3.46 The minimum wage has clearly brought challenges for certain companies, particularly smaller firms in low value-added sectors, and there is anecdotal evidence of some restructuring. In the course of our consultation, we came across companies in low-paying sectors which told us they had cut jobs or hours as a result of the National Minimum Wage, a point also made by a number of employers' representatives. The written evidence from the CBI, for example, noted that 'some job losses have been reported as a result of the minimum wage, but these do not appear to have been very significant'. This message also emerged from our post-implementation survey of small firms in retail and hospitality. Whether such changes are caused by the National Minimum Wage alone, and to what extent the demand transfers to other businesses, is difficult to determine.
- 3.47 So far, the signs in the official data are reassuring. Stronger-than-expected economic growth has dominated the outlook for the labour market, which continued to improve in the quarter following the introduction of the minimum wage.

Employment also continued to expand in Summer 1999 in retail, hospitality and business services, the largest low-paying sectors (Figure 3.10), and the share of total employment in retail and hospitality increased in the year to June 1999. But it is too early to assess whether job creation would have been even higher in the absence of the National Minimum Wage. Employment in clothing and footwear has been falling, continuing the long-term decline.

Figure 3.10

Employment Growth in Low-paying Sectors



Source: Employee jobs series, ONS

- 3.48 More up-to-date information than the official data has emerged from our consultation and research. The British Hospitality Association is typical when it says that in its sector ‘the impact on jobs appears to have been small’. We know that a number of larger companies in low-paying sectors, such as fast food and pubs, are expanding employment despite the additions to their labour costs. A similar message emerged from our research programme, both from studies across the economy and in particular regions and sectors. Thus IDS ‘found little evidence of any negative employment effect from the introduction of the NMW’, while a study of the textile industry in West Yorkshire concluded that ‘in the majority of cases, pay increases had not resulted in a reduction in employment’ (Gray and Heyes, 1999).

- 3.49 We also examined developments in hours worked. The growth in total hours slowed in the year to Summer 1999. During this period average weekly hours fell for male full-time workers, but were maintained for female part-time workers, the group most affected by the National Minimum Wage. Hence the slowdown in growth of hours worked may largely reflect the Working Time Regulations introduced in October 1998, and cuts in overtime during the slowdown in the economy in the first half of 1999. There is evidence from our consultation of adjustments to hours. The Brewers and Licensed Retailers Association, for instance, noted that one way to offset extra costs has been to 'review the hours of work required when recruiting new employees'. But such cases do not appear to be sufficiently widespread to show in the official data.
- 3.50 There has been some speculation that the National Minimum Wage might alter the age structure of employment. More time is needed to make a definitive assessment, but our research suggests that so far any such effects have been negligible. A study of over 1,500 small and medium-sized businesses in Summer 1999 found 'no evidence of substitution of younger aged workers, who are paid lower NMW or who are outside its scope, for older workers' (Hughes et al., 1999), while research by Industrial Relations Services Ltd. found 'only marginal evidence of age-related labour substitution as a result of the NMW' (IRS, 1999). We received little evidence on restructuring in our consultation, though the National Hairdressers' Federation told us that the minimum wage may cause employers to review the contracts of the least productive 19 year olds, and employ cheaper 16 and 17 year olds.
- 3.51 There is a longer-term need to monitor whether there are any changes in the types of jobs available and the status of workers. In hairdressing, for example, we were told that the minimum wage might increase the trend for stylists to operate as self-employed independent contractors within hairdressing salons, and the Biscuit, Cake, Chocolate and Confectionery Alliance reported that the introduction of the National Minimum Wage has resulted 'in a reduction in part-time and seasonal staff'. The minimum wage might cause employers at the fringes of the legitimate economy to make more use of 'cash-in-hand' employment to avoid compliance. Conversely, the protection that the legislation offers may attract workers

out of the informal economy into legitimate employment. The extent of the informal economy, and thus whether the minimum wage has had any impact, is difficult to assess. We will be interested to see the report, due in Spring 2000, which Lord Grabiner QC is conducting for the Chancellor into the nature and scale of the informal economy.

Income Distribution

- 3.52 The impact of the National Minimum Wage on household incomes is complex, being affected by the way that statutory wage increases interact with the tax and benefits systems. Analysts disagree about the effectiveness of minimum wages in tackling poverty. We held a seminar in December 1998 to examine this issue, and published the conclusions in our Occasional Paper 2; these are summarised in Appendix 3.
- 3.53 Research by Dickens (1999) shows that in-work poverty has become more widespread over the last thirty years. Thus the potential of a minimum wage to reduce poverty has grown over time, and in conjunction with other policies it should now have a more significant impact on the incomes of the working poor. In addition, there is a great deal of mobility within the labour market, and moves in and out of work mean that the National Minimum Wage will have a much wider impact than is apparent in cross-section data. Recent analysis of income dynamics shows substantial persistence of low pay over time, and strong evidence of a low pay/no pay cycle (Stewart, 1999). These findings strengthen the case for a National Minimum Wage to protect groups which have permanent disadvantage in the labour market.
- 3.54 Table 3.1 gives examples of the interaction of the minimum wage with the tax and benefits system for low-paid households with different family circumstances. In particular, it illustrates the impact on net incomes of the Working Families' Tax Credit, together with a 30 per cent rise in gross pay which is our estimate of the average gain for those directly affected by the minimum rates (see Appendix 2). The table shows a substantial impact of the National Minimum Wage on net incomes, particularly among single people working full-time and two-earner married couples. The former are not eligible for the Working Families' Tax Credit, while the married couple is

Low Pay Commission Seminar 'The National Minimum Wage, Incomes and the Low Paid'

The impact of the National Minimum Wage on household incomes is important and complex. In December 1998 we held a seminar to examine these issues, including the interaction of the National Minimum Wage with the tax and benefits system, its impact on the working poor, and pay mobility. The National Minimum Wage cannot solve all the problems of low pay and poverty. Nevertheless, it is clear to us that the minimum wage is an important instrument which, in tandem with other measures, can make a substantial difference to the household incomes of many low-paid people.

The National Minimum Wage, Incomes and the Low Paid, Low Pay Commission: Occasional Paper 2.

means-tested according to their joint income which is sufficiently high to remove entitlement to the credit. The table shows, however, that the Working Families' Tax Credit is having a substantial effect among one-earner married couples and lone parents. Where low-paid people's take-home pay is enhanced by the means-tested Working Families' Tax Credit, the National Minimum Wage has a smaller effect on household income.

Table 3.1

Impact of the National Minimum Wage on the Incomes of Low-paid Households			
	Pre-NMW net weekly income ^a with Family Credit ^c	Post-NMW net weekly income ^b with Family Credit	Post-NMW net weekly income with WFTC
	(£)	(£)	(£)
Single person aged 18	83	104	104
Married couple, 2 children, 2 earners ^d	55	71	71
Married couple, 2 children, 1 earner	201	208	232
Lone parent, 2 children	148	162	226

Notes:

- a Assumes pre-NMW gross pay of £2.75 per hour for married couples and lone parents, and £2.30 per hour for a single person. These levels illustrate the impact of a 30% rise in gross pay, which is our estimate of the average entitlement for those previously earning below the NMW in Spring 1998.
- b Assumes post-NMW gross earnings of £3.60 per hour for married couples and lone parents, and £3.00 per hour for a single person.
- c Family Credit was the main in-work benefit for low-paid working families in which the main earner works for 16 hours or more a week. It was replaced by the Working Families' Tax Credit from October 1999.
- d Specifies the income of the second earner, assuming the partner earns lower quartile male earnings of £265 per week.

Assumptions on weekly hours are that the single person and one-earner married couple work 37 hours, the married couple second earner works 20 hours, and the lone parent works 16 hours.

Source: HM Treasury

3.55 Recent reforms to the tax and benefits system complement the National Minimum Wage. A statutory pay floor cannot by itself eradicate in-work poverty. Targeted policies such as the Working Families' Tax Credit enhance the take-home pay of low-paid workers, and the reforms to the structure of taxation announced in the 1999 Budget enable low-paid workers to keep more of what they gain from statutory pay rises. Similarly, by increasing the earnings of the low paid, the minimum wage can either provide savings on the cost of Working Families' Tax Credit or, for a given cost, increase the number of beneficiaries from the Working Families' Tax Credit. The minimum wage also limits the scope for employers to depress wages and rely on tax credits to substitute for pay.

- 3.56 The Treasury's study *Tackling Poverty and Extending Opportunity* (1999a) shows that inequality is passed from one generation to the next: the children of the low paid are much more likely to become low-paid workers in the future. The National Minimum Wage and the reforms to the welfare system provide an opportunity for the children of the low paid to break out of a cycle of poverty and inequality.

Public Sector Finances

- 3.57 The National Minimum Wage has complex implications for both central and local government finances. The Government's evidence indicated the possible first-round effects on the Exchequer. The precise impact on revenues and costs depends on a number of factors, such as the scale of pay restoration, the level of compliance, and the impact on profits and jobs. More time is needed before we can fully assess the public finance flows. With a minimal impact on jobs, our assessment remains that 'the net effect on public sector finances should be relatively small and could be beneficial' (Low Pay Commission, 1998).
- 3.58 Most public-sector employees earn significantly above the National Minimum Wage, and the direct impact on public-sector pay is estimated to be small. The Government's evidence states that detailed estimates are not available, but it does estimate an increase in direct pay costs for the bulk of central and local government and the National Health Service of around £20 million in 1999–2000. This is substantially less than the estimate provided for our first report, which was based on April 1997 data and did not fully incorporate the local government agreement for a minimum £4 hourly rate in 1997.
- 3.59 While the impact on the pay of directly-employed staff is small, the minimum wage will add to public expenditure through the extra costs of goods and services purchased from the private sector. Many providers of contracted-out services – for example, social care, catering, cleaning and security – are low-paying employers. The Government evidence states that 'it is difficult to identify even approximately the impact of the minimum wage on procurement costs'. Nevertheless, it seems that the initial effects on procurement costs are small.

- 3.60 We know that certain public-sector customers for business services have agreed to small increases in fees arising from the minimum wage, though in some cases service requirements have been adjusted to keep overall costs constant. Other major customers such as the Ministry of Defence have established fixed contracts, so there is no effect until new contracts need to be negotiated. In the longer-term, however, some contract rates will inevitably rise. We are aware of considerable difficulties being caused by the refusal of some local authorities to acknowledge the National Minimum Wage in the fees they allow to their care-home contractors. In the light of inadequate funding to meet additional wage costs, certain care homes have had to reduce the quality of service they provide.
- 3.61 In our consultation for our first report, we were told of employers paying their workers a lower wage and encouraging staff to take income from in-work benefits. The National Minimum Wage limits certain employers' ability to exploit the in-work benefits system and tax credits. The increase in earnings of the low paid will reduce expenditure on tax credits, and in-work benefits such as Housing Benefit and Council Tax Benefit. Table 3.2 shows estimates of benefit savings presented in the Government evidence with total savings, including Working Families' Tax Credit, estimated at around £280 million for 1999–2000.

Table 3.2

Benefit and Credit Savings from the National Minimum Wage	
Benefit	Saving in 1999–2000 £m
Working Families' Tax Credit (from October 1999)	35
Family Credit (up to October 1999)	105
Housing Benefit	90
Council Tax Benefit	25
Jobseeker's Allowance	10
Income Support	15
Total Savings	280

Source: Government Evidence

Note: Simulations use the 1996–97 Family Resources Survey and uprate to 1999/2000 tax/benefits system.

- 3.62 The National Minimum Wage will increase the receipts from income tax and National Insurance. As the low paid spend their increased earnings, extra VAT receipts will also accrue. Any increase in labour costs may, at least initially, have lowered profits and caused a reduction in receipts from corporation tax. The Government's evidence estimates that the net impact of the minimum wage on income tax, corporation tax and National Insurance may be a small yield of £5–10 million in 1999–2000. These estimates are based on understandably cautious early assumptions about the effects of the minimum wage on corporate profitability. Our own evidence and research findings, however, suggest that these assumptions can be modified. There is ample evidence, not least from the CBI and British Chambers of Commerce, that many employers have been absorbing the increased cost of the minimum wage by improving labour productivity. We would thus expect the tax yield from the introduction of the National Minimum Wage to be considerably more than £5–10 million in 1999–2000.
- 3.63 The most important initial finding for our assessment of public sector costs is the evidence that the impact on employment has so far been minimal. Projections by the Department of Social Security put the average benefit cost of an unemployed person at £4,850 per person per year for 1999–2000. With a minimal effect on employment, additional benefit expenditure should be small in relation to the savings shown in Table 3.2.

Conclusion

- 3.64 We have assessed the impact of the National Minimum Wage nine months after its introduction. The policy has clearly brought substantial benefits to large numbers of people, especially women and part-time workers, with no indication so far of a significant adverse effect on the economy. Several years are needed before the full effects can be assessed. While there may be restructuring within the labour market, our judgment is that because the rate has been set prudently, the long-term costs are likely to be small. Even a cautious introductory rate will inevitably cause concern for certain businesses, for example where profitability is low or scope for innovation is limited. Hence the following chapter assesses the impact of the National Minimum Wage in the sectors where its effects have been concentrated.

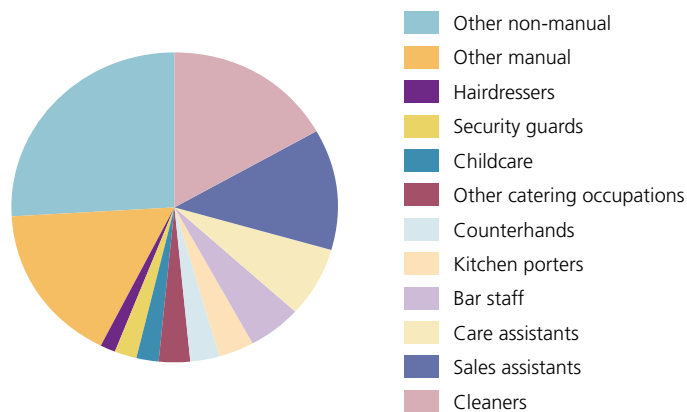
4 Managing the National Minimum Wage

Both employers and workers have adjusted well to the introduction of the minimum wage. Small businesses have been most affected, yet have successfully managed the transition. Each sector has had to adopt its own strategies to cope with the additional pay costs and, for some sectors or types of businesses within them, the adjustment has been considerable. Nevertheless, for the vast majority of employers, the transition has been successful and, consequently, most low-paid workers are receiving their full entitlement.

- 4.1 The great deal of well-informed evidence submitted to us, the research which we commissioned, and the findings of our regional visits revealed how so far businesses have managed the transition and workers have gained from the minimum wage. The overall picture is positive: most businesses have developed strategies to cope with the minimum wage, thus ensuring that workers have benefited. The National Minimum Wage has had some impact across a broad range of business sectors, but the impact has been more concentrated in the particular sectors and occupations which we identified in our first report.
- 4.2 Figure 4.1, based on the New Earnings Survey (NES), shows the occupations which make up the majority of those gaining from the minimum wage: for example, nearly 40 per cent of all those who directly gained are cleaners, sales assistants or care assistants. While the 'other manual' and 'other non-manual' categories represent well over a third of the whole, they comprise a myriad of occupations none of which individually has any significant proportion of workers affected by the minimum wage. Among the groups of low-paid workers who gained, those to benefit most are women, part-time workers and young people, some of whom have experienced significant increases in earnings.

Figure 4.1

Main Groups of Workers Whose Hourly Earnings Have Increased Following the Introduction of the National Minimum Wage



Source: NES matched sample, April 1998, 1999

- 4.3 The prudent level at which the wage was set, the 'keep it simple' approach to the definition of the wage, and the positive attitude which most employers adopted resulted in businesses generally being able to manage the National Minimum Wage. We are impressed by the manner in which most employers have handled the implementation. We are also pleased that many have identified benefits for their businesses. For example, Incomes Data Services (IDS) in its research for the Commission reported that 'one major theme park told us that the National Minimum Wage actually worked as an aid to recruitment and had helped prevent the previously habitual haemorrhage of staff to major supermarket chains paying higher rates'.
- 4.4 Both the CBI and the TUC evidence highlighted the way in which the minimum wage had been introduced and its ability to improve significantly the pay of low-paid workers without causing substantial damage to the economy or employment, as some commentators had predicted. During the lead-up to our first report, organisations representing small businesses supported the principle of the minimum wage, and this was reinforced in the latest evidence we received. For example, the Alliance of Independent Retailers stated in its evidence that

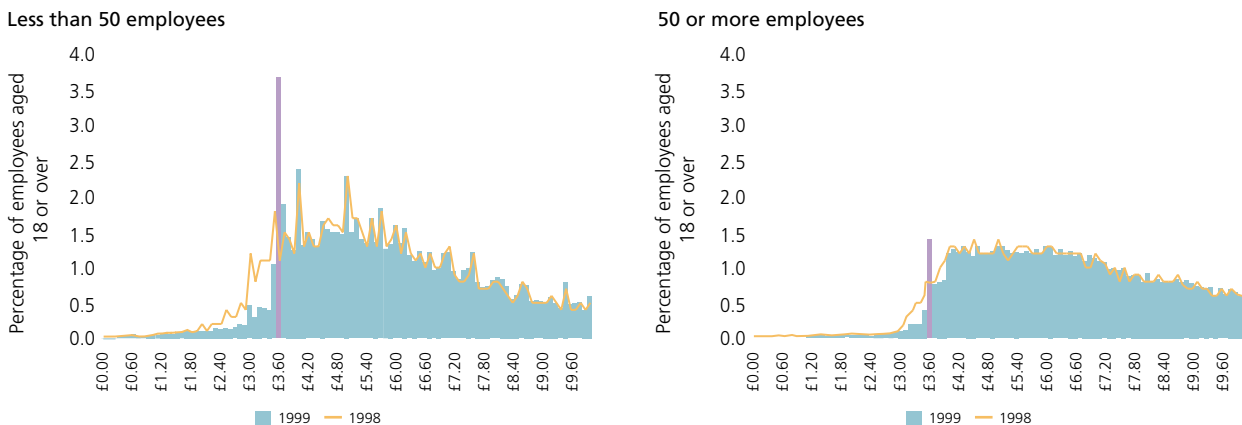
We believe that the principle of a minimum wage is simple and right. The most powerful argument is not directly one of social justice, but of practicality. It is wasteful and perverse for tax payers to subsidise bad employers who undercut rivals by paying lower wages.

Small Firms

4.5 In assessing the impact on these sectors, we were particularly concerned about the effect of the minimum wage on small businesses, from small single outlets with few workers to more substantial enterprises with tens of workers. As identified in our first report, low pay is more prevalent in smaller enterprises, and the impact of the minimum wage on business costs is therefore greater. We were also conscious that some small businesses face greater constraints in adapting to the minimum wage. As Figure 4.2 shows, the impact of the minimum wage on pay rates for businesses with fewer than 50 employees has been substantially greater than on larger firms.

Figure 4.2

Comparative Distribution of Pay Within Businesses with Fewer than Fifty Employees and those with Fifty or More Employees, 1998–1999



Source: NES, April 1998, 1999

4.6 Because of this disproportionate impact, most of the research projects we commissioned covered small businesses. We commissioned the Economic and Social Research Council's Centre for Business Research, for example, to examine the impact of the minimum wage on small and medium-sized enterprises. The survey was conducted between June and October 1999 and included responses from over 1,000 firms with less than 50 employees. It showed that a sizeable minority of firms who paid the minimum wage responded by attempting to improve their competitive performance, in particular by focusing on giving customers personal attention,

cost advantage and speed of service. Employment effects were reported in only a small minority of firms.

- 4.7 Studies by Undy et al. (1999) and Gray and Heyes (1999) in textiles and clothing manufacturing, Lucas and Langlois (1999) in retail and hospitality, and Pay and Workforce Research (1999) in social care also investigated the small firms sector, and found that small businesses had adapted well. Our own surveys included high proportions of small firms: of those businesses covered by the post-implementation survey, almost a third employed fewer than ten workers and three-quarters employed fewer than fifty workers. All studies reported that the impact of the minimum wage had been small and manageable for the vast majority of firms.
- 4.8 These findings were confirmed in the written evidence we received. A number of organisations which represented small businesses submitted evidence. Among the economy-wide organisations, the Federation of Small Businesses and British Chambers of Commerce both conducted surveys of the impact of the minimum wage. The former concluded that 'FSB members are, in the main, coping with the National Minimum Wage', while the latter commented that 'most firms have been able to afford to lower their profits to cope with the NMW'.
- 4.9 The opportunities and constraints faced by small firms differ across the sectors. In this chapter we discuss the impact of the National Minimum Wage on those low-paying sectors identified in our first report, and focus in particular on the smaller businesses in these sectors. We also consider which groups of workers have gained and what the impact has been on business, including, where appropriate, the implications for employment, business costs, prices, profitability, efficiency and productivity, and pay structures within sectors.

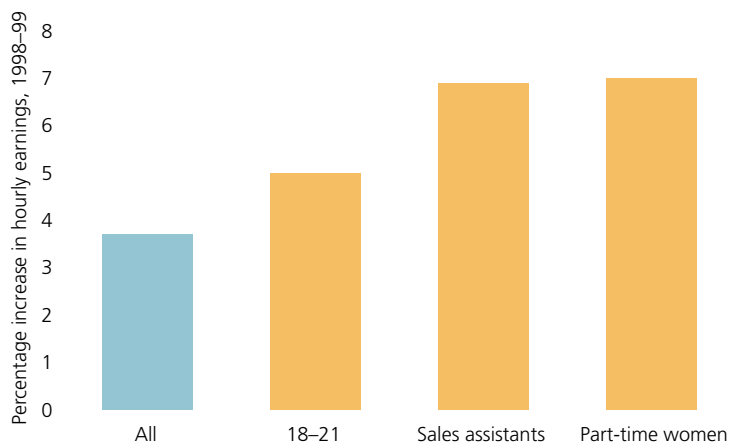
Retail

- Main gainers women, part-time workers and young people.
- Large firms well prepared.
- Small firms facing competitive pressures and price sensitivity.

4.10 The retail sector has the largest number of workers affected by the introduction of the National Minimum Wage. A significant proportion of women, young people and part-time workers are employed in the sector. Figure 4.3 shows how the hourly earnings of part-time workers, especially women and young people, have grown substantially more than the average for the sector. But it also shows a greater concentration of earnings growth in the sales assistant grades, indicating that there has been no widespread action to maintain differentials.

Figure 4.3

Average Hourly Earnings Growth in Retail, 1998–1999



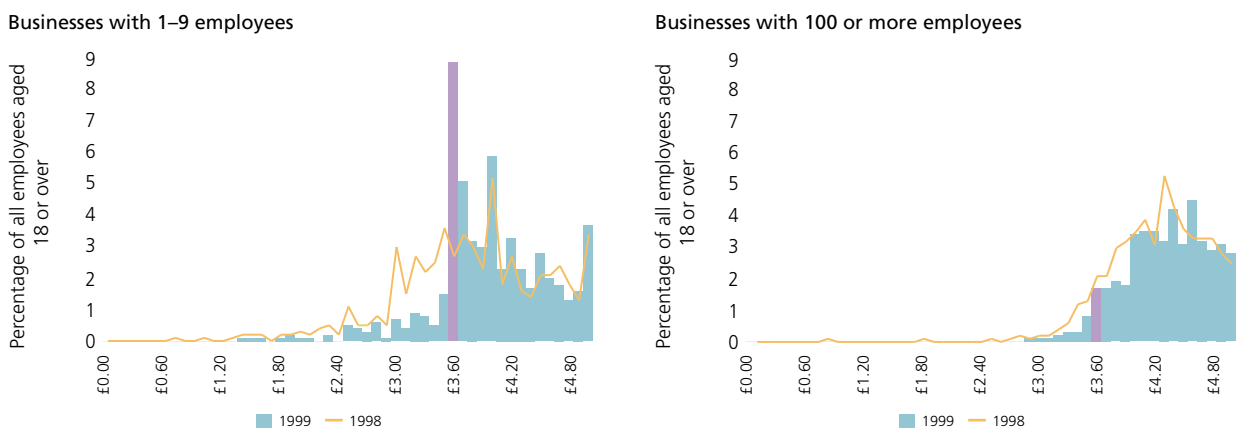
Source: NES, April 1998, 1999

- 4.11 Employment in retail does not appear to have been adversely affected by the minimum wage. In line with the buoyancy of the service sector overall, it continues to grow: for example, the ONS Employee Jobs Series shows a 1 per cent increase over the year to June 1999.
- 4.12 There is a pronounced pattern to low pay in the sector. Larger firms and retail chains tended to pay close to, or above, the

National Minimum Wage prior to April 1999, so adjustment for them has been limited. Very low pay is more concentrated in small businesses where a range of factors, not least strong competition from major retailers, has for many years affected viability and therefore influenced pay levels. Our post-implementation survey which attracted nearly two hundred responses from retail employers, mainly in small businesses, showed that nearly a half had experienced wage bill rises of 5–10 per cent. But increases had been confined to lower-paid workers: nearly two-thirds had not taken any action to restore differentials. Figure 4.4, based on NES data, clearly demonstrates the substantial impact of the minimum wage in small retail firms compared with that in companies with more than a hundred workers.

Figure 4.4

Earnings in Small and Large Firms in the Retail Sector



Source: NES, April 1998, 1999

- 4.13 For these smaller companies, the minimum wage increased business pressures. Nevertheless, the trade association representing many small retail businesses suggested that ‘when introduced, the minimum wage was perceived to be set at a “fair” level with conditions sensitive to the small store sector’ (Retail Trade Alliance (RTA) Evidence).
- 4.14 Trade associations also suggested that much of the sector was well prepared for the minimum wage, with many companies making provision to alter employment practices and wage rates in advance of implementation. The RTA found that in

December 1998, 60 per cent of businesses had no workers below the minimum rate. This finding was supported by our December 1998 business survey, which elicited over six hundred responses from the retail sector. Just under half expected the minimum wage to have no impact on their business. Where wages had to be increased, the impact was frequently managed by introducing measures to improve productivity, but also by increasing employment of part-time staff and young people where this was feasible. The Association of Convenience Stores suggested in its evidence, however, that the scope for such adjustment is limited for operators of single outlets: 'the opportunity to absorb extra costs by way of reducing total employee numbers or hours is also unrealistic due to the small number of staff employed'.

One company operated three retail brands: high street discount tobacconist/ confectioners, newsagents – which were in long-term decline – and convenience stores, which was a rapidly growing sector. The discount stores and newsagents were marginally less profitable as a consequence of the minimum wage, though none had yet closed as a direct result of it. But the company took case-by-case decisions whether to replace full-time staff with part-timers. The minimum wage had caused no major difficulties for the convenience stores.

Low Pay Commission Visit to the South West

- 4.15 We commissioned research on the impact of the minimum wage on employment practices in the retail and hospitality sectors (Lucas and Langlois, 1999b). It found that there had been minimal, if any, action by retailers to cut staff costs by employing greater numbers of workers on the young persons' Development Rate, or by increased use of exempt groups such as family members, apprentices or participants on government-funded training. Our post-implementation business survey showed that 90 per cent of firms had suffered a reduction in profits and in 50 per cent of cases this reduction had been significant. Many companies had sought to offset the impact by changing the way in which work was organised (64 per cent of firms), or to tighten control of labour costs (69 per cent).
- 4.16 While the minimum wage has had little, if any, significant impact on major retailers, the British Retail Consortium, which represents mainly larger firms, indicated that the ease of implementation had been assisted by prevailing business conditions such as the buoyant state of the labour market and low inflationary expectations. The minimum wage proved more of a challenge for smaller companies for which price sensitivity and strong competition from large companies restricted the scope for offsetting the impact by price increases. Overall, significant proportions of low-paid workers in the sector have gained from better than average increases in hourly earnings and there is no evidence of widespread business closures or job losses.

Hospitality

- Main gainers women, young people.
- Small firms more affected.
- Major adjustment of pay structures in some subsectors.

- 4.17 The hospitality sector is diverse, ranging from hotels and guest houses to contract catering and leisure facilities. For the purposes of this report, we concentrate mainly on hotels, restaurants, bars and catering, where the bulk of low-paid workers in the sector are employed. After retail, hospitality is the sector with most workers affected by the minimum wage, and the employment characteristics of the sector are similar to those of retail.
- 4.18 Employment has grown over recent years and this trend is forecast to continue. The current profile of the sector includes high proportions of female, young and part-time workers, and all of these groups have experienced substantial earnings growth from the minimum wage. Hourly earnings for female workers and 18–21 year olds have increased by just over 6 per cent and 8 per cent respectively, compared with an average of 4 per cent for the sector. But the most significant increases, between 8 and 9 per cent, were concentrated in the lowest grades, such as catering assistants and kitchen porters, demonstrating some narrowing of differentials.
- 4.19 A survey of members of the British Hospitality Association (BHA) indicated that the impact of the minimum wage has been limited in the hotel and catering industry: nearly three-quarters reported no effect on their business. The impact has generally been greater on small firms, although some leading hospitality companies also had to increase their base rates, particularly where they operated induction rates. For example, Whitbread Inns increased both its induction and base rates to £3.60 from £3.25 and £3.50 respectively (IDS, 1999b). But the impact has not been spread evenly across subsectors. Figure 4.5 shows that a quarter of workers in bars are now earning the minimum wage compared with around 10 per cent in hotels, restaurants and canteens. But each chart shows a significant spike at the level of the minimum wage, as in each subsector the proportion of workers earning £3.60 has doubled since April 1998.

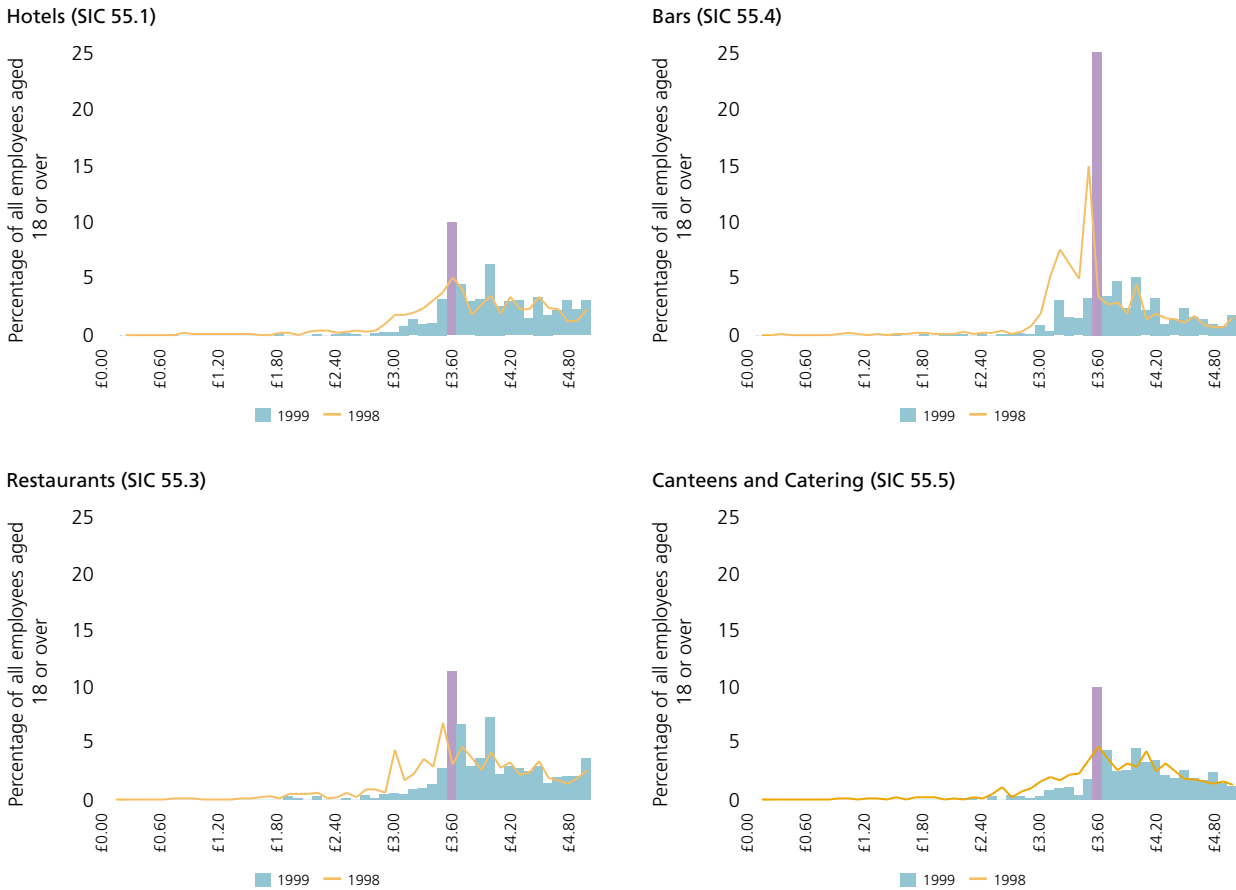
Low Pay Commission Research

We commissioned Rosemary Lucas and Michele Langlois of the Manchester Metropolitan University to undertake qualitative research examining preparation in the Autumn of 1998 for the minimum wage among a sample of thirty businesses in the hospitality and clothing manufacturing sectors. The project was a follow-up to research undertaken in 1997. Hospitality firms were generally smaller and expected the minimum wage to have little impact on their wage costs as the amount of the increase was relatively low and it covered few workers. The impact was expected to be greater on the wage costs of clothing firms, because they employed larger numbers of workers. But they were better prepared than hospitality firms to manage implementation. In a small number of companies the minimum wage was expected to affect piecework systems.

R. Lucas and M. Langlois, 1999.
Planning for the National Minimum Wage: Case Study Evidence from Firms in the Hospitality and Clothing Industries.

Figure 4.5

Earnings in Subsectors of the Hospitality Sector



Source: NES, April 1998, 1999

4.20 The BHA survey shows some regionality in the degree of impact: only 12 per cent of businesses in London and the South East were affected compared with 27–38 per cent in other regions. The wage bill increase has been reported by the BHA and Brewers and Licensed Retailers Association (BLRA) as averaging 5.5 per cent and 6 per cent respectively. But these organisations tend to represent the larger employers who are likely to be affected less by the National Minimum Wage. For some firms the increase was more substantial. The business survey which we conducted in September–October 1999 showed that while the wage bill for a third of hospitality firms had increased in the range 5–10 per cent, for a tenth of firms it had increased by more than 10 per cent.

- 4.21 Within specific subsectors, the wage bill increase has been more substantial. The British Activity Holiday Association (BAHA) reported wage costs increasing by between 25 and 125 per cent. This reflected a major change in pay structures from a system of full board and lodging plus pocket money, but also included some restoration of differentials. The BAHA has suggested that its members will have to raise prices by about 10–15 per cent in 2000. And it is still expecting reductions of 10–25 per cent in profitability.
- 4.22 Despite these pressures, overall the minimum wage has been positively accepted in the hospitality sector. The evidence of Tourism South and West Wales echoed sentiments expressed by a number of employers who responded to our own survey of the sector: ‘the introduction of the NMW has ensured that we can lay the low wage ghost which has haunted careers in tourism and hospitality for so long’.
- 4.23 Firms have used a variety of means to ameliorate the effects on the wage bill. In the BHA survey, more than half of those members affected by the minimum wage intended to respond by controlling labour costs and reorganising work. About 18 per cent intended to reduce working hours or staff numbers, while only 12 per cent expected to increase prices. Some businesses planned a range of measures; for example, a pub landlord in Oxfordshire quoted by Lucas and Langlois (1999a) stated that he would seek to increase his turnover to compensate:

I wouldn't get away with increasing the product price. I may have to take a cut in profits and I will try and improve recruitment and staff retention. Other than that, I suppose [that I would] train staff to be more multi-skilled.

- 4.24 Some companies coped by revising their pay structures. The BLRA reported some movement to convert benefits-in-kind into consolidated cash payments, while some companies introduced a service charge which can be consolidated into the minimum wage, or revised payment structures for overtime. For example, Bass plc stated in its evidence that

A positive impact was the decision to introduce more formalised pay structures in order to improve our control of wage drift and to ensure compliance whilst taking advantage of the accredited training route. Direct impact was a reduction in the application of overtime payments.

An activity holiday centre has seen its wage bill increase from 27 per cent to 60 per cent of total costs. Since April, an accommodation charge of £19.95 has been deducted and there is a voluntary agreement with live-in staff for a charge for meals. For consistency, live-out staff are also charged for meals, which had previously been provided free. Holiday prices for 2000 are to be increased by 10 per cent, rising to 12 per cent for the peak summer period. But the owners are concerned that higher charges may affect trade and opportunities for poorer children from inner-city state schools.

Low Pay Commission Visit to South West

4.25 As we discuss in Chapter 5, the level and scope of the accommodation deductor is an issue for certain types of hospitality establishment, though some businesses have offset the increased costs by introducing meal charges. While the impact of the National Minimum Wage has been more pronounced in smaller hospitality firms and some specialised sub-sectors, for the most part it has been managed effectively, possibly because of the greater scope in the sector for offsetting cost increases by restructuring work or increasing prices.

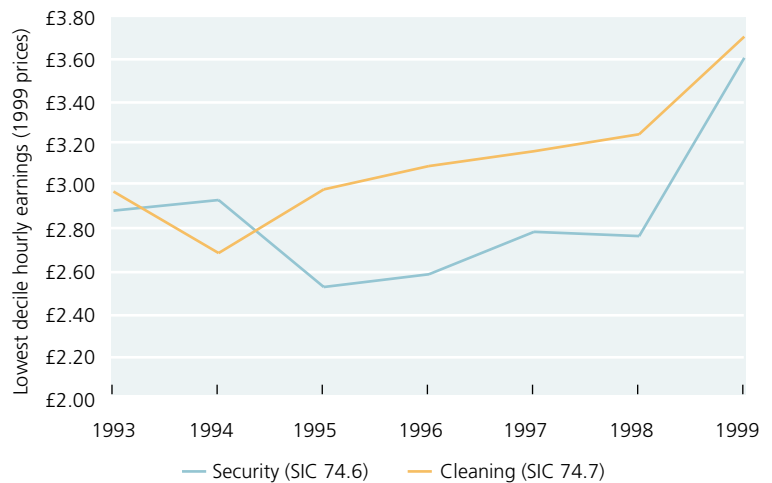
Cleaning and Security

- Main gainers female part-time workers in cleaning, men in security.
- Greater impact on smaller employers.
- Difficulties experienced in raising some contract prices.

4.26 In cleaning, the workforce predominantly comprises female and part-time workers. In contrast, security employs mainly male workers on a full-time basis. Wage levels in both sectors, but especially cleaning, have traditionally been very low. Figure 4.6 shows significant upward shifts in earnings which the minimum wage has brought about for workers in the lowest decile in each sector. In cleaning, lowest decile earnings increased by a third.

Figure 4.6

Lowest Decile Earnings in Cleaning and Security



Source: NES, April 1993 to 1999 (1999 prices)

- 4.27 Earnings for workers in security also rose significantly. The lowest decile earnings increase was 16 per cent. But further analysis of the data shows that the significant increase in the numbers of workers at £3.60 was accompanied by a slight drop at wage rates just above that rate. This may have been due, as some written evidence suggested, to some consolidation of allowances and premia to offset increases in basic pay.
- 4.28 Evidence from our visits and research indicated that for many firms the impact on wage costs in the industry has been substantial. Almost half of the twenty-six cleaning and security firms included in the post-implementation stage of our business survey reported increased wage costs of at least 5 per cent. Increases have affected leading companies, such as Office Cleaning Services, as well as smaller firms. Nevertheless, the introduction of the minimum wage has been welcomed by many employers and by workers' representatives. The Business Services Association (BSA) said in its evidence that 'we still strongly support the introduction of the NMW which has clearly levelled the playing field and eliminated low wage contractors to the benefit of employees and good companies'. And, as the TGWU pointed out in its evidence,

The introduction of the National Minimum Wage has had a positive effect on business and competitiveness. In the contract cleaning industry, for example, one officer reported that the National Minimum Wage has protected employment and encouraged companies to tender for contracts on the basis of the service they can provide rather than how little they pay their staff.

- 4.29 But the minimum wage has caused some transitional difficulties. The major trade associations – the Business Services Association and the Cleaning and Support Services Association (CSSA) – reported that their members have been able to increase fees to many customers, but 'in most instances where costs have been able to be passed on it has only been for a proportion of the total' (BSA Evidence).
- 4.30 Alternatively, customers have reviewed their requirements. The CSSA explained in its evidence that the need to minimise increased charges involved, 'changes to specifications and frequencies of service to avoid customers having large

A contract cleaning and security company experienced a range of difficulties. Some customers were unwilling to contract for a higher fee which anticipated the minimum wage; a number of larger organisations moved services in-house. In addition, the minimum wage had increased the wage bill by 8–10 per cent and it would take the firm two years to recoup this. In the meantime, long-term plans for training, capital investment and quality improvement were on hold. The employer recognised, however, that 'the bottom line is the customers; they've had these services too cheaply for too long'.

Low Pay Commission Visit to Scotland

increases in costs'. Consequently, some firms have reduced working hours, which may have resulted in workers being no better off as a result of the minimum wage. Research by the ESRC Centre for Business Research (Hughes et al., 1999) showed that two-fifths of cleaning and security firms in its survey had some workers paid at the minimum wage. It found that in cleaning and security, the firms with the highest proportion of workers paid at the level of the minimum wage were doing most to increase their efforts in the product market, for example, by increasing emphasis on service delivery or design.

- 4.31 Companies' ability to increase prices has been influenced by the purchasing power of major customers. Both the BSA and the CSSA highlighted the difficulties experienced with some public service contracts, most notably fixed-term, fixed-price contracts established with the Ministry of Defence. When these contracts were agreed, the Ministry precluded any clause allowing fees to be increased in response to changes in employment legislation. It subsequently refused to renegotiate the fees to take account of the effects of the Working Time Regulations and National Minimum Wage on contractors' wage costs. Those companies affected have therefore had to absorb the additional costs.
- 4.32 But this should be a transitional difficulty. Companies are likely to build the cost of the National Minimum Wage into contracts as they are renewed. Also, the business services industry and the Ministry of Defence have recently negotiated a set of new principles which will be adopted for future contracts between these parties to avoid the recent difficulties.
- 4.33 The introduction of the minimum wage in the cleaning and security industry has not been without some difficulties, but these have been well managed. There have been some initial problems with contracts but, in the longer term, improvements in wage rates should lead to improved recruitment and retention and better-quality service. On our visit to South Wales, we were told by GRW Security Services that clients had started to recognise the link between better pay and improvements in service:

Clients are accepting increases in rates for our services because they understand that increases in wage costs as a result of the National Minimum Wage would also mean an improvement in the standards of service. With a level playing field, clients will opt for the best standards available for the money they pay. In the security sector, improved levels of service will reduce insurance costs for companies, with the introduction of increased technology such as computerised monitoring of security visits. We welcome the sympathetic and supportive response from private sector clients which helped us manage the introduction of the minimum wage.

Social Care

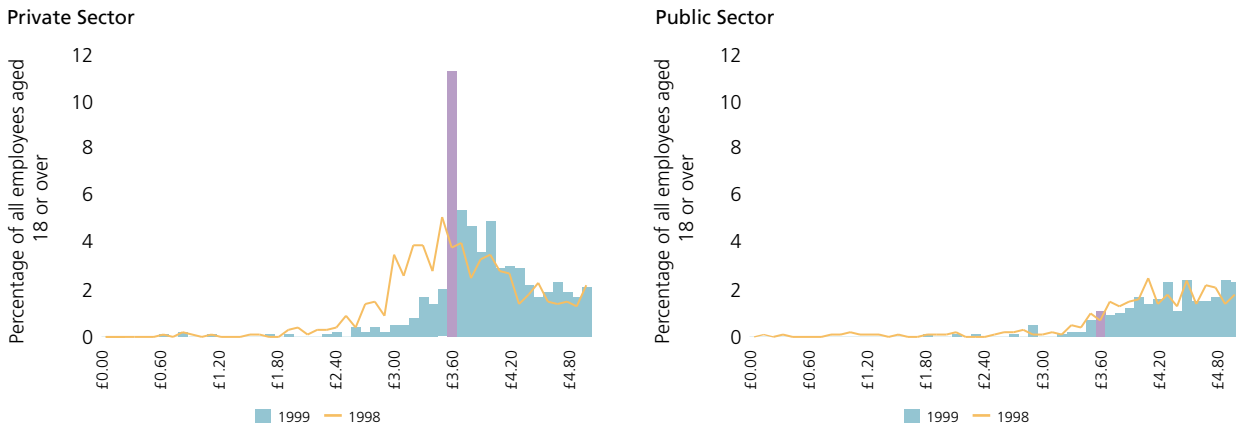
- Main gainers women.
- Greatest impact on private-sector provision.
- Concern about level of public funding of fees.

4.34 The sector comprises three main subsectors: privately-run care homes, voluntary care and local authority care. Commonly, workers in the public and voluntary sectors are better paid, although even in these sectors there are pockets of low pay. As UNISON highlighted in its evidence, ‘the introduction of the minimum wage had some beneficial effect on pay amongst staff on locally determined pay rates (in NHS Trusts) and those working for contractors. For example, the company ISS agreed to raise rates of staff earning below £3.60 to the minimum wage, without clawing back the increase from this year’s pay increase. Trusts increased the pay of many health care assistants in order to comply with the legislation’.

4.35 Generally, the privately-owned care sector has been most affected by the National Minimum Wage, particularly where the care homes are under contract to the local or health authority. This is clearly demonstrated by Figure 4.7 (overleaf) which compares earnings levels in private and public sector care. The proportion of workers earning £3.60 in private care homes has more than doubled, while the effect in the public sector is negligible.

Figure 4.7

Hourly Earnings in Private and Public Sector Social Care (SIC 85.31)



Source: NES, April 1998, 1999

For one large residential and nursing care company, the minimum wage had added £1 million or 2.5 per cent to staff costs. The impact on workers had varied between areas. Before April 1999, the basic rate of pay for their homes in Birmingham had been £3.60. In Alloa it had been £3.36 – and other local companies were said to have paid as little as £3.00.

Low Pay Commission Visit to Scotland

- 4.36 Over-provision in the sector has put some smaller homes, especially those with high capital debts, under significant pressure, and the minimum wage will have been an additional factor affecting their viability. This over-provision has started to lead to contraction in the sector. Employment figures show a drop of 2.5 per cent in residential care over the year to March 1999.
- 4.37 Earnings growth has been more concentrated among care assistants, who comprise the bulk of female employees in the sector. Their increases have been about 7 per cent compared with an average of less than 4 per cent for the sector overall. These findings are supported by the research undertaken by Pay and Workforce Research (PWR), which showed that where rates had been increased to comply with the minimum wage, the main beneficiaries were care assistants and domestic assistants.
- 4.38 Written evidence from proprietors of individual small care homes indicated that wage bill increases varied between 8 and 40 per cent, although this was not entirely due to the minimum wage. Market forces are driving up nurses' pay substantially and this is an important element in the pay costs of those employing qualified staff.
- 4.39 The research by PWR showed that just over 40 per cent of residential and nursing homes had to raise some rates to

comply with the minimum wage. Some adjustments had been made prior to April 1999, with increases ranging from less than 1 per cent to 80 per cent, but again levels were influenced by a range of factors. For example, nearly 15 per cent of respondents said the Working Time Regulations had more impact on their business than the National Minimum Wage.

- 4.40 Most businesses appear to have managed the pay increases, though not without some difficulty. Private care homes which provide contracted services to local and health authorities have limited ability to raise prices as they are constrained by the level of fees which the authorities will meet. This has had knock-on effects on pay settlements. Evidence from our consultation and visits indicated that owners had concentrated on raising the pay of the lowest paid with limited impact on differentials. A residential care home owner in Mablethorpe commented in written evidence that the wages of ‘other staff were increased by a token gesture only. ... Our nurses are paid £7.20, previously £7.00 an hour and a cleaner now £3.60, previously £3.00 an hour’.
- 4.41 Most firms have adopted tighter controls on working practices and on non-pay items, though some have made reductions in staffing and hours. The PWR research reported firms reducing some services to clients, but also provided examples of activities, like dishwashing, having been mechanised.
- 4.42 The adequacy of local authority fees is the main issue for this sector. Although the minimum wage was a factor in the financial settlement under the Government’s Comprehensive Spending Review, authorities have not necessarily adjusted care fees accordingly. A residential care group in Scotland, which dealt with eighty local authorities, reported that only five or six gave grants above the standard inflation increase (2.5 per cent) to meet the additional costs of the minimum wage. PWR reported that overall costs have increased by 5–10 per cent while funding increased by only 2.1 per cent. Comments from two care home owners in the evidence from the Lincolnshire Association of Care Home Owners illustrated the impact of the minimum wage on staff costs and the limited amount by which fees had been increased:

Low Pay Commission Research

We commissioned Pay and Workforce Research to study the impact of the National Minimum Wage in the independent healthcare sector. Its findings, based on responses from 415 organisations, were that increases in pay to comply with the minimum wage averaged from 8 per cent to 14 per cent according to the type of organisation.

Pay and Workforce Research, 1999.
Monitoring the Effects of the Minimum Wage in Independent Healthcare.

Since the minimum wage was introduced, our wages bill has increased by £3,000 per month. ... The increase of fees dictated by Social Services accounts for only £1,500 per month, so on top of other escalating costs, we are £18,000 [a year] out of pocket.

I was so annoyed at the paltry sum by which our fees were increased that I tore up all of the figurework that I had done on the minimum wage ... as being a useless exercise.

- 4.43 Anecdotal evidence suggests that some authorities are seeking to exploit over-provision in the market, with some companies accepting low fees to remain in business. But this approach is not sustainable and we are concerned about the longer-term impact. The funding of residential care is an important issue to be addressed by the Government to ensure both quality care for those who need it and an adequate level of remuneration for workers in the sector. **We recommend that the Government should ensure that adequate funding is made available to meet the additional costs caused by the introduction of the National Minimum Wage in social care.**

Childcare

- Main gainers women, part-time workers, young workers.
 - Greater impact on small playgroups.
 - Small playgroups under other financial pressures, such as competition from schools for funding.
- 4.44 Childcare includes both pre-school/early education and daycare. It employs substantial numbers of part-time, female workers, but also many young people as nursery nurses.
- 4.45 We met the Daycare Trust and Pre-school Learning Alliance (PLA) which highlighted the degree of low pay in the sector. The PLA, for example, suggested that 40 per cent of pre-school staff had been earning below, and that 10 per cent of playgroup leaders had been at or below, £3.60 before April 1999. The NES shows that the National Minimum Wage has had a significant impact on wages in childcare and similar occupations: the lowest decile earnings increased by 10 per

cent. Increases were almost double for young workers aged 18–21 years: 18 per cent compared with 9 per cent overall.

- 4.46 Commonly, the strategy to manage the wage bill increase has been to raise prices. One group of private nurseries reported that the introduction of the minimum wage had caused a knock-on effect on wages in some areas of its business and that, as a consequence, it had raised childcare prices by 18.5 per cent, resulting in some parents having to withdraw their children because of the additional costs. The company also planned to reduce sick pay to the statutory minimum to help absorb National Minimum Wage costs.
- 4.47 Evidence suggests that the National Minimum Wage could, potentially, have an impact on training in the sector. We were told that the narrowing of already tight differentials may discourage assistants from training to become leaders. But training opportunities may also be cut by employers seeking to offset employment costs. One employer told us that as a result of the Government's decision to restrict the exemption for apprentices to only one year, he would stop taking new trainees from March 2000. Instead, he would seek to employ only those who were already qualified.
- 4.48 The Daycare Trust was concerned that profit margins were very tight for smaller private nurseries and that the impact of the minimum wage would put further financial pressure on the sector. This view was echoed by the PLA which told us that some playgroups are facing closure due to a range of factors, including the additional costs imposed by the minimum wage and Working Time Regulations. The Children Act defines the ratios of staff to children, thus restricting opportunities to cut costs by reducing staffing. In areas where unemployment is high and parents' earnings are low, there are limited opportunities to raise prices. Furthermore, the government subsidy of £500 per child for pre-school learning for four year olds has created competition with schools for children of this age. The Childcare Tax Credit element of Working Families' Tax Credit will assist funding, but there is some concern in the sector that many childcare users do not qualify: for example, those working less than the minimum requirement of 16 hours a week.

A small playgroup in Somerset had to increase the pay of the nursery assistant by £2.00 an hour to comply with the minimum wage. The wages of other staff had been increased, although differentials had been squeezed. Fees had been increased from £2.50 to £2.80 for each 3½ hour session, but this had not fully met the increased costs, so the playgroup had to increase its fund-raising activities.

Low Pay Commission Visit to the South West

Low Pay Commission Research

We commissioned Alex Gray and Jason Heyes of Leeds University to undertake a research project examining the impact of the minimum wage on businesses and workers in the textiles and clothing industries in West Yorkshire. The results were based on responses from 168 firms and 213 workers, including 91 homeworkers. It found that while 35 per cent of firms had increased the wages of some employees to comply with the minimum wage, increases were more in evidence among clothing firms than in textile manufacturers. A quarter of all employees surveyed had gained, mainly women.

A. Gray and J. Heyes, 1999.
The Impact of the National Minimum Wage on the West Yorkshire Textiles Industry.

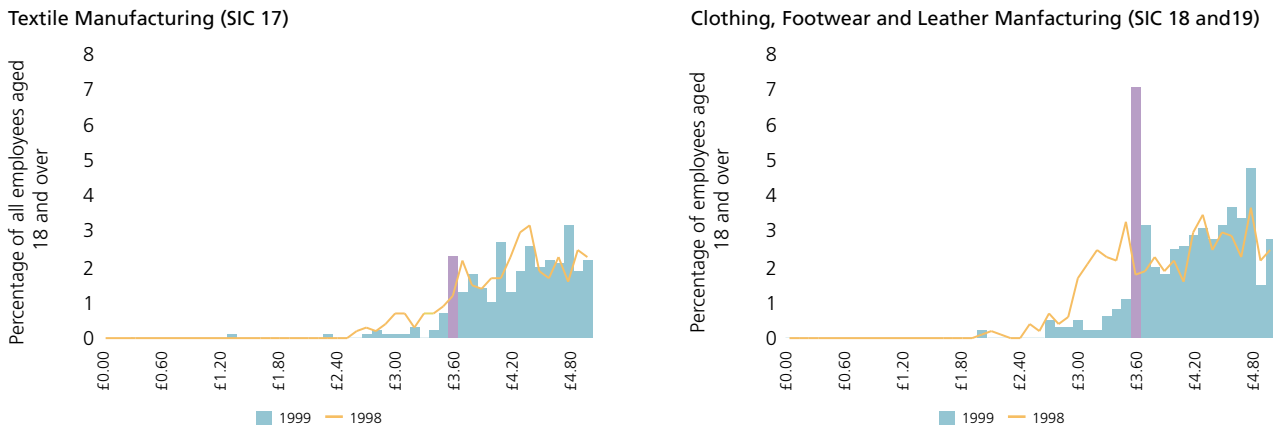
4.49 The minimum wage has put pressure on wage costs for the sector, but most groups are managing to comply. While the viability of some of the smaller playgroups has been affected, there is no evidence that this has been brought about by the impact of the minimum wage alone.

Clothing, Footwear and Leather

- Main gainers women, homeworkers, ethnic minorities.
 - Large companies well prepared, small businesses less so.
 - International competitive pressures in the sector.
- 4.50 Within the overall clothing and textile industry, the impact of the minimum wage has been concentrated in clothing, footwear and leather manufacturing where low pay has been more prevalent. This is illustrated by Figure 4.8 (opposite) which shows the relatively minor impact on earnings in textile manufacture compared with a significant shift towards the minimum wage in clothing, footwear and leather.
- 4.51 The overall impact of the minimum wage on these sectors is difficult to separate from other longer-term business pressures, such as strong international competition, particularly from developing countries where labour costs are much lower. Competition on prices has led to a trend for UK firms to move production overseas, and employment in the sector has fallen significantly in the last thirty years. Some demand remains for home production, especially where retailers require rapid response times, and the clothing, footwear and leather subsectors of the clothing and textile industry currently employ some 150,000 people in the UK, predominantly female workers in full-time jobs.
- 4.52 Detailed analysis of NES data shows that women gained substantially from the National Minimum Wage: the lowest decile for female full-time workers increased by 11 per cent. The equivalent increase for part-time workers was 15 per cent. Large increases were confined to the manufacturing grades, thus squeezing differentials.
- 4.53 In general, the sectors have been able to accommodate the minimum wage within their existing industry and company collective agreements. According to IDS (1999a), in many firms

Figure 4.8

Comparison of Hourly Earnings in Textiles with Clothing, Footwear and Leather



Source: NES, April 1998, 1999

covered by these agreements, there was a phased increase in minimum pay rates prior to the introduction of the minimum wage so that the cost was spread. Much of the spike at £3.60 shown in Figure 4.8 is likely to be attributable to smaller, and probably non-unionised, companies making adjustments to their pay rates.

4.54 Discussions with the leading trade associations led Undy et al. (1999) to conclude that a level of £3.60 would have little impact outside ‘small unorganised firms’. They identified, however, that the minimum wage had a greater impact on the clothing industry in Northern Ireland than in other regions. The two-stage research by Lucas and Langlois (1999a), which examined preparations for the minimum wage among clothing firms, found that far fewer firms were concerned about the impact of the minimum wage in Autumn 1998 than in 1997, though part of this reduction may have been due to the certainty about the level of the minimum wage by Autumn 1998. As the Leather Producers’ Association reported in its evidence,

The levels of the National Minimum Wage did not cause concern, having been pitched at manageable levels. There was a reasonable amount of time and warning before the NMW took effect; this gave employers the opportunity to examine their pay structures.

For one firm the additional wage cost is less than 2 per cent. The company sells all its output to one purchaser which is seeking to enter new markets and will not countenance a price increase due to the minimum wage. The firm is under contract to supply a certain quantity of goods this year and it has no scope for cutting jobs or reducing hours. Therefore, it has accepted a lower profit margin, but it expects to be able to increase its product prices when its contract is reviewed in early 2000.

Equality Commission for Northern Ireland
Evidence

Low Pay Commission Research

We commissioned Roger Undy, Ian Kessler, and Marc Thompson of the Oxford Institute for Employee Relations, Templeton College, Oxford to conduct a study of the impact of the minimum wage on pay structures in the clothing, knitwear and footwear industries. The research was based on interviews conducted in 66 companies ranging from individual businesses to members of multinational groups, as well as with three employers' associations and the two main unions in the sector. It found that the National Minimum Wage had a significant direct effect on pay and employment in only a limited number of companies. Many had only a few employees earning below the minimum wage because earnings under incentive-based pay systems, which are widespread in the industries, frequently exceeded £3.60 an hour. Indirectly, however, the National Minimum Wage had a disincentive effect on some workers earning towards the lower end of piecework earnings.

R. Undy, I. Kessler and M. Thompson, Oxford Institute for Employee Relations, Templeton College, University of Oxford, 1999. *The Impact of the National Minimum Wage on the Clothing, Knitwear and Footwear Industries.*

- 4.55 In contrast, the evidence from the British Apparel and Textile Confederation claimed that 'there can be no doubt [that the minimum wage] has been a contributory factor to the very significant loss of jobs in the clothing and textile industry over the last year. It has, moreover, accelerated the trend of manufacturers moving production offshore'.
- 4.56 Some firms report that the requirement to pay poor performers the minimum wage has reduced the incentive and thus the productivity of higher-paid workers. Most employers are dealing with this by improving performance management including re-training poor performers. In some cases, tighter performance targets have improved productivity for the companies concerned. Such measures to offset wage costs by increasing productivity are important, especially for smaller firms, given the limited scope to increase prices in the face of strong international competition. Employers within the sector can also face strong competition for labour. The research by Gray and Heyes (1999) and Undy et al. (1999) found that some employers are struggling to recruit and retain workers where there is local competition for labour from higher-paying retail firms and other high street employers.
- 4.57 The clothing and textiles sector employs large numbers of homeworkers, particularly from ethnic minority backgrounds. Homeworkers have traditionally been among the lowest-paid workers. Non-compliance remains the major concern for this group, which by its nature is more vulnerable to exploitation. We discuss this issue in more detail in Chapter 7.
- 4.58 Within the clothing, footwear and leather sector, the impact of the National Minimum Wage has been more limited than some commentators had previously feared. Few companies have had significant increases in their wage costs as the incentive-based pay structures which commonly exist in the sector already allowed many workers to earn at least the minimum wage at the prudent level we recommended. Where there has been an impact from the minimum wage, businesses are looking to improve staff management and performance rather than resort to price increases given the fierce international competition. The general view remains that international competition remains the greatest threat to employment.

Horticulture

- Main gainers casual workers.
- Smaller growers most affected.
- International competitive pressures on sector.

- 4.59 Horticulture is another industry facing strong and increasing international competition. Employment is predominantly casual and subject to seasonal peaks, with local labour often supplemented by foreign workers.
- 4.60 The implementation of the National Minimum Wage overlaid the setting of agricultural wages by the Agricultural Wages Boards for England and Wales, Scotland and Northern Ireland, and the current quinquennial review of the Agricultural Wages Boards will consider the need for a continuing additional mechanism for setting agricultural wages. Most permanent workers in horticulture, and in agriculture more widely, were already paid above the National Minimum Wage under the Agricultural Wages Orders. The minimum wage increased the casual rate by 12 per cent from the previous Agricultural Wages Order minimum of £3.21, although the Agricultural Wages Board for England and Wales subsequently increased this further from £3.60 to £3.69.
- 4.61 The businesses most affected by the National Minimum Wage are those which employ large numbers of casual workers. For example, we were told on our visit to the South West that there may be some problems for daffodil growers, while the National Farmers Union of Scotland highlighted that the most significant impact had been felt in the soft fruit sector, where wage increases of 15–20 per cent had been reported.
- 4.62 The minimum wage has had some impact on working practices and record keeping in the sector, particularly where workers are paid on a piecework basis. Some employers suggested that the convergence of the legal minimum and the potential maximum wage could reduce the incentive effect of piecework, especially for less productive workers, leading to decreased productivity and increased costs. But employers are limited in their ability to raise prices because of the purchasing power of major retailers and strong competition from imports. Therefore, improving efficiency and productivity are the major ways in which employers are coping. There is no evidence of any significant adverse impact on the sector.

We met a number of horticultural producers in Worcester. They all employed casual labour and were concerned about the 15 per cent increase in the basic rate for casual workers. But of equal concern was the administrative burden of the National Minimum Wage and wage-related costs like increased National Insurance Contributions. None reported any significant impact from the minimum wage on the viability of their businesses.

Low Pay Commission Visit to the West Midlands

Hairdressing

- Main gainers women, part-time workers, young trainees.
- Some potential negative impact on training and employment of young people.

- 4.63 Over 80 per cent of workers in hairdressing are female, many of whom work part-time. The sector also relies heavily on the employment of young workers (16–18 year olds) undergoing training on very low wages – often fixed at the level of the National Insurance Contribution threshold. Consequently, the minimum wage has had a significant effect on the pay of the lowest-paid workers.
- 4.64 The National Hairdressers’ Federation (NHF) and the Hairdressing Employers Association (HEA) have pointed out that it is difficult to separate the impact of the National Minimum Wage from other changes. They estimate, for instance, that the average wage bill increase arising from the minimum wage is 2 per cent compared with 2½–3 per cent for the Working Time Regulations. Both the NES and the trade associations’ survey show pay increases in excess of 20 per cent for workers in the lowest quartile of the sector. In the associations’ survey, the most common reported wage for this group increased from £2.11 an hour in 1998 to £3.03 in 1999, a 43 per cent increase.
- 4.65 For some employers, especially those who employ large numbers of young workers and trainees, the minimum wage has caused a transitional shock. Many have responded by increasing prices. The NHF/HEA evidence shows that more than half have raised prices in the region by 3–5 per cent, but nearly a tenth by 10 per cent. Such increases have been manageable: official Retail Price Index figures show hairdressing price increases are consistently around 6 per cent a year. But the scope for raising prices varies considerably according to the type of business or location.
- 4.66 There is also evidence of changes in working patterns to reduce costs. Some salons are employing fewer staff for single days in favour of those who can work for several days or a full week.
- 4.67 The major issue for the sector, affecting employees and employers alike, is the impact on training opportunities. Employers are concerned at the cost implications of restricting the exemption for apprentices aged 18–26 years to one year. They

A hairdresser in the North West had increased prices by an average of 25 per cent, in two stages, to cover the immediate impact of the minimum wage, but also to restore differentials for all employees up to salon manager.

Low Pay Commission Visit to the North West

In the area around Skegness, it was difficult for hairdressers to pass on costs to customers.

Low Pay Commission Visit to Lincolnshire

suggest that training in salons may be reduced: firms will look to colleges to provide training in technical skills and will employ newly-qualified staff to teach them interpersonal or salon skills. The NHF reports some evidence of employers making apprentices redundant at 19 years of age if they do not attract sufficient turnover to justify the minimum wage. A training provider we met in Stockport similarly suggested that older apprentices would be 'let go' in order to avoid liability for the minimum wage.

- 4.68 Overall, hairdressing employers have used exemptions for very young workers and apprentices, as well as the Development Rate for 18–21 year olds, to manage the impact of the minimum wage. In oral evidence, the associations said that the minimum wage had caused their members to consider quality and productivity more critically.
- 4.69 In hairdressing, the National Minimum Wage has increased earnings, and thus employers' wage costs, considerably. But most employers have been able to increase prices or seek greater productivity to manage the impact successfully. The impact on training opportunities for young people will, however, need to be monitored as the minimum wage beds down.

Voluntary Sector

- Main gainers part-time workers.
 - Little overall impact.
 - Smaller voluntary and grant-funded organisations under pressure.
- 4.70 Employment in the voluntary sector relies heavily on part-time and casual staff: nearly half are part time, with a further 10 per cent casual. But the National Minimum Wage has had less impact on workers in the voluntary sector than those in other sectors because 'many organisations have traditionally adopted the pay structures used in the public sector, particularly those in local authorities' (IDS Report 791, 1999). Pay restructuring to meet competitive pressures on recruitment and retention has further increased pay levels in the sector. As a consequence, little adjustment has been needed. Indeed, research undertaken by the National Council for Voluntary Organisations (NCVO) reported that 'several

Low Pay Commission Research

With joint funding from the Low Pay Commission, the National Council for Voluntary Organisations undertook a qualitative study of fifteen voluntary organisations and four service/contract providers within the sector. It found that where wages had been increased in anticipation of the National Minimum Wage, the total cost was often small in relation to the overall wages bill and was easily absorbed.

National Council for Voluntary Organisations, 1999. *The National Minimum Wage and the Voluntary Sector: Assessment of the Initial Impact.*

organisations had taken the changes in the law as an opportunity to improve their position as an employer, and had experienced very little difficulties in the process’.

- 4.71 Generally, increases in wage costs have been absorbed into existing budgets. There is some evidence of consolidation of allowances or premia into basic pay. Some organisations have had to reduce the level of service they provide, although this strategy has been resisted wherever possible. Evidence from the NCVO indicated that where reductions were necessary, reduced grant funding or the effect of local authorities contracting on a ‘best value’ basis had been factors.
- 4.72 A number of organisations which provide accommodation, such as the Youth Hostels Association, have had to revise their pay structures to take account of the accommodation offset. Several have found the subsequent increase in wage costs difficult to manage and have sought a higher offset. Some organisations have also experienced difficulty in determining whether their voluntary workers are eligible for the minimum wage. We discuss both the accommodation offset and definitional issues in Chapter 5.

Conclusion

- 4.73 The National Minimum Wage has made a difference to many low-paid people employed within a range of sectors. Women, especially those in sectors such as retail, hospitality and social care, where part-time work is common, have been the main gainers. But many young people have also benefited. As a consequence, for some employers, the National Minimum Wage has led to a substantial increase in the wage bill and managing such an increase has not been without pain, especially for small businesses and certain subsectors. Generally, however, the effects have been transitional and one-off, and most firms affected have been able to adjust, despite also having to cope with other business pressures.
- 4.74 We are impressed by the way in which employers have sought to manage the process by improving productivity, restructuring working practices and absorbing costs through reduced profits rather than by resorting to significant job reductions or price increases. Nevertheless, a few minor issues, relating to interpretation and implementation, were raised in the evidence we received and these are discussed in the next chapter.

5 Defining Workers, Pay and Working Time

While in general the definitions of a worker, pay and working time have performed well, a small number of anomalies have emerged. More guidance is needed on voluntary workers and on people undertaking therapeutic activity. Coverage of students should be more consistent. The level of the accommodation deductor needs to be kept under review, and the broader question of non-standard work (such as sleeping over) should be reviewed in the longer term as the National Minimum Wage settles in.

- 5.1 As we said in our first report, ‘the definition we recommend goes with the grain of existing pay structures and – what is even more important – it is fair’. The evidence at a sectoral level, discussed in Chapter 4, shows that in general the implementation of the National Minimum Wage has gone very smoothly, and the definition of the wage has been easily accommodated by business. Some anomalies, nevertheless, have been drawn to our attention. These can be grouped under three headings:
- the definition of a worker: who is eligible to receive the National Minimum Wage;
 - the composition of the wage; and
 - the definition of working time.

Definition of Worker

- 5.2 The areas of concern expressed to us about the definition of a worker for National Minimum Wage purposes are coverage of voluntary workers, people with disabilities who are undertaking work-like activities for therapeutic reasons, and directors who are also employees. Anomalies in the coverage of students and seafarers were also drawn to our attention.

The main area of uncertainty has been over what constitutes a ‘worker’ for the purposes of the Regulations. In the vast majority of cases the issue is clear. As ever it is on the margins where there are problems.

English Heritage Evidence

Voluntary Workers

- 5.3 In its consultation document on the draft National Minimum Wage Regulations (DTI 1998), the Government set out clearly the position of volunteers, stating that ‘most volunteers will automatically be excluded from the Act, because they are not covered by the definition “worker”, due to the absence of any intention to enter into legal relations and the resulting absence of a contract’. Thus genuine volunteers are not entitled to the minimum wage. In common usage, the distinction between a volunteer and a worker is clear. But the introduction in the legislation of two types of voluntary worker – the first entitled to the minimum wage, and the second (who receives only expenses or subsistence) exempt – has created confusion.
- 5.4 Section 44 of the National Minimum Wage Act, which was drafted in consultation with voluntary organisations, created exemptions to the coverage of voluntary workers. While DTI produced guidance specifically on this issue, our evidence shows that some uncertainty remains over status: as the National Council for Voluntary Organisations stated in its evidence, ‘grey areas remain around definitions of worker, voluntary worker and volunteer’. The National Centre for Volunteering summarised these concerns in its evidence:
- Although the Minimum Wage Act is not intended to affect volunteers, the voluntary workers exemption clause (clause 44) is causing confusion in the voluntary sector and for lawyers in voluntary organisations. This results from uncertainties about:*
- *what constitutes an employment contract;*
 - *what constitutes a contract between an organisation and its volunteers;*
 - *what expenses may be reimbursed; and*
 - *what benefits-in-kind are allowable.*
- 5.5 Typical of the problems raised is that of the sporting associations which cited the person who ‘volunteers’ to act as an official at a sporting event and receives some form of benefit, such as free tickets for a future event. The associations were concerned that such benefits might be interpreted as conferring worker status, and thus entitlement to the National

Minimum Wage, on the individual. The British Red Cross Society was also concerned that the National Minimum Wage meant that ‘we are now extremely limited in what we can offer to attract, reward and retain the volunteers that are vital to the service we provide’. Age Concern England mentioned that for many years it had paid its key volunteers, such as day centre organisers, honoraria of about £10–15 per week. The charity claimed that changes in the treatment of these honoraria required by the National Minimum Wage legislation had adversely affected the relationship between the organisation and its volunteers.

- 5.6 Because of the continuing confusion there remains the danger that in some cases genuine workers in voluntary organisations who are entitled to the minimum wage may not be receiving it. While we would not wish those voluntary workers who are exempt under Section 44 to be deterred from volunteering, we are concerned that organisations should not seek to use Section 44 as a loophole to avoid compliance.
- 5.7 Given the significant degree of confusion which continues to exist in the voluntary sector, **we recommend that the Government should issue further detailed guidance on the definition of worker which is geared specifically to the needs of the voluntary sector.** Where possible, the two more familiar terms should be used: ‘volunteer’ to include those who are not covered by the minimum wage, even though they may receive payments to reimburse expenses, and ‘worker for a voluntary organisation’ to cover those who are entitled to it. The guidance should help organisations and workers to distinguish not only between the status of genuine volunteers and workers for voluntary organisations, but also whether payments made, or benefits provided, to volunteers confer entitlement to the minimum wage.

People With Disabilities

- 5.8 In our last report we were clear that workers with disabilities should be covered by the National Minimum Wage:

We believe that there are compelling arguments for treating disabled workers in the same way as other workers. To do so recognises the value of disabled workers to employers and supports a culture of social inclusion. Moreover, for those people with severe disabilities that limit their productivity, the Government funds the Supported Employment Programme which helps employers recruit and maintain these workers in jobs.

The great majority of disabled people in work are no less productive than non-disabled colleagues and are paid on the same basis. So there is no question about these disabled workers being eligible for the minimum wage.

- 5.9 For those who have limited productivity, but who can nonetheless work alongside non-disabled workers, the Government provides the Supported Employment Programme. These workers are eligible for the National Minimum Wage and therefore the costs to agencies and employers of supporting them may have risen. A number of submissions we received from agencies complained of inadequate increases in government funding to cover these additional costs. For example, the Shaw Trust told us that:

The need to bear additional costs of £200,000+ on our contracts on a year on year basis will have a significant impact on the numbers of people we are able to support, unless we receive some additional assistance from central government.

Hence **we recommend that, where necessary, the Government should fully meet the additional costs caused by the introduction of the National Minimum Wage to the Supported Employment Programme.**

- 5.10 The rules covering Incapacity Benefit and Severe Disablement Allowance allow some work to be undertaken which the Benefits Agency and the individual's doctor have agreed might improve a person's medical condition and perhaps help the chances of a full return to the labour market. Before the introduction of the National Minimum Wage the limit on earnings (known by Department of Social Security/Benefits Agency officials, but not defined in legislation, as 'therapeutic earnings') was £46.50 per week, with a maximum of 16 hours

work a week on average. In order to ensure that the National Minimum Wage did not disadvantage these individuals, the Government increased the earnings limit to £58 (i.e. approximately 16 x £3.60) per week from 1 April 1999.

- 5.11 Some people with disabilities will be in receipt of Income Support, either as a supplement to Incapacity Benefit or Severe Disablement Allowance, or because they have no entitlement to these benefits. In these cases, too, the benefit rules allow for some work, but the regulations are different and these have not been changed as a result of the minimum wage. Work must be for less than 16 hours per week, with any earnings above £15 per week offset in full against the benefit entitlement. But for people with disabilities, the earnings received up to that limit are often referred to, by themselves or others, as ‘therapeutic earnings’.
- 5.12 On our visits, in discussions with disability groups and in evidence put to us, we were made aware of the confusion over the different rules and criteria, and the apparent anomalies, surrounding the amount of work people with disabilities can undertake before any benefits are affected. **We recommend that the Government should review the guidance on benefits for workers with disabilities who are in receipt of ‘therapeutic earnings’, with the aim of making it more coherent and accessible.**
- 5.13 Our discussions and the evidence submitted to us show that, regardless of the benefit involved, there is confusion over which activities should be defined as work for the purposes of the National Minimum Wage. Some of the work designated ‘therapeutic’ for benefits purposes is in fact similar to that undertaken in open or supported employment. People undertaking this work are entitled to the National Minimum Wage. The basic principle, consistent with the provisions of the legislation, must be that an individual should be considered a ‘worker’ unless the employer can demonstrate otherwise.

Low Pay Commission Research

We commissioned research from the Association for Supported Employment which looked at the impact of the National Minimum Wage on the employment of people with disabilities. Findings were based on a survey of thirty-three agencies working with disabled people and from interviews with individual workers, their support agency and their employer. The research for the most part found that those in receipt of Income Support had reduced their hours to minimise loss of benefit while those not in receipt who earned less than £3.60 increased their income by about £13 per week on average as a result of the National Minimum Wage.

Association for Supported Employment, 1999. *The Impact of the National Minimum Wage on People with Disabilities.*

- 5.14 There are cases, however, where the activity is purely therapeutic rather than productive, and is of no commercial benefit to the employer. MIND raised these issues with us:

If the employer is benefiting from a person's work they should pay them at least the minimum wage. However, there may be circumstances in which the employer does not get significant value from what the person does, but the activity is still therapeutic and valued by the individual. In these circumstances people should be able to supplement their benefit with payments that are not a wage.

So did MENCAP:

The most difficult group are those producing very low output (well below supported employment levels), who are basically being given something to do by an altruistic employer. These people would undoubtedly lose their 'job' if the NMW was applied. We do not believe that this was the intention of Ministers or Parliament. We believe the sensible way forward is to regard this narrowly defined activity as not being work.

In these cases employers, keen to offer opportunities for therapeutic activities to people with disabilities, may be nervous of doing so for fear of adverse publicity should there be a claim that the activity is really work and therefore covered by the National Minimum Wage Act. As a result, they pay the National Minimum Wage, which results in the beneficiary reducing their hours of activity to avoid incurring loss of benefit. This is to the detriment of the individual.

- 5.15 We understand that the DTI had discussions with organisations representing people with disabilities and subsequently issued guidance on the principles for determining an individual's status. The Government's evidence quotes this guidance, pointing out:

In some cases, the informal nature of the arrangements that are in place make it unclear whether a 'worker's contract' exists or not. Where such uncertainty exists, tribunals and courts will take into account a number of factors that will indicate whether there is a contractual relationship. These include:

- *that the intention of both parties is to create a relationship of employer and worker, with the associated mutual obligations, rather than simply to enable the individual to acquire certain skills, experience, or therapy;*
- *that the individual is rewarded (with money or benefits in kind), and the payment is a 'wage' related to work actually done and which the individual has a right to receive, rather than the payment being an ex gratia 'allowance', for example;*
- *that the individual is required to turn up at work at a certain time and work a set number of hours, rather than the individual being free to come and go as he chooses.*

Case law, particularly in the area of 'trainees', shows that tribunals take a common sense approach when deciding about an individual's status in the absence of a specific employment contract. They will look at the full circumstances rather than a narrow interpretation of the law. In the context of so-called 'therapeutic work', the intention of both parties and the 'wage' related to work actually done may be crucial factors.

- 5.16 But other evidence we received, particularly from smaller agencies and individuals, and the research by the Association for Supported Employment, suggests that more advice is needed. **We recommend that the relevant departments and agencies work together to produce, and widely disseminate, clear guidance on what constitutes worker status for individuals undertaking therapeutic activity to ensure that they are not adversely affected by confusion about the legal position.**

Directors Who Are Also Employees

- 5.17 Directors as office holders are not workers for the purposes of the National Minimum Wage Act. Where directors are employed by that company, however, they are entitled to the minimum wage. Directors of small limited companies, particularly those which are in the process of becoming established, have pointed out that they are insufficiently

An individual is in full-time employment and is setting up a business through a limited company (e.g. for when he retires). He is the sole director and employee and is spending 20 hours a week building up the business. It is unlikely the business will make any profit for the first two or three years. If he pays himself the National Minimum Wage during this time, the company may never be able to establish itself as viable.

An Accountancy Firm's Evidence

viable to be able to pay the National Minimum Wage for each hour worked. They also draw attention to the freedom they have enjoyed in the past to take their income as shares or dividends rather than through pay.

- 5.18 In addition, some organisations, including the British Hospitality Association (BHA), suggested that there is an anomaly in the treatment of workers in family businesses where those businesses are limited companies. Regulations 2(3) and 2(4) of the National Minimum Wage Regulations exempt work done by 'a member of the employer's family'. But where the family business is a limited company, then Regulations 2(3) and 2(4) do not apply. The BHA suggests that this position is anomalous as the policy intention was clearly to exempt members of family businesses.
- 5.19 There are clear advantages and disadvantages in becoming a limited company. The National Minimum Wage Act has affected the workings of some very small companies in making worker directors entitled to the National Minimum Wage. Nevertheless, these directors are also benefiting from the advantages of being a limited company. An exemption of any group has adverse consequences for the universal acceptability of the National Minimum Wage, and should only be made for compelling reasons. We believe that this group of workers is in a strong position to order the remuneration of their work to suit their own business needs, and should readily be able to adapt to the minimum wage.

Students

- 5.20 The Regulations provide that students studying on higher education courses or trainee teachers do not have to be paid the National Minimum Wage where they are placed with an employer as part of their course. The provision only applies to undergraduates (other than trainee teachers) where the course is provided by a university or college in the UK.
- 5.21 The requirement for students who undertake a placement with an employer as part of a postgraduate course to be paid the minimum wage is anomalous and may damage students' prospects of finding suitable placements. Employers with budgetary constraints may opt to provide placements to undergraduates instead.

- 5.22 In addition, many students from European Union (EU)/European Economic Area (EEA) universities and colleges are placed with employers in the UK as an intrinsic part of their courses. Currently they have to be paid the National Minimum Wage whereas their counterparts from UK establishments do not.
- 5.23 While wishing to keep any exemptions to the minimum, we do not wish the minimum wage inadvertently to damage students' prospects of obtaining good quality placements. Consequently, we suggest that these anomalies should be addressed by the Government. We see no case for post-graduates to be treated differently from undergraduates. In the case of students from the EU/EEA, however, we recognise that there may be difficulties of definition and documentation, and we would not wish to create loopholes in the coverage of the minimum wage. Nevertheless, if definitional issues can be satisfactorily overcome, students from EU/EEA establishments should be treated similarly to students in UK establishments. In all cases, employers should be required to obtain documentary evidence that the students are on *bona fide* sandwich courses in which the placements are intrinsic to the course of study. Therefore, **we recommend that the Government should address anomalies in the coverage of students to make the treatment of postgraduates and, where feasible, students on EU/EEA higher education courses the same as undergraduates.**

Seafarers

- 5.24 We have been informed that there are some anomalies with the coverage of mariners. Section 40 of the Act sets out the entitlement of mariners to the National Minimum Wage. Most seamen working on board a ship registered in the UK are eligible, even if they work for long periods outside the UK. But the minimum wage does not apply if all the work is carried out outside the UK or if the seaman is not normally resident in the UK, even if working on a UK-registered ship. We suggest that the Government should consider the coverage of seafarers in any future review of marine policy. If it is to be reviewed, we would welcome consultation.

Definition of Pay

- 5.25 Our recommended definition of pay for the National Minimum Wage was designed to be simple and fair, easily enforceable and consistent with the needs of business and the low paid. In general, this definition appears to have been implemented with few problems. The CBI said that it was 'pleased that the Low Pay Commission took into account the variety of pay systems that exist when deciding on what should count as pay'. The Royal Association for Disability and Rehabilitation welcomed 'the decision not to consider most "benefits-in-kind" as pay for the purposes of the National Minimum Wage'.
- 5.26 While most employers in the hospitality sector have found the definition workable, a few suggested that the definition of tips and gratuities should be amended to include tips left on the table for waiting staff since these are counted by the Inland Revenue for tax purposes. But one large employer who had initially been concerned over the coverage of tips wrote that 'we are satisfied with the present system and would like to see it continue unchanged' (Whitbread evidence). Moreover, tips left on the table are counted as taxable income but not necessarily as pay; they do not count for National Insurance Contributions, for instance. We remain convinced that tips should not be counted as pay if they do not go through an employer's payroll.
- 5.27 We received substantial evidence on only one specific aspect of the definition of the wage: the accommodation offset. In our first report we recommended that employers should be allowed to make a deduction from the worker's wage where accommodation is provided (but not for board or meals), but limited to £20 per week. The Regulations set the accommodation offset at £19.95 per week (or 50p per hour or £2.85 per day).
- 5.28 Following a number of submissions from employers during the consultation period on the Regulations, we were asked by the Secretary of State for Trade and Industry to review the amount of the accommodation offset and report in March 1999. Our conclusion in that review was that 'there is little evidence that the majority of businesses cannot cope with the rate recommended' (Low Pay Commission, 1999b). We said that 'the most sensible approach would be for us to monitor the impact of the level and scope of the accommodation offset,

and to make recommendations for its application in the longer term as part of our report in December'. We have subsequently received further written and oral evidence from both employers and unions, we have visited some of the employers most affected, and have undertaken further research.

- 5.29 For some hoteliers who provide accommodation the modest offset allowed has had a significant impact on their costs. The BHA argued in its evidence to our earlier review of the accommodation offset that 'the maximum figure of £20 "to protect workers from unreasonable charges" is itself unreasonably low, particularly given that no additional offset is available for meals, heat, light and laundry which are traditionally provided free with the accommodation' (Low Pay Commission, 1999b).
- 5.30 For many employers running activity holiday centres, the impact of the National Minimum Wage, and the modest accommodation offset, has meant very substantial changes to their whole remuneration packages. Before the legislation, employees were often paid only about £50 a week or so, with full board and lodging. The remuneration package now has to consist of the National Minimum Wage with just £19.95 offset for accommodation. Some companies charge for meals to recoup some of their increased costs.
- 5.31 Despite these difficulties, the sectors affected by the accommodation deductor have managed the initial transition to paying the National Minimum Wage well. It has meant very big changes for some and has been met in some cases through increased prices or lower profits.
- 5.32 While the representatives of hospitality and activity holiday sectors argued for a higher offset, the GMB – which is the major trade union in the hospitality sector – says that employers have adjusted their pay rates (both up and down) to take the maximum deductor into account. The GMB believes that the level of the offset is relatively high in relation to the level of the National Minimum Wage, and has told us that most workers in receipt of accommodation are young workers on the lower rate of £3.00 an hour.
- 5.33 Some not-for-profit organisations are in a more difficult situation because they have limited means of paying the additional costs of the National Minimum Wage. For these

Twenty-six members of staff had received increases as a result of the NMW at a cost of £644 a week (£33,500 a year, or 40 per cent of profits), whereas, if the company's internal food and accommodation offset of £45 had been allowed, only eleven staff would have been affected with a total cost of £75 a week or £3,900 a year, under 5 per cent of profits.

Hotel Group, Low Pay Commission Visit to Scotland

An activity holiday centre's remuneration package had been £50 a week plus free accommodation and meals. It now pays staff the National Minimum Wage, but less an amount of £19.50 a week for accommodation. It also offers staff meals for which a separate charge is made. Since the introduction of the minimum wage, recruitment and retention had improved, but prices had risen.

Low Pay Commission Visit to the South West

organisations the accommodation offset is part of a more general problem of finding the resources to meet the additional labour costs required by the National Minimum Wage rather than a specific problem of accommodation.

- 5.34 Our own research provided further information about the use of the deductor. For some employers, the pre-existing accommodation offset was less than the National Minimum Wage deductor and has been raised to take advantage of the full offset (IDS, 1999b). As we commented in our earlier special report on the accommodation offset, the statistics indicate that this benefit-in-kind is in decline. In most of the sectors affected, the proportion of employers for whom accommodation is an issue is not large. According to a survey carried out by the BHA, only 33 of 712 respondents reported increased costs because of the deductor limit and only about a dozen said that they were reducing the availability of staff accommodation as a result of the limit. In our own first survey of 600 businesses in the hospitality sector, only 12 respondents mentioned the accommodation offset.
- 5.35 We recognise, nevertheless, that where accommodation is provided it is of benefit to both employers and workers, and a higher deductor would be one means of offsetting the impact of the National Minimum Wage. But so long as the National Minimum Wage is set at the current prudent level, we see no reason for either raising or reducing the level of deduction allowable for the provision of accommodation.
- 5.36 There may be more concern among some employers about the method of calculation of the deductor rather than its level. The BHA argues for the Regulations to be simplified so that the complexities of the alternative hourly and daily calculations and what they describe as 'the incomprehensible special calculation for holidays and sick leave should be dispensed with'. Bass plc told us 'we have regularised our situation in respect of deductions for accommodation in order to ... maintain clear records and avoid non-compliance. We would welcome change relative to accommodation, since it is very difficult to administer the offset for people who are sick.' Employers are clearly confused by the Regulations concerning the accommodation deductor. The three separate rates (hourly, daily and weekly), and the treatment of workers who are absent, are too complicated and may hinder compliance.

- 5.37 **We recommend that the accommodation deductor should be retained at its present rate and its level considered again when the National Minimum Wage is reviewed. We also recommend that the Government should investigate whether the regulations relating to the deductor could be simplified to make compliance easier for employers. At the least, simpler guidance should be issued.**

Definition of Working Time and Pay Reference Period

- 5.38 The TUC argued in its evidence to the Commission that ‘workers who do “sleepovers” were, as a group, perhaps the most vulnerable to having their terms and conditions worsened as a result of the NMW’. They claimed that some employers had taken advantage of the National Minimum Wage Regulations, which do not require any allowance for ‘sleepovers’, to cut the pay of their night workers. The TUC pointed out that measuring and recording the hours when a worker is awoken and asked to work is difficult, and that ‘some employers were designating unrealistic numbers of hours as “sleeping time”’, while others were making it difficult for workers to claim money for the time actually awake and working at night:

A worker doing a sleepover is obliged to be on the premises and to be ready to work at any time. They are unlikely to get as comfortable or relaxing a night’s sleep as they would at home, even assuming that their duties allow them to get a comparable amount of sleep. It is surely wrong that time when they are required to be at and ready for work should require no payment at all from the employer.

- 5.39 The TUC suggested that we should recommend that the Regulations are altered so that workers are fairly compensated for ‘sleepovers’, either by requiring an on-call allowance for such periods, or requiring sleeping time to be paid at a percentage of the National Minimum Wage rate.
- 5.40 In our first report we said that ‘for hours when workers are paid to sleep on the premises, we recommend that workers

should agree their allowance, as they do now. But workers should be entitled to the National Minimum Wage for all times when they are awake and required to be available for work'. We based our original recommendation on evidence that most workers required to do a 'sleepover' are paid an allowance for the inconvenience (similar to an on-call allowance). These allowances cannot count towards the National Minimum Wage calculation. If workers are contractually required to sleep on the employer's premises, as opposed to choosing to do so, then that, including any payment made as compensation, is a matter for both parties to the employment contract.

- 5.41 Although it is not our role to determine the various pay allowances and supplements which employers agree with their employees, we are concerned that there is scope for employer abuse of the 'sleepover' practice. **We recommend that the Government should produce specific guidance to emphasise the difference between 'sleepovers', where the assumption must be that the worker would not normally be wakened and where an allowance is usual practice, and 'on-call' and 'standby' arrangements, where a worker is required to be at the workplace outside of normal working hours with the expectation that he or she will be required to work, for which the National Minimum Wage is payable.**
- 5.42 We received some evidence that employers found it difficult to apply the requirement for a 'fair estimate' or 'daily average' of working time where a worker is paid entirely by output or has no specified working hours. A clothing manufacturer in Leicestershire highlighted the difficulty in obtaining a written agreement prior to each pay reference period, and the need for a fresh agreement when the nature of the work changed. The Newspaper Society said that this requirement was 'disproportionately onerous' and proposed a threshold for minimum pay or working hours below which the Regulations would not apply in such a formal way.
- 5.43 We know from evidence from those representing workers' interests that the 'fair estimate' is often not applied. Research by the National Group on Homeworking reported that the 'fair estimate' agreement had not been widely used and, where it was, it had either been misunderstood or abused

to avoid payment of the National Minimum Wage. Gray and Heyes (1999) also found that 'fair estimate' agreements were being ignored by some employers.

- 5.44 Overall, the evidence to date does not point to any immediate need to revise the Regulations which are straightforward. We suggest that the application of the 'fair estimate' and 'daily averaging' agreements should be kept under review with the aim of ensuring necessary protection is provided to workers while minimising burdens on business.
- 5.45 One anomaly in the Regulations was drawn to our attention by the United Kingdom Home Care Association. This concerns workers who, in the course of their work, have to travel between locations. The DTI Guidance (paragraph 127) is clear about the policy intention: 'There are some periods of travel time when the national minimum wage must be paid. These include time when a worker is travelling from one assignment to the next.'
- 5.46 The Regulations 15 (2) and (3), however, may be interpreted more narrowly. There is a need to clarify the intent of these Regulations. **We recommend that the Government should ensure that the regulations on travelling time properly reflect the policy intention, which is set out in the guidance: the National Minimum Wage must be paid 'when a worker... is travelling in connection with his work during normal working hours or the normal range of hours that the worker does', and, if necessary, amend the regulations at a suitable opportunity.**

Conclusion

- 5.47 Overall, the definitions of worker, working time and pay have generally been implemented well, and there are no strong arguments for fundamental changes. There are some anomalies, but these generally relate to particular industries and occupations where working practices are less easily accommodated by the standard definitions. For most cases, what is required is not changes to the Regulations, but clearer guidance from the Government.

6 Young People and the Development Rate

The Development Rate for young workers has meant a pay rise for very many young people while not affecting their employment opportunities. Most 21 year olds are already earning at or above the level of the full minimum wage. To include them in the upper threshold, therefore, makes sense. The data also suggest that a level of £3.20 per hour for 18–20 year olds would pose no significant problems for employers. The six-month Development Rate for older workers has the potential to improve their employment prospects. But more work needs to be done to ensure this potential is realised.

- 6.1 Of all the issues the Commission addressed as part of its original work, the treatment of young people proved the most difficult and challenging. Throughout we were driven by a concern for the particular problems of youth unemployment and also a belief that the way to secure and keep well-paid jobs was through the acquisition of skills and experience. As we said in our first report,

Those in the youth labour market, or trying to enter that labour market, are among the most vulnerable in the workforce. Above all else they need work, and they need work which will allow them to acquire basic skills to enable them to develop.

Our recommendation for a lower rate for young people reflected the reality of the labour market, but our longer-term aspiration was a lower Development Rate 'solely dedicated to clearly identifiable and accredited training'.

- 6.2 We recommended a Development Rate for 18–20 year olds at a level of £3.20 per hour from April 1999, rising to £3.30 per hour from June 2000. The Government chose to be more cautious and extended coverage of this Development Rate to include 21 year olds and staged this rate, setting the initial level at £3.00, to move to £3.20 in June 2000. Even at this level the Development Rate has already made a difference to the pay of young workers. In fact, it has affected the earnings

of a larger proportion of 18–21 year olds than those age 22 and above who have benefited from the full minimum wage.

- 6.3 Since its introduction, trade unions and groups representing young people have argued strongly against a lower rate for young workers. The Scottish Trades Union Congress Youth Committee in their evidence expressed concern that younger workers need protection from exploitation:

The minimum wage legislation, as it stands, is not only doing little to protect the position of young people in the current labour market, but is actually opening them up to further exploitation and hardship, as they are now a recruitment target for low-wage employers.

The Union of Shop, Distributive and Allied Workers told us that an age-based differential was discriminatory:

Age-related criteria compromise the Government's commitment to promoting economic efficiency by combating ageism. Pay rates must be directly related to competence rather than age if we are to have a more efficient labour market and a more productive economy.

We acknowledge the strength of feeling that lies behind these arguments and accept many of the principles involved.

- 6.4 Our recommendations for young people reflect our analysis of the youth labour market as it is now and our particular concern for those towards the bottom of the wage distribution. Young people are more likely to be unemployed. They are often in need of additional education or work-based training, or both. When in work, they have always been far more likely to be among the very low paid. These facts informed our discussions and shaped our conclusions and recommendations.
- 6.5 We were clear in our first report that any lower rate should encourage employers to invest in the development of their workers. The benefits to business come in improvements in performance and productivity which underpin higher wages. Where young workers have qualifications, skills and experience, they are often paid at higher rates.

Low Pay Commission Research

We commissioned research from Industrial Relations Services Ltd. which considered whether pay arrangements and employment practices, in particular those applying to young workers, had changed as a result of the National Minimum Wage. Prior to the introduction of the National Minimum Wage, two surveys of employers (one across the economy and one focusing on retail and hospitality) were supplemented by twenty-five in-depth case studies of employers identified as low-paying. Over six in ten employers paid adult rates at age 18. Case studies of ten of these firms were conducted after the minimum wage came into force. Findings suggested that young people’s pay had increased with only slight negative consequences on their employment. Rises in wage costs encouraged a focus on efficiency.

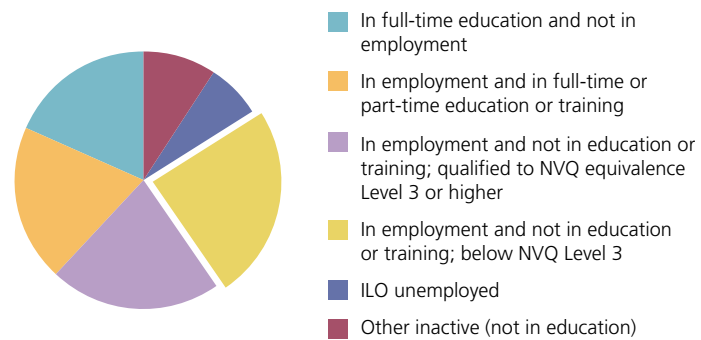
Industrial Relations Services Ltd., 1999. *The Impact of the National Minimum Wage on Young People’s Pay and Employment; and The Impact of the National Minimum Wage on Young People’s Pay and Employment: Findings of a Follow-up Study.*

Young People and the Labour Market

6.6 Young people’s position in the labour market has changed over time. In line with the overall performance of the economy, employment has risen and unemployment fallen among young people. Particularly noticeable has been the rise in the numbers staying in full-time education. Those most likely to be vulnerable to unemployment and low pay throughout their lives, however, are those leaving full-time education with few, if any, qualifications. They often move into jobs where there is no formal training or any chance to participate in a programme of learning which leads to a nationally-recognised qualification. Almost a quarter of all 18–24 year olds are in jobs without formal training and have not reached National Vocational Qualification (NVQ) Level 3 (Figure 6.1).

Figure 6.1

Education, Training and Qualifications of Young People Aged 18–24, 1999



Source: LFS, Spring 1999

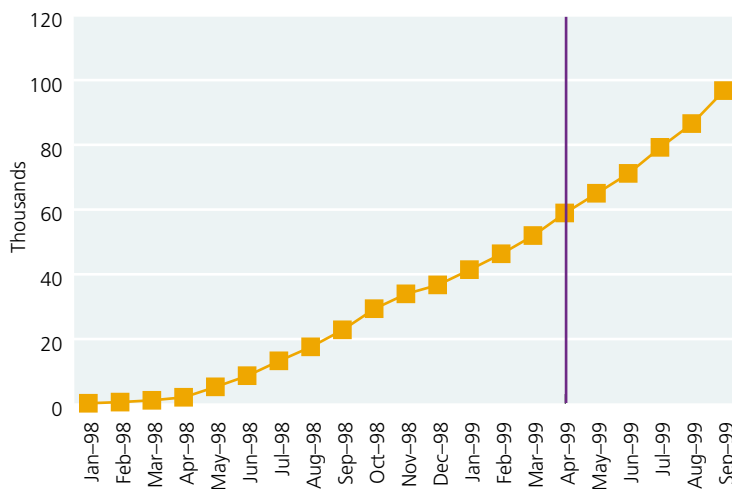
6.7 These young people, and those who are unemployed or economically inactive whose position is potentially much worse, are the most vulnerable to exclusion from mainstream society. This has long been recognised, and the Government is taking action to address their specific problems. But there is currently no sufficiently coherent work-based training provision to ensure that young people are not left in low-paid jobs with no qualifications. Without coherent provision, the youth labour market remains inefficient; young people lacking essential skills will continue to face the threat of low-paid work or, worse,

unemployment. We remain some way from our stated goal of being able to link a lower rate with formal training. There is a danger that if the full National Minimum Wage were applied immediately to young people, without exploring a phased or incremental approach, it could disadvantage those who most need protection.

- 6.8 The New Deal for 18–24 year olds is a major initiative designed to help young unemployed people find and keep jobs. We were clear in our first report about ‘the need to avoid the National Minimum Wage acting as a disincentive for employers to become involved in the initial six-month phase or to offer permanent jobs’. Fears that this might have been the case have proved unfounded. Figure 6.2 shows that the number of participants moving into sustained (thirteen weeks or more) employment has continued to rise.

Figure 6.2

Numbers of Young People Entering Sustained Employment on Leaving the New Deal



Source: New Deal Evaluation Database

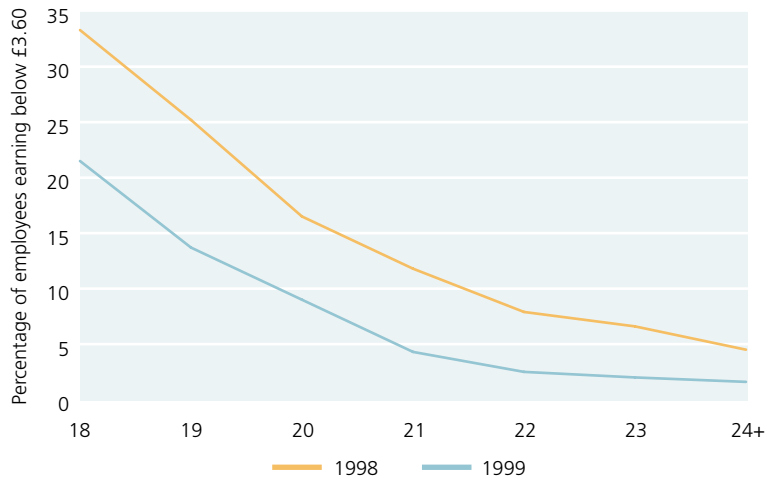
6.9 The Government gave us anecdotal evidence that New Deal participants were paid at the same rate as their colleagues, with any increase necessitated by the minimum wage applied to all. One of our research projects involved a small-scale survey of firms, primarily with less than fifty employees, involved in the New Deal (Edwards, 1999). Fewer than one in ten employers said that the minimum wage would make it less likely that New Deal participants would be retained once the subsidy had finished.

21 Year Olds

- 6.10 In our current terms of reference, the Government specifically asked us to review the position of 21 year olds. Once again we have considered the available labour market data, our own research and evidence received from employers, worker representatives, and other interested organisations and individuals.
- 6.11 In our first report we made clear that deciding whether the cut-off should be at age 20, 21 or 22 was difficult because the data could be interpreted in different ways. Certainly there were a larger proportion of 21 year olds than older workers earning less than £3.60. But we also gave weight both to views expressed by employers and to evidence of existing practice which suggested a cut-off below age 20 would be appropriate. The final decision was always going to be a matter of judgment.
- 6.12 For this report, the data are clearer. Figure 6.3 gives details from the New Earnings Survey (NES) of changes in the proportion of workers earning less than the full adult minimum wage between 1998 and 1999. This shows that the proportion of 21 year olds earning less than £3.60 per hour fell by two-thirds to around 4 per cent in the year to April 1999. The remaining proportion is now lower than the equivalent figure for all workers aged 22 or over in 1998, and around half of the 1998 figure for 22 year olds.

Figure 6.3

Proportion of Workers Earning Less Than £3.60 Per Hour, 1998–1999

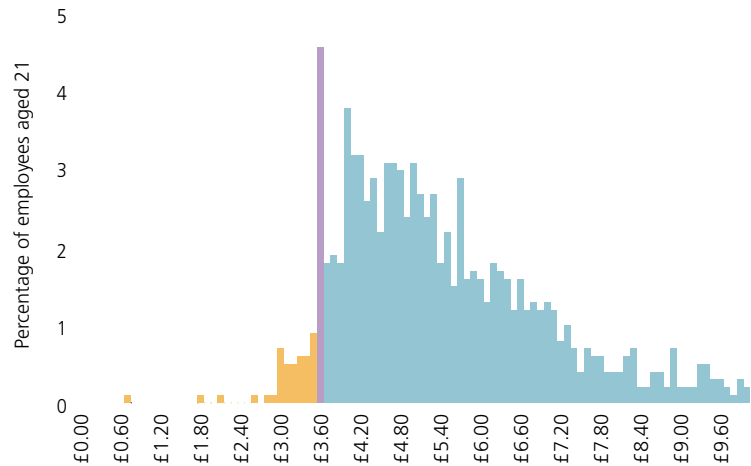


Source: NES, April 1998, 1999

- 6.13 While the pattern is clear, we can be less certain about the actual number of workers who would be affected by a lowering of the age threshold of the full minimum wage. The NES undersamples low pay, and the Labour Force Survey (LFS) data for specific age groups are unreliable, not just through general precision problems, but also because of small sample sizes and a large level of proxy response on pay questions. As a guide, therefore, the 4 per cent NES estimate corresponds to less than twenty thousand 21 year old employees. Figure 6.4 shows the hourly pay levels of 21 year olds at April 1999. Further movements in earnings, the result of normal wage settlements, will mean that the number paid below £3.60 per hour in June 2000 is likely to be considerably below twenty thousand. Hence, even allowing for undersampling, the numbers affected will be small.

Figure 6.4

Hourly Earnings of 21 Year Olds, 1999

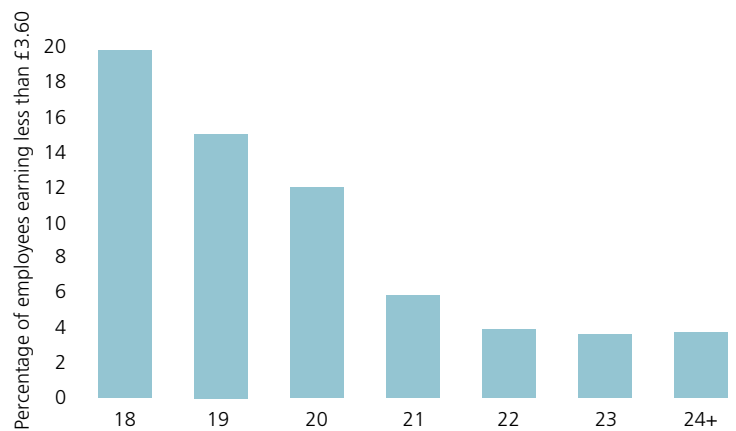


Source: NES, April 1999

6.14 In our first report we noted that young people tended to be concentrated in particular sectors. The 1999 NES shows, for example, that almost two-fifths of 21 year olds earning below £3.60 per hour worked in hospitality and retail. Figure 6.5 shows that the pay of 21 year olds in these sectors is very much closer to that of 22 year olds than to 20 year olds.

Figure 6.5

Proportion of Workers Earning Less Than £3.60 Per Hour in Hospitality and Retail, 1999

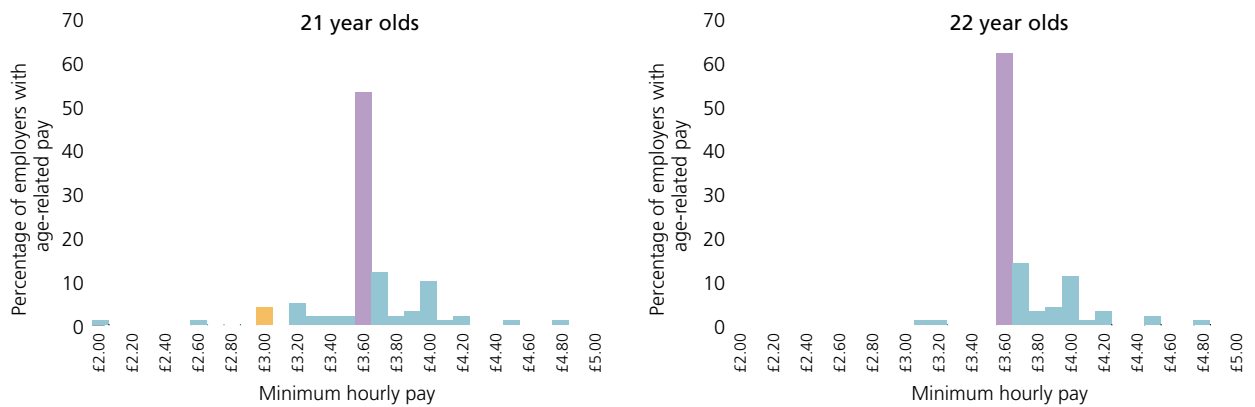


Source: NES, April 1999

6.15 Our own post-implementation survey was of 360 firms, mainly small, which were directly affected by the minimum wage. Half of these had no age-related pay. Of those that did, 85 per cent paid 21 year olds at levels of £3.60 or higher. Overall, as Figure 6.6 shows, pay rates for 21 year olds were close to those for 22 year olds.

Figure 6.6

Minimum Rates of Pay for 21 and 22 Year Olds in Low-paying Firms, 1999

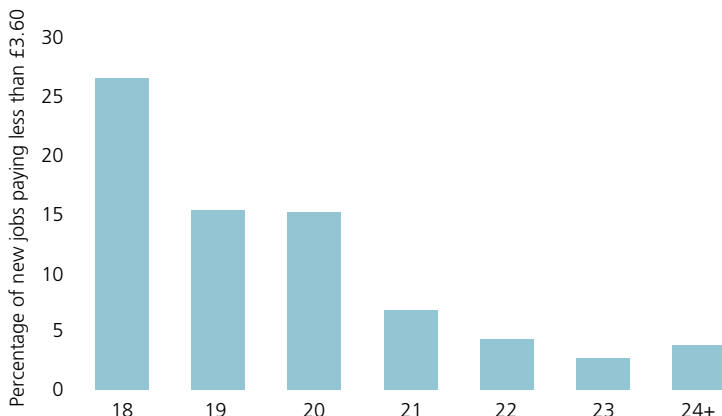


Source: Low Pay Commission Survey, September–October 1999

6.16 Any assessment of young people’s entry into the labour market must take account of their initial levels of pay. Figure 6.7 gives details of the earnings of 18–24 year olds in new jobs. This gives further weight to the evidence we have already noted. We can see that 19 and 20 year olds are more than twice as likely as 21 year olds to be paid less than £3.60 per hour when starting work.

Figure 6.7

Proportion of New Jobs Paying Less Than £3.60 Per Hour By Age of Employee, 1999



Source: NES, April 1999

- 6.17 We examined what impact the inclusion of 21 year olds in the coverage of the full minimum wage would have on the overall wage bill. Using data from the April 1999 NES, and allowing for increased compliance and the impact of normal wage inflation up to June 2000, we estimate that making this change would add only 0.2 per cent to the cohort wage bill. We noted earlier that the NES understates low pay but, nonetheless, we are confident that such a change would have minimal effects.
- 6.18 In evidence submitted to us, trade unions generally argued that the full rate of the minimum wage should apply at age 18. UNISON argued for paying the full rate at age 16. There was also support for a lower training rate irrespective of age. Many employers suggested that age was not the most important criterion. The Federation of Licensed Victuallers Associations said in their evidence that the 'majority of our members pay 18–22 year olds £3.60 per hour once they are fully trained. We are surprised that 21 year olds were not brought into the £3.60 pay structure'. Some employers and employer representatives, in their evidence to us, tended to support the *status quo*, in order to avoid any disruptive changes at this early stage in the development of the minimum wage. But there was no significant evidence arguing for the exclusion of 21 year olds from the full rate. The general view tended to support the pay data: that a threshold at age 22 cuts across prevailing pay practices.
- 6.19 Youth unemployment continues to decline, partly reflecting the success of the New Deal. Recently youth unemployment has been falling faster than overall unemployment. The ILO Unemployment Rate (from the LFS) for 18–24 year olds declined in the year to Summer 1999 by 0.7 percentage points. The number of 18–24 year olds on the claimant count fell by almost 40,000 in the year to October 1999. More detailed analysis shows that in the year to Summer 1999, ILO unemployment for 21 year olds fell by 1.5 percentage points, but among 22 year olds there was a 0.9 percentage point rise. But, since neither of these changes is, in statistical terms, significant, we do not believe that conclusions can be drawn from them. Figures from the claimant count for October 1999 show annual falls in the number of 21 year old and 22 year old claimants of 5,000 and 7,500 respectively. We therefore

believe that the minimum wage has had no discernible negative impact on youth employment. The overall trend remains firmly on a downward course.

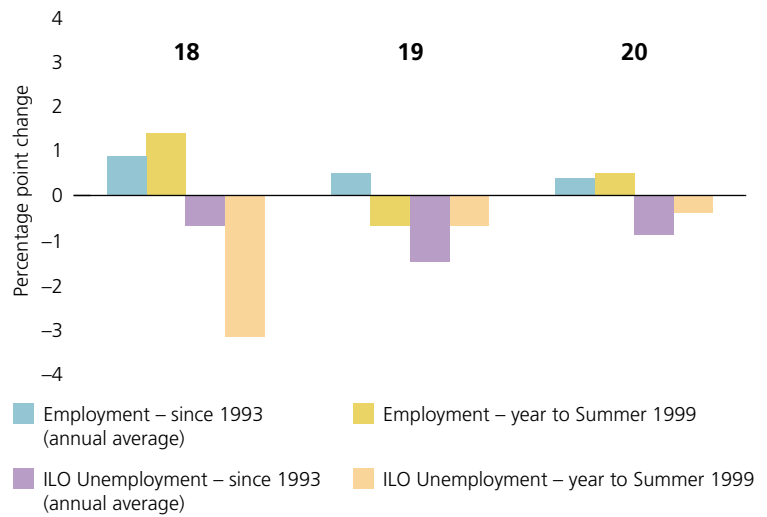
- 6.20 Research for us by Hughes et al. (1999), involving a survey of over 1,500 mainly small businesses showed some overall increase in the employment of 18–21 year olds, but not to the detriment of older (more expensive) workers. There was no evidence of younger workers, who are paid a lower National Minimum Wage or who are outside its scope, being substituted for older workers. With only one exception, in all firms where the employment of younger workers had increased, the employment of older workers had also increased or had remained unchanged.
- 6.21 Overall, the official data were supported by our own research and our extensive consultation: the vast majority of 21 year olds earn at least £3.60 per hour. But we believe it is important to offer formal protection against exploitation to those paid below £3.60 now, and for those at risk in the future. Such a change would not have any significant negative impact either on the employment prospects of 21 year olds or on their employers. Hence **we recommend that the Government should include 21 year olds in the coverage of the full National Minimum Wage from June 2000.**

18–20 Year Olds

- 6.22 We showed in Chapter 3 that the overall labour market has performed strongly over the last few years, with unemployment continuing to fall and employment increasing. This finding also holds for the youth labour market, including those below age 21. Figure 6.8 shows the overall picture for 18–20 year olds during the recent recovery. Unemployment continues the decline which started in the early 1990s.

Figure 6.8

Changes in Employment and Unemployment Among 18–20 Year Olds, 1993–1999

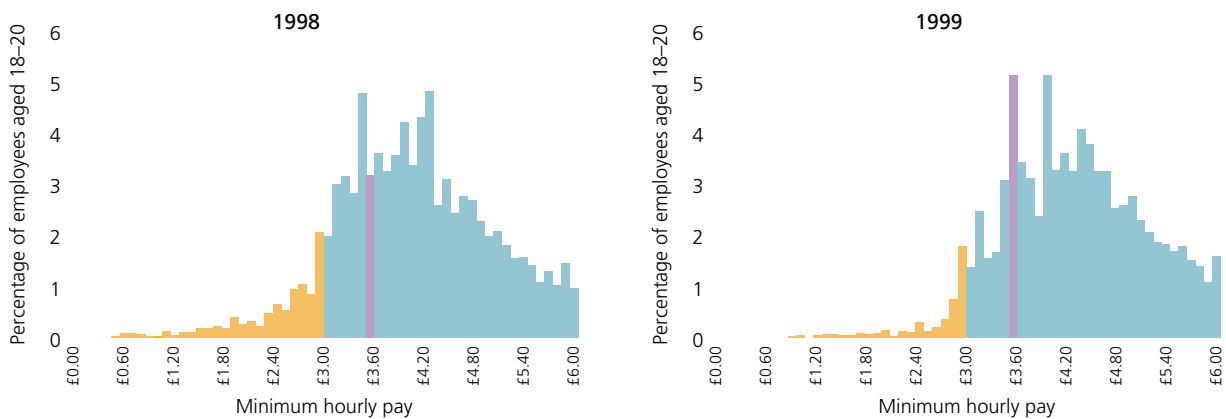


Source: LFS, Summer Quarters 1993–1999

6.23 With no discernible negative effect on the overall employment of 18–20 year olds, the minimum wage has clearly had a positive impact on their pay. Figure 6.9 gives a picture of change over the period April 1998–April 1999 which provides early evidence that large numbers of 18–20 year olds have seen their pay rise to £3.00 per hour or more. Upward drift at levels higher than £3.00 might also be a consequence of the minimum wage. But the further away from £3.00, the more likely it is that any increase is a reflection of normal wage inflation.

Figure 6.9

Hourly Earnings of 18–20 Year Olds, 1998–1999

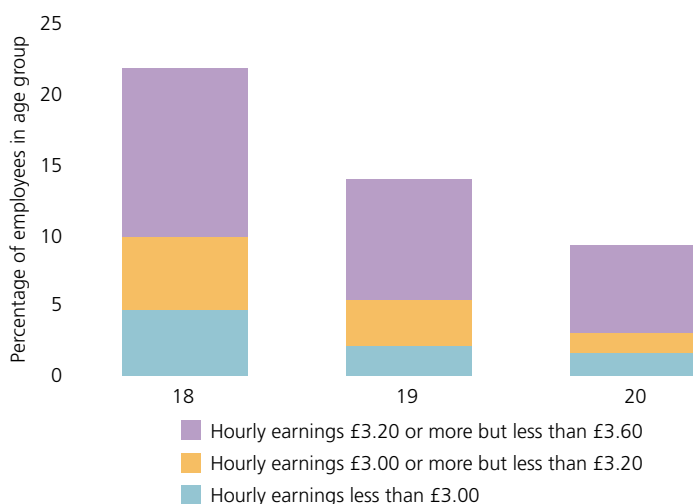


Source: NES, April 1998, 1999

6.24 Figure 6.10 shows the proportions of 18, 19 and 20 year olds earning less than £3.00, £3.00–£3.19 and £3.20–£3.59 per hour in April 1999. The proportion of these young workers earning less than £3.00 is very small. Some will have seen their pay rise subsequently; some will be exempt because they are apprentices. There is also a comparatively small proportion earning £3.00–£3.19. Allowing for even minimal wage inflation, this proportion should decline still further over the coming year. Certainly the numbers likely to be affected, and the size of the pay hike involved, are far lower than the comparative position in April 1998 when the £3.00 rate was introduced. The Government’s declared intention to increase the rate for 18–20 year olds to £3.20 in June 2000 (Hansard, 1998), therefore, should have only a very small impact on employers. But, as Figure 6.10 makes clear, the picture changes when considering the proportions of 18–20 year olds being paid below £3.60.

Figure 6.10

Low-pay Incidence Among 18–20 Year Olds, 1999



Source: NES, April 1999

6.25 Paying a full adult rate at 18 is a practice followed by very many employers, particularly larger businesses in higher-paying sectors. Analysis of pay details in vacancies held by Jobcentres conducted for us by the Low Pay Network found only a very small number of advertisements which featured the lower rate for 18–21 year olds (Low Pay Network, 1999). But for some employers the ability to

Low Pay Commission Research

We commissioned research from Rosemary Lucas and Michele Langlois of the Manchester Metropolitan University which examined the impact of the National Minimum Wage on young workers in hospitality and retail. The work involved a postal questionnaire and thirty-one follow-up interviews. Findings suggested that few employers had changed employment, training and pay policies for workers aged under 22; that most employers paid the adult rate from age 18 or 21; and that there was little use of apprentices or government trainees.

R. Lucas and M. Langlois, 1999.
The National Minimum Wage and the Employment of Young People.

Low Pay Commission Research

We commissioned the Low Pay Network to examine the impact of the National Minimum Wage on young people. The work involved a survey of Jobcentre and Careers Service vacancy and pay information, and case studies of individuals who contacted employment rights advice lines operated by Low Pay Network members. The research found that, where details were given, 70 per cent of jobs paid above £3.60, with over 40 per cent above £4.00.

Low Pay Network, 1999. *The National Minimum Wage.*

pay young people a lower rate, at least initially, determines whether the young person is employed at all. The Association of Convenience Stores told us in their evidence that ‘the young workers’ rate allows retailers to take on staff at a lower rate of pay – often for a trial period – before raising this rate’.

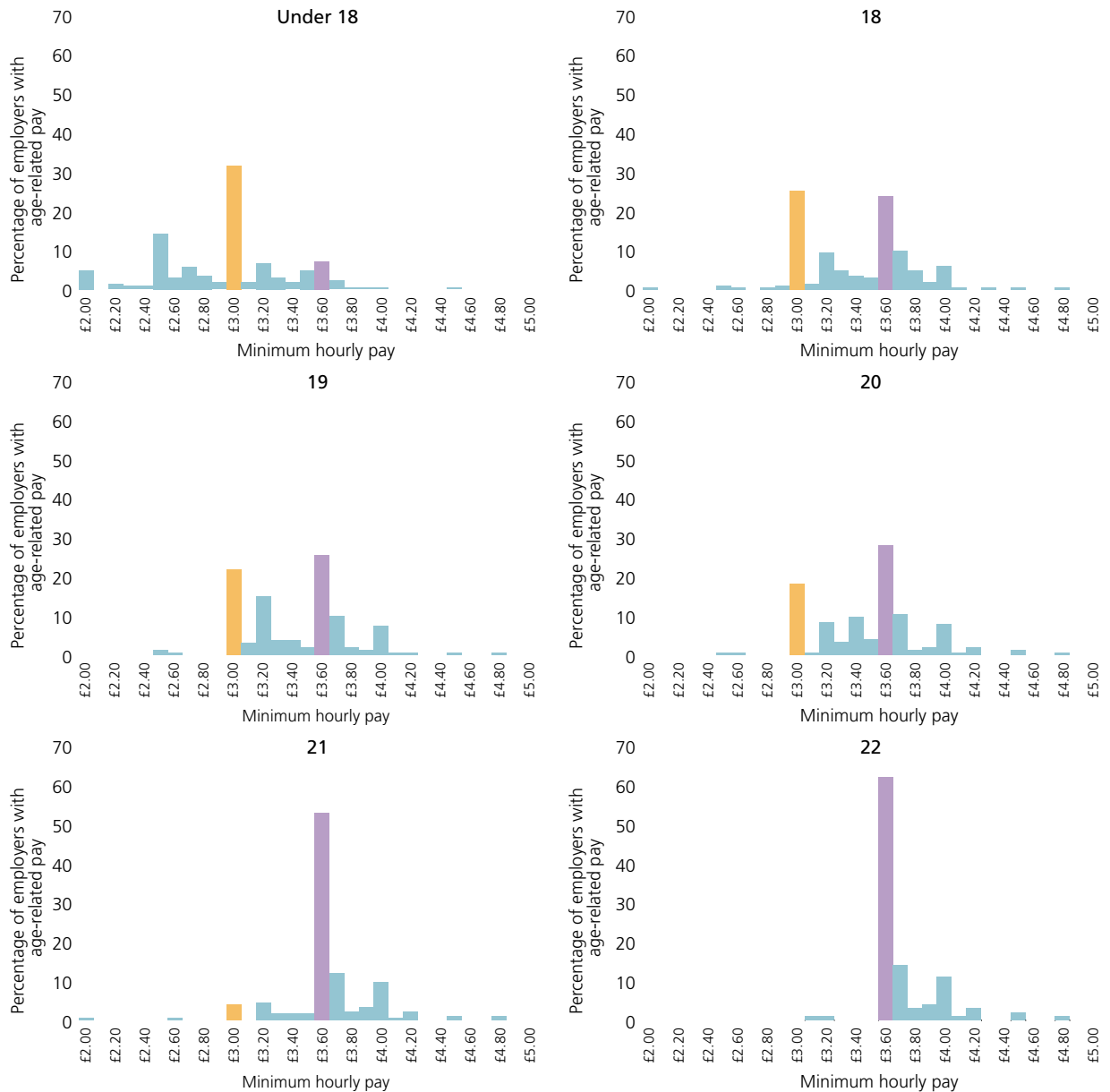
- 6.26 Our post-implementation survey of 360 mainly small firms directly affected by the minimum wage revealed clear differences in young workers’ pay. Figure 6.5 gave details of the pay of 21 and 22 year olds. Figure 6.11 shows the distribution of minimum pay rates for those aged up to 22. Over half the firms have minimum pay rates below £3.60 for 18–20 year olds. For those aged under 18, minimum pay rates are below £3.00 per hour in 40 per cent of firms. The pay profiles of 21 and 22 year olds are similar but distinct from those of younger workers.
- 6.27 Clearly, pay profiles can and will change over time. The changes shown in Figure 6.3 and Figure 6.9 broadly reflect the requirements of the minimum wage. The key question is how far the profiles can change without any increase in unemployment.
- 6.28 Our initial recommendation of a lower rate for younger workers was aimed at encouraging not just their employment but employment with the opportunities to develop their skills and experience. This is the best safeguard against being locked into a damaging cycle of low pay and unemployment. We said in our first report that

In the longer term ... the ‘Development Rate’ for young people should be linked with, and clearly dependent on, the promotion of structured training and development. Government, employers and training organisations need to develop coherent strategies for the education and training of 18–20 year olds.

We hope that those young workers most likely to be at the bottom of the earnings distribution, and therefore in most need of protection, would over time become engaged in some form of education or accredited vocational training. We find it encouraging that increasing numbers of young workers are participating in National Traineeships and Modern Apprenticeships. But we are still a long way from the position where young people in low-paid jobs are receiving that type of accredited training.

Figure 6.11

Distribution of Minimum Hourly Pay Rates by Age, 1999



Source: Low Pay Commission Survey, September–October 1999

6.29 Too many young people continue to enter the labour market with few, if any, qualifications. They find themselves in jobs which offer the prospect of neither higher wages nor proper training. In 1999, 60 per cent of 18–20 year olds in employment were not in any form of education or training. For this group, levels of achievement remain disappointingly low. A third had not reached NVQ Level 2 or equivalent;

three-quarters had not reached NVQ Level 3. This represents only marginal improvement since 1997.

- 6.30 Many employers have coherent and sophisticated training strategies. But many do not. Overall, there seems to have been little change so far in employers' training policies in response to the National Minimum Wage. Where training exists, this has continued (often with a wage much higher than the £3.00 rate). In other workplaces there is still an absence of training.
- 6.31 We are disappointed at the apparent perception of those responsible for education, employment and training strategies that statutory minimum wage rates for young people are irrelevant to their organisations' performance and policies. The key bodies – such as the Department for Education and Employment, the Social Exclusion Unit and National Training Organisations – need to recognise the minimum wage as a positive tool that could help achieve broader Government objectives. The design of the Working Families' Tax Credit took into account its dynamic interaction with pay and other benefits, including the minimum wage, thereby creating a coherent and very effective policy on in-work poverty. This seems to us a model that could usefully be copied by those responsible for training policies.
- 6.32 If, as we hope, the Government's policies for young people are eventually successful, then the large majority would either be in full-time education or in jobs which provide accredited training or education opportunities, and could thus be covered by a lower Development Rate linked to training. But if developing policies do not prove successful, with large numbers of young workers in low-paid jobs which offer no prospect of training or development more generally, we would need to reassess the use of the Development Rate for younger workers.
- 6.33 We do not claim that a lower rate for young workers is fair. We restate our aspiration that in time any lower rate would be linked to the provision of accredited training. But our initial recommendation that there should be a lower rate for young people reflected the size of the wage rise that would have been needed to bring young people's average wage up to the adult minimum. With the loss of jobs that would certainly have followed, to recommend otherwise would have been irresponsible.

- 6.34 Future consideration of the treatment of 18–20 year olds should include a full assessment of the impact of their initial pay levels, and employer practices in the light of the prevailing economic circumstances and the new Government initiatives. It should also be based on an assessment of the broader labour market and, more specifically, of the age/earnings profiles for details of the likely impact of any increase in the coverage of the rate. Figures 6.10 and 6.11 indicate that any such increase would need to be incremental to avoid too great a wage hike and the consequent negative impact on young people's employment. The minimum wage would quickly fall into disrepute if it ceased to have any real impact on the labour market. But we must continue to ensure it does not increase young people's vulnerability to unemployment; this has to be the context in which any further reduction in the qualifying age is considered.
- 6.35 We also believe in the importance of looking at the use employers make of the lower rate for younger workers and of assessing how effective it proves as part of the emerging employment and training framework. There will continue to be employers who will not offer structured training to their young workers. Some will be paying at levels above the Development Rate or even the full National Minimum Wage; some will be paying the minimum required. Monitoring take-up will allow judgments to be made about the relevance of this lower rate in the changing labour market and what, if any, modifications might help increase its use.

16 and 17 Year Olds

- 6.36 In general, the position of 16 and 17 year olds in the labour market remains very much like that described in our first report. Three-quarters are in full-time education. A further 15 per cent are in part-time education or work-related training.
- 6.37 The extended and additional Government initiatives aimed at 16 and 17 year olds have reinforced our view that they should not be considered full-time participants in the labour market. But many more will be reliant on employers providing the training and work experience they need to underpin successful working lives. We must not do anything which might reduce these opportunities.

- 6.38 Over the next few years there needs to be a full examination of the impact of the minimum wage on young people in work, both those workers covered by it and those aged under 18 who fall outside its coverage. For the present, we draw attention to research cited earlier (paragraph 6.20) which found little evidence that older workers were being replaced by young people. The same survey reported that there had been no change in the employment of 16 and 17 year olds in the vast majority of firms covered. There is anecdotal evidence, however, of the growing importance of 14 and 15 year olds in the labour market. This should be kept under review.
- 6.39 We cannot yet assess fully the impact of the minimum wage on the youth labour market: for instance, whether its introduction at age 18 has unintended consequences for younger workers. Future considerations should include the possibility that 16 and 17 year olds at least need some specific labour market protection, either through a lower rate minimum wage or an extension of existing legislation covering child labour. A broad agenda would need to consider the treatment and experiences of young people in England, Northern Ireland, Scotland and Wales, and to focus not just on the world of work but on the various routes that exist between school and work.

Government Initiatives for Young People

- 6.40 Since our first report, there have been a number of new Government initiatives and an extension of existing ones, with the primary focus on young people with few, if any, qualifications. (A brief summary of these initiatives is contained in Appendix 6.) The particular concerns about 16–18 year olds who are not in education, training or work have been articulated by the Social Exclusion Unit (*Bridging the Gap*, 1999). The new and developing policies are designed to encourage maximum development of individual skills. For young people, the aim is to ensure either that they stay in full-time education or, when they enter employment, that there are opportunities for them to achieve nationally-recognised skills and qualifications which will help secure their future. We have noted with great interest the recent work of the National Skills Task Force in ensuring

the necessary practical focus for this aim (see, for example, its second report, *Delivering Skills for All*, 1999).

- 6.41 As we made clear in our first report, it is important that the National Minimum Wage does not cut across these new initiatives; ideally, the minimum wage should support them. For this to happen there needs to be continuing dialogue between all the interested parties. Many of the initiatives launched by the Government have been based around successful working partnerships within Whitehall and between government departments and outside bodies. There needs to be a similar approach to the continuing development of the minimum wage, especially in its relationship with employment and training opportunities.
- 6.42 We have been greatly encouraged to learn of employers formalising existing training arrangements and taking on Modern Apprentices, and to be told by employers that the minimum wage had not deterred them from active participation in the New Deal. We came across only one or two instances where the operation of the National Minimum Wage had resulted in some unanticipated or unwanted practices. For example, the regulations governing exemptions for apprentices appear in hairdressing to be encouraging some employers to take on 16 and 17 year olds, and to reduce opportunities for those aged 19 and above. The Hairdressing Employers Association and the National Hairdressers' Federation reported in their evidence that 'employers are seeking to attract younger workers and that consequently mature students will find it difficult to find a position'. While the main target is the younger person, it would be wrong for those only slightly older to be denied access to this type of training.
- 6.43 One anomaly drawn to our attention concerns the position of those young people in England and Wales engaged in National Traineeships. In essence this training is the same as a Modern Apprenticeship, although leading to NVQ Level 2 rather than Level 3. It is treated quite differently for minimum wage purposes, however, because of the timing of the introduction of National Traineeships: they were too new for us to consider properly in the first report and we therefore did not recommend any exemption. Given that the training meets the key criteria of being nationally recognised and based on

a formal agreement between employer, young person and training provider, there are good grounds for a National Trainee with employed status to be treated in the same way as a Modern Apprentice. Hence **we recommend that the Government should amend the regulations so that National Traineeships are treated in the same way as Modern Apprenticeships.** That is, National Trainees aged 18 should be exempt, and those aged 19–25 should be exempt for the first 12 months of their Traineeship.

- 6.44 There are differences between the education and training systems in England, Northern Ireland, Scotland and Wales. The youth training programmes in Northern Ireland (Jobskills) and Scotland (Skillseekers) incorporate Modern Apprenticeships, but also include other training of similar structure and standard to Modern Apprenticeships (NVQ/SVQ Level 3) or National Traineeships (NVQ/SVQ Level 2). The term National Traineeship is not recognised in either Northern Ireland or Scotland. The Government's evidence drew attention to the implications of this for eligibility for the minimum wage. When the training is equivalent to Modern Apprenticeships and National Traineeships, and the young people are in employment, then clearly it should be treated similarly for minimum wage purposes. As training and education systems are further developed in different parts of the UK, we would urge decision-makers to ensure that differences in nomenclature do not give rise to confusion over treatment under the minimum wage.

Development Rate for Older Workers

- 6.45 The importance of training and development to workers of all ages, not just the young, was recognised in the Commission's first report:

People joining the labour market, whether newcomers or people returning after absence, are in particular need of training. Without an incentive, there is a danger that employers either will not offer these people work, or will hire them but not train them.

The Development Rate for Older Workers recommended by the Commission was designed to be such an incentive. The Government subsequently decided that workers aged 22 or above who start a new job with a new employer, and who are undertaking accredited training, would be entitled to a minimum rate of £3.20 per hour for the first six months. In line with our recommendation that the full minimum wage should apply to 21 year olds, we would expect the Development Rate to be extended to cover workers aged 21 or above.

- 6.46 So far, take-up of this Development Rate has been low. The initial focus of attention, understandably, has been on the main rates of the minimum wage. While it is unrealistic to expect very many employers to have been able to change existing practices, or introduce new ones, so soon after April, there is some encouraging evidence. In our survey of 360 mainly small firms affected by the minimum wage, 29 per cent had increased investment in training and development as a result of the minimum wage. There are some cases, notably in the pub/restaurant sector, which we believe provide good examples of how this Development Rate can benefit businesses and workers. Bass plc told us in their evidence that ‘training plans have become more structured and generalised as a result of accreditation’. And Scottish and Newcastle Retail said that the Development Rate ‘did not alter the amount of training undertaken but served to further embed it within the organisation’.
- 6.47 There are two general observations we would make. First, there seems to be some genuine confusion and misunderstanding about the Development Rate; some employers appeared not to have known of its existence. Second, some employers, particularly in smaller businesses, appeared unsure about what exactly was meant by ‘accredited’ training, and whether their training was, or could be, accredited. The Brewers and Licensed Retailers Association told us that

Smaller operators in our sector have ... experienced difficulties in meeting the requirements for accredited training and have been unable to utilise the Development Rate. Some support or guidance for SMEs on the introduction of formal training schemes could be helpful in improving the take-up of the Development Rate among smaller employers.

- 6.48 Research we commissioned from Lucas and Langlois (1999a) quotes a pub landlord as saying 'I don't fully understand what accredited training is, so I don't know if it's feasible ... I don't know ... whether I have the staff or financial resources to provide it'. For some, there was an assumption that 'accreditation' necessarily involved time-consuming bureaucratic processes. In addition, and this must be of particular concern, employers often did not know where to turn for advice.
- 6.49 There is a need to publicise the Development Rate more widely. Accreditation of essentially in-house training is an issue which should be addressed by bodies such as the National Training Organisations and, in the near future, by the new organisational structures being created following the post-16 review. This would be a sensible extension of the arrangements developed as part of the employer option of the New Deal we referred to in our first report.
- 6.50 If the Development Rate is to work as we hoped, encouraging employers to invest in the development of workers' skills, not least to the benefit of the business, and making a positive contribution to the achievement of the Government's Lifelong Learning initiatives, then more work needs to be done by those agencies and organisations most closely involved in providing training and employment opportunities. We note the changes around accreditation which may accompany the review of post-16 education and training and the developments in opportunities for older people (see Appendix 6) and very much welcome the Government's commitment to keep us advised about developments.

Conclusion

- 6.51 The youth labour market continues to perform strongly. Unemployment continues to fall and employment to rise. The Development Rate for young people has seen wages rise without any significant negative impact on employment. Most 21 year olds are already being paid at or above the full minimum wage. We believe it is right to include these workers in the coverage of the full National Minimum Wage. We are reassured that the move to £3.20 per hour for 18–20 year olds in June 2000 will not have any significant negative impact: compared with the initial introduction of the £3.00 rate, it will affect far fewer people, and the hike in wages will be much less. While take-up of the six-month Development Rate has been slow, there are already good examples of how this can support employment and training initiatives. We expect there to be further examples in future.
- 6.52 A full analysis of the impact of the minimum wage on the youth labour market will need to be made over a longer period. Only then will it be possible to identify the full effects not just on those eligible for the minimum wage but also on those younger workers currently outside its coverage. This will also allow the necessary assessment of the new training initiatives, and their take-up by employers, to be made.

7 Compliance and Enforcement

The National Minimum Wage should be largely self-enforcing, and the initial publicity was successful in raising awareness among employers and workers. Early indications are that the vast majority of businesses are meeting their obligation to pay the National Minimum Wage, but not all workers entitled to it are receiving it. The Inland Revenue has made a successful start to enforcement, adopting a pro-active stance towards non-compliance. There are further practical steps which might be taken to increase compliance by raising awareness and improving enforcement procedures.

We have been on the receiving end of substantial pleasure and excitement from people who realised that this piece of legislation does work for them We have been encouraged by the largely positive and common sense approach of most employers who accept that the rates are hardly extortionate and who agree that workers deserve proper financial recognition of their work. The problems of outright non-payment have ... been less than we anticipated.

Yorkshire and Humberside Low Pay Unit Evidence

- 7.1 During the consultation for our first report, workers and employers strongly impressed upon us the importance of compliance and enforcement for the success of the National Minimum Wage. They were particularly concerned about employers at the fringes of the formal economy and in the informal economy who would seek to avoid the minimum wage. A full assessment of the degree of compliance must await further data and evidence, but we are aware from research and evidence that some workers are failing to gain their entitlement. Nevertheless, the overall signs are encouraging.
- 7.2 Official data sources cannot yet be used in any meaningful way to inform our estimate of compliance, particularly as the New Earnings Survey (NES) shows a snapshot immediately after the implementation of the minimum wage, and we know that some employers did not comply straight away. Even in the longer term, official pay data cannot be used as the sole measure of compliance with the National Minimum Wage. Other countries with minimum wages, such as the US and France, do not use pay data as definitive measures of compliance, and it is unlikely that UK pay data alone could ever be used in this way. For this evaluation, we have considered other statistical sources, as well as evidence from our consultation, research and visits.

- 7.3 We commissioned a range of studies to assess the impact of the minimum wage on low-paid workers and whether they experienced any difficulties with compliance. Much of the research – such as those studies conducted by advice agencies, including the Low Pay Units, National Association of Citizens Advice Bureaux (NACAB) and its equivalent organisations in Northern Ireland and Scotland – considered the impact of the minimum wage on low-paid workers generally. For example, the Low Pay Unit (LPU) undertook a before-and-after study of a range of low-paid workers who originally contacted advice lines prior to the implementation of the minimum wage, while the Northern Ireland Association of Citizens Advice Bureaux undertook a questionnaire survey of enquiries made at a number of its offices, supplementing this survey with detailed examination of a sample of case studies.
- 7.4 Some studies were more targeted, considering the effect of the minimum wage on certain types of worker. The Low Pay Network, comprising five Low Pay Units across the UK, undertook research focused on young workers. The research was based on data from nearly eight thousand job vacancies which were collected in two stages, in April and September 1999, nearly two thousand vacancies in Careers Services collected in April, and case study evidence from telephone enquiries. Research by the National Group on Homeworking (NGH) was particularly useful in helping us assess how this very low-paid group had been affected by the minimum wage. Some of our research aimed at specific sectors also considered the impact on certain workers in those sectors. For example, the Gray and Heyes study of the West Yorkshire textile and clothing industries examined the impact of the minimum wage on pieceworkers and homeworkers. The significant fund of information provided by these research studies proved particularly valuable to our assessment of compliance and helped us identify action which might be taken to improve compliance and enforcement.

Low Pay Commission Research

We commissioned the Low Pay Unit to monitor the impact of the minimum wage on a sample of workers across Great Britain who approached the Unit for advice on the legislation. The research, which covered forty-five workers who were paid less than the minimum wage prior to April 1999, included two post-implementation interviews to examine the workers' experiences of the minimum wage. It found that awareness was high and blatant non-payment of the minimum wage was rare, though it identified some examples of infringement of minimum wage and other employment legislation.

Low Pay Unit, 1999.

The Low Paid and the Minimum Wage

Compliance

- 7.5 There is strong evidence that most employers are complying. The LPU (1999) found that approximately one month after the introduction of the wage the overwhelming majority, more than four-fifths, of workers in the case studies examined were being paid the proper hourly rate. These findings were reinforced by evidence from business surveys indicating that large numbers of firms were complying. A Federation of Small Businesses survey (1999) showed that smaller firms, which we indicated in our first report might be more affected by the National Minimum Wage, were complying.
- 7.6 The Inland Revenue helpline statistics included in the Government's evidence show that most calls were to seek information and advice rather than to register complaints. In the first six months to the end of September 1999, the helpline received nearly 84,000 enquiries, but fewer than 3,000 complaints. Similarly, research conducted for us by advice centres indicated that levels of complaint were relatively low. For example, Citizens Advice Scotland's survey of nine bureaux showed that 'NMW cases made up an average of 6 per cent of employment terms and conditions issues raised'. In discussion, the Low Pay Network told us that although the minimum wage queries had considerably increased caseloads, they were significantly overshadowed by enquiries on other employment rights.
- 7.7 We know that some companies did not comply immediately on 1 April, but have done so since. In addition to some highly-publicised cases of delayed compliance, we were told in our meeting with the Youth Hostels Association that because of the lateness of the guidance, it was unable to adapt its pay systems until June, when the minimum wage was implemented with payment of full arrears from April.
- 7.8 In addition, compliance has improved as workers have become more aware of their rights and sought to enforce them. The LPU research showed that in more than three-quarters of the forty-five case studies they examined, workers paid less than the minimum wage in April eventually gained a pay increase, though some had not obtained the increase until they had challenged their employer. Enforcement action undertaken by the Inland Revenue or advice agencies on behalf of workers

has similarly increased the level of compliance since April, as we discuss later in this chapter.

- 7.9 Inevitably, there will have been instances of unwitting non-compliance, especially in less formal employment and in very small businesses, where employers and workers may be unaware of the full implications of the minimum wage. Such cases are symptomatic of the novelty of the National Minimum Wage and they should decrease significantly as the minimum wage continues to bed in and becomes more widely understood.
- 7.10 None of this, however, is a basis for complacency. From our visits, research and discussions with advice agencies, we learned of many workers who are failing to receive their full entitlement. Some are reluctant to tackle their employers about non-payment of the wage, or even to register an anonymous complaint, because they fear reprisal. Such fears are sometimes well-founded.

The Fringes of the Economy

- 7.11 Evidence from trade unions and advice agencies has highlighted cases of non-compliance. We were told that, commonly, non-compliance exists in companies operating at the edges of the legitimate labour market, and particularly in the informal economy. Employers in this fringe economy exploit the most vulnerable workers. Typically, these include people dependent on benefits for their main income and those for whom family commitments, lack of skills or high local levels of unemployment deny them an alternative choice of work. Many are also from ethnic minority groups whose opportunities may be restricted by cultural barriers or outright discrimination.
- 7.12 These sections of the economy are characterised by the flouting of a whole range of legislation. In extreme cases they employ illegal labour. Many clients seeking advice on the minimum wage at Citizens Advice Bureaux, Low Pay Units and similar advice centres were found not to have employment contracts or to be receiving their entitlement to paid holidays and wage slips. The Northern Ireland Association of Citizens Advice Bureaux research reported the following case:

The Leicester City Council Low Pay Campaign and the textile union KFAT held a meeting with a community association, Belgrave Baheno, primarily to attract Asian workers. Most workers attending appeared to have genuine grievances about the minimum wage, but were reluctant to make official complaints. One of the women at the meeting was dismissed after her employer had spotted her on local television attending the meeting.

Leicester City Council Evidence

Client works part-time 20 hours a week approximately, over 2 years, has never had paid/unpaid holidays. No written contract Client receives his wages in an envelope at the end of the week, no statement of any kind included re. national insurance contribution, tax.

Thus one of the unintended advantages of the minimum wage has been to enable agencies to raise awareness of wider employment rights.

- 7.13 Non-compliance with the minimum wage, therefore, follows the established pattern for these areas of the labour market. Information and advice are less likely to reach workers within them, and the vulnerability of such workers makes them reluctant to jeopardise their jobs by challenging their employer or reporting non-compliance.
- 7.14 We received anecdotal evidence of collusion between employers and workers, especially in the informal economy. We heard allegations of both parties conspiring to deal in cash-in-hand payments below the minimum wage because the worker was defrauding the social security benefits system. A study by Warwick Business School indicated that this practice was widespread in some restaurants in Birmingham. A chef alleged that 'most of the people in the restaurant trade ... are signing on at the same time If they are really going to make it on the books [legitimately employed] ... then it's going to be only a very few restaurants that are going to remain open' (Edwards et al., 1999).
- 7.15 The nature of the fringe economy means we are unable to estimate its size or the degree to which workers within it are failing to obtain the minimum wage. This aspect of the economy warrants in-depth research in order to facilitate both a better assessment of its impact on low pay, and the planning of targeted enforcement strategies.
- 7.16 Evidence from a wide range of sources indicated that some employers were exploiting workers' lack of awareness by advising them that they were not eligible because, for example, they were part-timers or they worked in small firms. The research which we commissioned from NACAB reported a range of such cases:

Client works part-time and told by employer that this excludes her from the minimum wage.

Client is currently working for £55 for a 40 hour week. She has been told by her employer that she is not entitled to receive the minimum wage because the firm has less than five employees.

- 7.17 The research and evidence indicate that many ethnic minority workers are particularly at risk of such exploitation. Typical is the ethnic minority worker cited in the KFAT evidence, whose employer attempted to avoid paying the minimum wage by suggesting that piecework was not covered:

For the first 4 weeks I was paid correctly at £3.60 per hour. After this, however, when I saw that my wages were low, I went straight to my boss's office and asked him why my wages were so low as they had never been like this before. My boss replied that I was now working on piecework. On another occasion I was called into the boss's office where I explained that £3.60 is the rule, it was the law, he had to pay me that. But my boss said no, that the factory had a system of piecework.

- 7.18 A frequently reported response to the minimum wage was a unilateral reduction of workers' hours by the employer. In some instances, the worker was required to maintain the same output in fewer hours. The Fawcett Society evidence cited an example of 'someone who cleans an office [who] is now expected to cover the same space in less time to get the same total wages as before'. The survey conducted by NACAB showed that, at the time of implementation, a reduction in hours accounted for 13 per cent of queries they received relating to the National Minimum Wage. But in a later survey, this accounted for just 4 per cent, indicating that reducing hours may have been mainly a transitional adjustment.

- 7.19 Other action reported to us includes consolidation of allowances or similar payments into the basic wage, or loss of paid breaks. Where these actions are taken by agreement, they are legal means of coping with the new legislation. There are instances, however, where reductions in terms and conditions have been introduced unilaterally by employers, in contravention of the National Minimum Wage Act provisions.

'Mrs T... has worked in a cafe for the same employer for 13 years. She was paid £3.45 per hour and has not had a pay rise for over six years. From 1 April she has been paid £3.60 per hour but her weekly hours have been cut from 21.5 to 18.5. She is therefore earning less than before the minimum wage was introduced. She has not taken any action over the contractual changes, even though she was not happy with the situation.'

Low Pay Unit Research

Low Pay Commission Research

We commissioned the National Group on Homeworking to assess the introduction of the minimum wage and its impact on homeworkers. A survey was conducted between April and September 1999, but those who were surveyed before the end of July were contacted again in September. The sample of nearly one hundred homeworkers was drawn from those who contacted the National Group for advice. The research showed that nearly half of those still engaged in homeworking in September were receiving less than £3.60 an hour. Having access to information, advice and support appeared to be the most important factor in ensuring that homeworkers, especially those from ethnic minorities, receive their entitlement to the minimum wage.

National Group on Homeworking, 1999. *Monitoring the Introduction and Impact of the National Minimum Wage on Homeworkers*

Homeworkers

- 7.20 Evidence shows that the minimum wage is making a difference to some homeworkers: research in the West Yorkshire textile industry (Gray and Heyes, 1999) indicated that 33 of the 91 homeworkers surveyed had gained. Nevertheless, substantial numbers continue to be underpaid. The study by the National Group on Homeworking (NGH) found that nearly half of the 66 homeworkers who gave information about their pay were receiving less than £3.60 an hour. The concentration of non-compliance was greater among homeworkers from ethnic minorities: 11 out of 14 were receiving less than £3.60 an hour. These findings must be qualified: the cases in the survey were drawn from workers who approached the NGH or their local homeworking project, so were largely self-selecting. Nevertheless, non-compliance is a major concern for workers from ethnic minority backgrounds and it is important for the Government to ensure that publicity about the minimum wage reaches this group to encourage enforcement action.
- 7.21 Many employers have traditionally considered their homeworkers to be self-employed, and we have been told that more employers have been adopting this practice in order to avoid paying the minimum wage. The research by Gray and Heyes did not indicate that it was widespread: only 2 out of 91 homeworkers had been redesignated as self-employed. The NGH found that 'several homeworkers were asked to sign agreements which stated that they were, or were about to become, self-employed at around the time of the introduction of the national minimum wage' (NGH, 1999). But it also found that where workers were designated as self-employed, they were not necessarily paid less than the minimum wage: more than a third of workers who appeared to have been incorrectly classified as self-employed were being paid at least the minimum wage.
- 7.22 The research projects conducted by Gray and Heyes and the NGH indicate that many employers of pieceworkers were failing to use the written agreements of working hours which are required by the Regulations. Even where 'fair estimate' agreements existed, pieceworkers were at risk of employers manipulating the contents. On our visit to the West Midlands, we were shown examples of agreements which bore no estimate of working hours nor any agreed rate of piecework.

The Regulations require a written agreement specifically to protect pieceworkers against exploitative expectations of output. We believe that as part of the campaign to publicise the minimum wage, the Government should target homeworkers and make it clear that the agreement exists to protect those workers most at risk.

Enforcement

Awareness

- 7.23 In our first report, we suggested that, as far as possible, the National Minimum Wage should be self-enforcing. A high degree of awareness of the National Minimum Wage is a key element in promoting self-enforcement. The Government's publicity campaign accompanying the launch, together with the extensive press coverage which implementation attracted, raised awareness of the minimum wage across a wide audience. In addition, a wide range of bodies including trade unions, trade associations, community groups and advice organisations provided pre-implementation publicity and advice through posters, articles in trade publications and helplines. The post-implementation survey commissioned by the DTI suggested a very high level of awareness of the full rate of the National Minimum Wage among workers and employers. This was supported by research we commissioned: for example, the Low Pay Network reported that one Low Pay Unit found that 90 per cent of people it surveyed were aware of the minimum wage coming into force.
- 7.24 As the minimum wage beds in, it should become a standard feature of the labour market, with wide recognition and compliance. Until then, however, as the impact of the initial publicity fades, awareness might be reduced, and this could affect the level of enforcement by workers of their entitlement to the minimum wage. The profile of the National Minimum Wage must therefore be maintained.
- 7.25 Evidence from visits, and enquiries to the Commission, suggest that while knowledge of the £3.60 rate is high, there is a substantial amount of confusion about the Development Rates and the more detailed rules relating to the National Minimum Wage. For example, we were told by a Training and Enterprise

Low Pay Commission Research

We commissioned three research projects from the National Association of Citizens Advice Bureaux, Citizens Advice Scotland and the Northern Ireland Association of Citizens Advice Bureaux to assess the impact of the minimum wage on clients who sought advice and guidance from the bureaux. The organisations used questionnaire-based data and/or evidence from individual case studies. Given the basis for its selection, the sample inevitably included a large number of cases of underpayment or strategies by employers to avoid paying the minimum wage. But, overall, the researchers found little evidence of poor awareness of the minimum wage and found most approaches to bureaux were to check entitlement and payment in the context of non-payment by employers.

National Association of Citizens Advice Bureaux, 1999. *The Impact of the Minimum Wage on CAB Users.* Citizens Advice Scotland, 1999. *National Minimum Wage Implementation.* Northern Ireland Association of Citizens Advice Bureaux, 1999. *The National Minimum Wage – The Experience of Citizens Advice in Northern Ireland.*

AEKTA is an employment rights agency which represents textile workers mainly, but not exclusively, from ethnic minority backgrounds. The agency was concerned about the lack of understanding among workers of the National Minimum Wage, especially the more detailed aspects. Language difficulties exist, but AEKTA stressed that lack of awareness is not confined to ethnic minority workers.

Low Pay Commission Visit to the West Midlands

Council in the North West of employers who were providing accredited training to NVQ level, but who knew nothing of the Development Rate. In Northern Ireland, the Federation of Small Businesses told us that its members were well aware of the £3.60 rate, but a number of them were unclear about the entitlement of young workers. Throughout our consultation, many organisations representing low-paid workers, especially workers from ethnic minorities, impressed upon us the importance of a high level of awareness about the National Minimum Wage and the criticality of its role in assisting compliance and enforcement.

- 7.26 Unions and advice agencies, particularly those dealing with workers in the textile industry, highlighted the fact that workers from ethnic minorities were frequently unaware of the National Minimum Wage and how it applied to them. Language difficulties present a barrier to some ethnic minority workers attempting to obtain help and information about the National Minimum Wage and other employment rights. This is clearly an issue which needs to be addressed in order to encourage enforcement action. As the TUC highlighted in its evidence,

The Government's publicity drive in the run-up to 1 April was successful in raising awareness of the National Minimum Wage. However, there is a need for ongoing publicity ... targeted at employers and workers in regions and sectors where non-compliance seems to be high; in areas where many workers do not have English as a first language, there should be publicity in other languages.

- 7.27 **We recommend that the Government should continue to publicise the National Minimum Wage widely and, in particular, promote it effectively among the ethnic minority communities.** Publicity should not focus exclusively on the main rate of minimum wage. It should include wider aspects such as the treatment of young people and those undertaking training. In particular, the increase, in June 2000, from £3.00 to £3.20 for young workers should be well publicised. We welcome the Government's recent campaign focused on the Asian communities as an initial step towards the goal of increasing awareness among ethnic minorities, but this publicity must be sustained and supported by the availability of literature and advice in ethnic minority languages.

Advice and Complaints

- 7.28 The Inland Revenue helpline offers guidance on the minimum wage and acts as the initial point of contact for people who wish to register a complaint. Helpline staff are reinforced by a team of officers who can take initial investigative and enforcement action by telephone. Where complaints lead to more detailed investigation, the Inland Revenue has found that most employers comply with the National Minimum Wage after an initial approach. If not, the threat of enforcement action is frequently sufficient to achieve compliance, though in some instances the employer refuses to comply until the point at which a formal enforcement or penalty notice is about to be issued. The Government's evidence cites an example of an employer refusing to comply until the enforcement notice was issued, resulting in his having to pay a total of £17,000 arrears to more than one hundred homeworkers.
- 7.29 As few cases investigated by the Inland Revenue have yet reached employment tribunals or courts, enforcement action has attracted little press or public attention. Several organisations representing workers have argued for greater publicity of enforcement action as a deterrent. The TUC suggested in its evidence that 'the best way of reversing tendencies towards non-compliance in particular areas and sectors is to reverse the expectation that employers can "get away with it" This should include unannounced visits to workplaces, publicity of the NMW and the publicising of successful cases of enforcement'. The publicity given to the first employment tribunal case taken by the Inland Revenue at the end of October was an encouraging start and we look forward to wider and more frequent coverage as the tribunal cases and criminal prosecutions increase.
- 7.30 Other bodies play an important part in enforcement. Research carried out by organisations such as Citizens Advice Bureaux and Low Pay Units indicates that where these organisations have provided advice to the worker, or have intervened on the worker's behalf, a high proportion of cases have resulted in the employer complying. Humberside Law Centre, reporting on the research which we commissioned, stated that it had helped fourteen clients with employment tribunal applications. Three cases had been heard by tribunals, with two having been

decided in favour of the worker. A further six cases had been settled in full by the employer before reaching a hearing. The remaining five were awaiting a hearing, but employers might yet settle. But the following example from NACAB illustrates how a less formal approach than a tribunal application can still be successful:

Client earns £2 an hour When he asked his employer why he did not receive the minimum wage he was told he should be grateful for a job at all and that employees like him did not qualify. Client says that he has been discriminated against because he has learning difficulties. CAB wrote to employer and client received minimum wage immediately.

Service Delivery

- 7.31 While the Inland Revenue has been appointed to investigate complaints and enforce the National Minimum Wage, its remit extends only to cases where the worker has not received the National Minimum Wage. In cases of detriment or dismissal, the worker is referred directly to the Advisory, Conciliation and Arbitration Service (ACAS) for advice, or to the Employment Tribunal Service or the Employment Service to obtain a tribunal application document.
- 7.32 For the complainant, the need to be referred to a separate agency can be confusing and be perceived as poor public service. Several workers' organisations have advocated that the Inland Revenue should represent workers in cases of detriment or dismissal. The Inland Revenue is still getting to grips with employment tribunal procedures and any revisions would be premature. Furthermore, we have serious reservations about the practicality of the Inland Revenue extending its remit to cover areas of employment protection which stray far beyond its core purpose and competence.
- 7.33 There may be scope for some simplification of complaint procedures, possibly by instituting a single initial point of contact for all National Minimum Wage-related complaints. The Inland Revenue and ACAS are working together to handle National Minimum Wage enquiries. From March to the end of August 1999, ACAS handled nearly 9,500 enquiries about the

minimum wage. Almost one thousand of these were referred to the appropriate ACAS office by the Inland Revenue helpline, but also ACAS identified nearly four thousand enquiries as being relevant to the Inland Revenue and advised callers about the Inland Revenue Helpline. The Inland Revenue is in consultation with ACAS about how the two organisations might work more closely together, and we endorse this approach. We appreciate, however, that the unique position of ACAS as an independent arbitration service, rather than as an enforcement body, will preclude any substantial transfer or sharing of responsibilities.

Targeted Enforcement

- 7.34 In their evidence, a range of advisory organisations argued for greater use of targeted inspections and for the Inland Revenue to take cases on behalf of workers. They considered that this would have a significant deterrent effect, and ensure that enforcement would reach companies or sectors where workers were reluctant to act on non-compliance. The GMB in its evidence suggested that ‘there is a need for the Inland Revenue to take more cases on behalf of workforces, in order to overcome the fear which can prevent named workers from taking cases to Employment Tribunal’.
- 7.35 The Inland Revenue has established a model aimed at identifying those sectors and geographical areas where non-compliance is likely to be most prevalent, as well as those types of worker most at risk of non-payment. The model is being used as the basis for targeted enforcement, and this should ensure that resources are used to best effect.

Alternative Approaches

- 7.36 Most other countries rely on an inspectorate to enforce individuals’ cases or pursue employers (see Appendix 7). Experience in the US system demonstrates that enforcement can also be successfully approached on an industry basis. The US enforcement body has made use of top-down approaches in the clothing industry. Its ‘Eradicating Sweatshops’ initiative sought to work in partnership with leading firms in the industry and introduced retailer and manufacturer monitoring programmes. The resultant pressure on retailers to avoid

companies which violated the minimum wage was considered to have a significant effect. Overall, \$12.6 million arrears of minimum wage had been paid. Supplementary actions such as random inspections and publication of violations were significant deterrents to underpayment.

- 7.37 There may be lessons to be learned here for enforcement in the UK. Responsible employers have expressed to us their concern that the minimum wage should be effectively enforced in order to ensure that they are not undercut by those who exploit cheap labour. We believe, therefore, that they may be willing to act in partnership with the Inland Revenue to enforce compliance in their sectors. We suggest that this is a further proposal which the Government should consider for the medium term.
- 7.38 We fully support the work being undertaken by the Inland Revenue to work with third parties, such as Low Pay Units, trade unions and advisory bodies, to enforce the minimum wage. This is only the start of an evolving process and greater emphasis needs to be given to it in the longer term. Evidence from advice bodies working closely with those workers most vulnerable to exploitation and non-compliance emphasised that such workers, especially ones from ethnic minority backgrounds, are reluctant to challenge the employer about compliance or register a complaint with the Inland Revenue helpline. These workers are often more comfortable seeking help from a locally-based advice agency or community association than dealing with an official enforcement agency. We consider that this may offer an opportunity for overcoming workers' hesitancy to report non-compliance.
- 7.39 **We recommend that the Government should fund a small number of community-based pilot projects in areas where workers are likely to be at most risk of non-compliance.** The projects should enable local advice agencies and trade unions, working closely with the Inland Revenue, to reach into areas of the labour market or communities where workers are most reluctant to report non-compliance. The aim should be to build workers' confidence in the effectiveness of enforcement procedures and thereby encourage greater levels of reporting of non-compliance. As for all enforcement, it will be important to maintain confidentiality under such schemes.

Conclusion

7.40 Current evidence suggests that the vast majority of employers are complying with the National Minimum Wage. The relatively low level of complaints about non-compliance is encouraging, but not a basis for complacency. There are clearly still substantial numbers of workers being paid less than the minimum wage. Increasing awareness of the National Minimum Wage is important with publicity targeted at communities in which awareness is lowest. The role of the Inland Revenue should be kept under review because the success of the minimum wage lies in compliance, and effective enforcement is key to compliance.

8 Conclusion and Next Steps

The National Minimum Wage has been introduced successfully, with no significant adverse effects on the economy. Large numbers of low-paid workers have benefited, particularly women, and the National Minimum Wage, together with the Working Families' Tax Credit, will benefit low-income families. Low-paying sectors have adapted well. This success needs to be built on. Levels of compliance should be improved, and the minimum wage will need to be updated.

- 8.1 Nine months have passed since the National Minimum Wage was introduced. We knew our recommendations were cautious, and we were confident that businesses would cope and many workers would benefit. Nevertheless, the introduction of a National Minimum Wage is a major Government intervention in the labour market, and we have been impressed by the smoothness of its introduction. There is certainly progress to be made in compliance and enforcement, but our conclusion at this early stage is that the introduction of the minimum wage has been a success.
- 8.2 From the best available data and statistical advice our assessment is that well over one and a half million workers were due to benefit from the introduction of the National Minimum Wage in April this year. From all the evidence we have – our research, visits, written evidence, the work of the Inland Revenue and early data – our judgment is that a substantial majority of these have already seen their wages rise because of the new legislation. Early indications are that these wage rises have been considerable, with average increases in hourly earnings of around a third.
- 8.3 For low-earning families, the combined impact of the National Minimum Wage and other tax and benefit changes – in particular the introduction of the Working Families' Tax Credit – will mean a substantial rise in family income. Because the Working Families' Tax Credit was only introduced in October of this year, more time is needed to assess its impact. But it,

together with the minimum wage, should prove a powerful tool in tackling in-work poverty.

- 8.4 As we predicted in our first report, working women have benefited most from the minimum wage: two-thirds of beneficiaries are women and, of these, two-thirds are part-time workers. Indeed, the minimum wage has been instrumental in bringing about the sharpest increase in women's wages in relation to men's for almost a decade.
- 8.5 Young people have seen their pay rise because of the minimum wage, while their employment prospects have not been damaged. There appears to have been no adverse impact on recruitment or retention in the New Deal for young people. Labour market evidence shows that the increase to £3.20 in June 2000 for young workers already announced by the Government is manageable.
- 8.6 The Government specifically asked our advice on 21 year olds. We recommend that 21 year olds should be entitled to the full adult minimum wage rate. The data, our research and the evidence are all clear. The vast majority of 21 year olds are already receiving at least the full minimum wage. And there is no evidence that employers are substituting older or younger workers for this group. Our judgment is that including 21 year olds in the full minimum wage entitlement would not damage their employment opportunities, and would have no adverse effects on individual sectors or the economy as a whole.
- 8.7 Although a large number of workers have benefited, our findings show that there has been no detrimental impact on the economy, with around 0.5 per cent being added to the national wage bill, and with no measurable impact on overall employment. In many low-paying sectors, there has actually been expansion in employment.
- 8.8 Its impact on specific sectors has varied. Where sectors are particularly price sensitive, such as in certain parts of the hospitality and small retail sectors, the main impact has been on profits. In sectors such as hairdressing and activity holidays, the minimum wage will have caused some price rises. Some companies, particularly in cleaning and security, have found that on long-term contracts which were won on the basis of

lowest costs, profits have been seriously eroded, and will not be restored until the company re-contracts.

- 8.9 But in most sectors we were told that the impact of the minimum wage was manageable, and less than that of other economic and regulatory changes. Although some firms have had difficulties adjusting, overall none of the low-paying sectors have experienced significant damage from the minimum wage. And we were pleased to see evidence that in many cases businesses had responded by improving productivity.
- 8.10 Although the majority of businesses are complying with the new legislation, not all those workers who are entitled to the minimum wage are receiving it. While total compliance may never be achieved, this must be the Government's aim. The initial advertising campaign was very effective in raising awareness of the minimum wage, and this has helped make the measure largely self-enforcing. But some employers are paying less than the statutory minimum and, indeed, are not meeting their obligations in many areas of employment law. The Inland Revenue has made a good start in enforcement, but we would like to see more community-based support and enforcement to ensure that those most vulnerable in the workforce receive their full entitlement.
- 8.11 The successful introduction of the National Minimum Wage is a major achievement. But the minimum wage has to be durable. Its substantial benefits will not be sustained over time unless it is periodically updated. As we said in the conclusion to our first report, 'our recommendations for introducing the National Minimum Wage offer progress in raising the wages of the lowest paid, with a prudent approach that will avoid adverse effects on business and the economy. This must be a continuing process with periodic updating to ensure that the benefits of the National Minimum Wage continue to be felt well into the new millennium.'
- 8.12 We recognise that the Government should want to see the first-ever minimum wage settle in before making decisions about the future. But we are clear that there should not be a long gap between the first and second setting of the rate, so that the benefit of the initial rate is not lost. Our original advice to Government was that the rate of £3.60 should be increased

to £3.70 in June 2000, and that to do so would have no adverse economic consequences. We remain confident in this advice. It is supported by all the available economic evidence, including the current buoyant labour market, and the way firms have adapted to the initial rate.

- 8.13 In our consultation for this report both employers and workers' organisations raised the question of re-setting the level of the minimum wage. All employers stressed the importance of a reasonable lead-in time for implementation. The evidence for this report shows that when employers can plan ahead, pay increases can be managed in such a way as to benefit both workers and businesses. Some employers were wary of regular uprating, fearing that this could lead to automatic, index-linked rises, irrespective of economic circumstances. Many small businesses, however, told us that they would prefer to manage predictable uprating with small, regular increases rather than larger *ad hoc* increases. Businesses relying on long-term contracts said that annual uprating would be better for planning purposes. Unions in general favoured regular re-setting based on the Commission's recommendations. Almost all evidence we received supported the process of social partnership in recommending the design and level of the wage.
- 8.14 When we investigated other countries' minimum wages, we considered their mechanisms for re-setting the levels. There is a range of approaches, which can be grouped broadly into those countries – the vast majority – where there is an annual re-setting based on some form of indexation (often with additional recommendations from government or a commission), and those where re-setting is less frequent with the level established through political agreement. But there are a number of options within this range. Regular uprating does not preclude using judgment rather than simple indexation; less regular uprating could still aim to avoid purely political judgments. Certainly, the more regular the re-setting, the smaller the change is likely to be, and thus easier for businesses to manage.
- 8.15 The Commission acknowledges that the introduction of the UK minimum wage might be too recent for the Government to make decisions on what longer-term mechanisms might be put

in place for re-setting it. A further re-setting might be necessary before we can be confident what level and frequency of changes are right for the UK economy. Nevertheless, if it is not updated it will cease to be a useful labour market tool, and cease to provide any material benefit for low-paid workers. The more belated the adjustment, the greater the disruption to companies. During 2000 there will be further data, and a full picture of the impact of the minimum wage on the economy and low-paid workers, from which to make sensible recommendations on a future rate.

- 8.16 This report has covered the immediate introduction of the minimum wage. In the longer term, to ensure that we thoroughly understand the workings of the minimum wage in the economy, we should set in train detailed studies of specific labour market issues to supplement current information. We would like to study in greater depth the patterns of low pay in particular groups, including ethnic minorities – on whom information is very limited – and part-time workers. We need to undertake further work on compliance and develop a better understanding of the informal economy. We hope to look in greater detail at the interaction of tax and benefits for low-paid workers, and to consider how the employer manages the minimum wage alongside the administration of other employment rights. The participation of young people in education, training and work is changing dramatically; we need to look broadly at these changing patterns to understand how the minimum wage should work with other rights and protections to ensure that young people have the best possible preparation for adult work and life. Such information should inform future recommendations.
- 8.17 The UK's first National Minimum Wage has had a successful introduction. Through further consultation, research, and analysis, and through discussion and debate, the Commission hopes to contribute to its successful future.

Appendix 1

Consultation

We are grateful to all the people and organisations that helped us by providing oral and written evidence, and by organising or participating in visits and meetings. All organisations which participated, and gave consent for us to publish their names, are listed below according to the nature of their contribution.

Oral Evidence to the Commission

Brewers and Licensed Retailers Association
 British Activity Holiday Association Ltd.
 British Hospitality Association
 British Youth Council
 Confederation of British Industry
 GMB
 Hairdressing Employers Association
 National Hairdressers' Federation
 National Union of Knitwear, Footwear and Apparel Trades
 National Union of Students
 Scottish and Newcastle Retail Ltd.
 Trades Union Congress
 Trades Union Congress Youth Forum
 Transport and General Workers Union
 Union of Shop Distributive and Allied Workers
 Unique Pub Co. Ltd.
 UNISON
 YHA (England and Wales) Ltd.

Written Evidence to the Commission

Advisory Committee for Disabled People in Employment and Training
 Age Concern England
 Aims of Industry
 Alliance of Independent Retailers
 ALVA (Association of Leading Visitor Attractions)
 Angel Human Resources plc
 Association of British Travel Agents Ltd.
 Association of Charity Officers
 Association of Chartered Certified Accountants
 Association of Convenience Stores
 Association of Direct Labour Organisations
 Association of Disabled Professionals
 Association of Independent Museums Ltd.
 Association of Licensed Multiple Retailers
 Bass plc
 Bell Social Work Agency, Dorset
 Birmingham Chamber of Commerce and Industry
 Biscuit, Cake, Chocolate and Confectionery Alliance
 Bradshaw, Professor J, Department of Social Policy and Social Work, University of York
 Brewers and Licensed Retailers Association
 British Activity Holiday Association Ltd.
 British Actors' Equity Association
 British Agricultural and Garden Machinery Association

British Apparel and Textile Confederation
British Chambers of Commerce
British Footwear Association
British Horseracing Board Ltd.
British Hospitality Association
British International Freight Association
British Printing Industries Federation
British Red Cross Society
British Retail Consortium
British Sandwich Association
British Security Industry Association
Broadcasting, Entertainment, Cinematograph and Theatre Union
Burfield and Co. (Gloves) Ltd., Somerset
Business in Sport and Leisure Ltd.
Business Services Association Ltd.
Campaign Against Domestic Violence
Camping and Caravanning Club
Caravan Club Ltd.
Carers National Association
Catholic Bishops' Conference of England and Wales, Committee for World of Work
Cefn Lodge Nursing and Residential Home, Neath Port Talbot
Charity Commission for England and Wales
Chartered Society of Physiotherapy
Cherubs Day Nurseries, Nottinghamshire
Cheshire County Council Social Services
Choice Hotels Europe
Church Action on Poverty
Cinema Exhibitors' Association
Cleaning and Support Services Association
Communication Workers Union
Confederation of British Industry
Convention of Scottish Local Authorities
Cook J A, West Yorkshire
Cornwall Rural Community Council
Country Landowners Association
Countryside Agency
Crofters Commission
Dairy Industry Federation Ltd.
Dorking Riding Centre Ltd., Surrey
Edwards, Professor P, Gilman M, Warwick Business School, University of Warwick; Ram, Professor M, De Montfort University
Electrical Contractors' Association of Scotland
ELITE Supported Employment Agency Ltd., Mid Glamorgan
Employers' Organisation for Local Government
Engineering Employers' Federation (EEF)
Engineering Employers' Federation, Northern Ireland Association
English Heritage
Equality Commission for Northern Ireland
Fawcett Society
Federation of Licensed Victuallers Associations
Federation of Small Businesses
Federation of Small Businesses (Northern Ireland)
Federation of Small Businesses (Scotland)
Federation of Small Businesses (Wales)
Food and Drink Federation
Further Education Development Agency
General Assembly of the Church of Scotland Committee on Church and Nation
Glasgow Chamber of Commerce

GMB	MIND (The National Association for Mental Health)
Golden Sunset Homes Trust, Suffolk	Multiple News Association
Greater Manchester Low Pay Unit Ltd.	National Caravan Council Ltd.
Hairdressing Employers Association	National Centre for Volunteering
Heatherwood and Wexham Park Hospitals Trust, Berkshire	National Council for One Parent Families
Her Majesty's Government	National Farmers' Union (NFU)
Highlands and Islands Enterprise	National Farmers' Union of Scotland
Homeless Network	National Federation of Fisherman's Organisation
Hotel Victoria, Suffolk	National Federation of SubPostmasters
Hull and Humber Chamber of Commerce, Industry and Shipping	National Hairdressers' Federation
Hull CityVision Ltd.	National Housing Federation
Independent Healthcare Association	National Institute of Economic and Social Research
Industrial Services Group (ISG), Devon	National League of the Blind and Disabled
Industrial Therapy Trust (North Somerset) Ltd.	National Pharmaceutical Association Ltd.
Institute of Directors	National Schizophrenia Fellowship (Scotland)
Institute of Payroll and Pensions Management	National Trainers Federation
Joseph Rowntree Foundation	National Union of Knitwear, Footwear and Apparel Trades
Kathrina Fashions Ltd., Belfast	National Union of Rail, Maritime and Transport Workers
Kingfisher plc	National Westminster Bank plc
Kingston upon Hull City Council	NCVO (National Council for Voluntary Organisations)
Labour Relations Agency, Northern Ireland	Nevis Bank Hotel Ltd., Highland
Leather Producers' Association	Newspaper Society
Lincolnshire Association of Registered Care Homes (LARCH)	Newtake Newsagents, Devon
Local Authority Caterers Association	NHS Confederation
Low Pay Unit	North East Chamber of Commerce Trade and Industry
Low Pay Unit (Northern Ireland)	Northern Ireland Amusement Caterer's Trade Association
Meetings Industry Association	Northern Ireland Childminding Association
MENCAP (Royal Society for Mentally Handicapped Children and Adults)	Northern Ireland Council for Voluntary Action
Methodist Church	Northern Ireland Hotels Federation
	Organisation for Economic Co-operation and Development
	Pembrokeshire County Council

Pre-school Learning Alliance	Tourism South and West Wales
Producers Industrial Relations Services Ltd.	Trades Union Congress
Professional Association of Nursery Nurses	Training Consortium, East Sussex
Public and Commercial Services Union	Transport and General Workers Union
RADAR (Royal Association for Disability and Rehabilitation)	Traprain Consultants Ltd., East Lothian
Reed Personnel Services plc	Union of Independent Companies
Refugee Council	Union of Shop Distributive and Allied Workers
Relate Derby and District	UNISON in conjunction with the British Youth Council
Religious Society of Friends (Quakers), Quaker Home Service	UNISON Northern Ireland Region and the Northern Ireland Anti-Poverty Network
Religious Society of Friends (Quakers), West Kent	United Care Homes Association, Lincolnshire
Restaurant Association	United Kingdom Home Care Association Ltd.
Retail Motor Industry Federation Ltd.	Universities and Colleges Employers Association
Retail Trade Alliance	Unquoted Companies' Group
Rural Community Network (Northern Ireland)	VOICES (Voluntary Organisations Involved in Caring in the Elderly Sector)
SCOPE (for people with cerebral palsy)	West Midlands Low Pay Unit
Scottish Agricultural Wages Board	Whitbread plc
Scottish and Newcastle Retail Ltd.	White Horse Child Care Ltd., Wiltshire
Scottish Association Master Bakers	Williams T, Kent
Scottish Chambers of Commerce	Working Men's Club and Institute Union Ltd.
Scottish Engineering	YHA (England and Wales) Ltd.
Scottish Executive	Yorkshire and Humberside Low Pay Unit
Scottish Grocers' Federation	
Scottish Licensed Trade Association	
Scottish Media Group (Services) Ltd.	
Scottish Trades Union Congress	
Scottish Trades Union Congress Youth Committee	
Shaw Trust	
Southern Council for Outdoor Education	
Speedwell Enterprises, Berkshire	
Swallow Hotels Ltd.	
Theatrical Management Association Ltd.	

Visits and Meetings

England

Access Training Ltd., Tyne and Wear
Adventure International, Cornwall
AEKTA Project, West Midlands
Allied Domecq Retail Ltd.
Allied Leisure plc
Arundell Arms, Devon

Ashdene Service Station, East Sussex	Grand Hotel, Tyne and Wear
Association for Supported Employment	Hands Cleaners Ltd., Leicestershire
Association of Convenience Stores, Hampshire	Hereford and Worcester Chamber of Commerce, Training and Enterprise
Association of Residential Care Homes, Cornwall	Hotel Bristol, Cornwall
Bass Leisure Retail	Hull and East Riding Chamber of Commerce, Industry and Shipping
Bells Stores, Cleveland	Hull Area Business Advice Centre
Birmingham Chamber of Commerce and Industry	Humberside Law Centre
Brambles Foods Ltd., Cleveland	Industrial Finishing Specialists, Tyne and Wear
Business Link Cumbria (Eden and South Lakeland)	Industrial Mission, Humberside
Business Services Association Ltd.	Institute of Chartered Accountants, North West
Busways Travel Services Ltd., Tyne and Wear	James Cropper plc, Cumbria
Calemcal Ltd., Cumbria	Jobcentre (Employment Service), Humberside
Classic Coaches Ltd., County Durham	J T Catering, Cleveland
Commission for Racial Equality	Kingston upon Hull City Council
Cornwall and Devon Careers	Knights End Farm Training Centre, Cambridgeshire
Cornwall Care for the Elderly	Leicester African-Caribbean Business Association
Cornwall County Council	Leicester City Council
Cornwall Rural Community Council	Leicester Outworkers Campaign
Daycare Trust	Lincolnshire TEC
De Montfort University	Lumley Castle Hotel, County Durham
Dorset Chamber of Commerce	Manchester TEC
Durham City Coaches Ltd.	Mansfield Brewery plc
Durham Travel Services Ltd.	McDonald's
Engineering Employers' Federation (EEF)	Mill on the Brue, Somerset
Enesco European Giftware Group Ltd., Cumbria	Milverton Community Playgroup, Somerset
English Lakes Hotels Ltd., Cumbria	National Group on Homeworking
Federation of Small Businesses	National Union of Rail, Maritime and Transport Workers, North East Area
Federation of Small Businesses, Eastern Region	Newlife Cleaning Systems Ltd., Tyne and Wear
Fledglings Nursery, Greater Manchester	Northern Foods plc, Humberside
GMB, Midlands and East Coast Region	
Graham Austin Training, Greater Manchester	

North Lakes Hotel, Cumbria
NTL Teesside
PAS (Grantham) Ltd., Humberside
Perkins Frozen Foods UK, Cumbria
Pre-school Learning Alliance
Remploy Ltd.
Rex Hotel, Tyne and Wear
RH Patterson and Co. Ltd., Tyne and Wear
Shap Wells Hotel, Cumbria
Skegness College of Vocational Training
Society of Mary and Martha, Devon
Somerset College of Arts and Technology
South Tyneside College
Spar, Dorset
St. Loye's College for Training Disabled People for Employment, Devon
Studio Cadcam Ltd., Avon
Superchoice, Dorset
T and S Stores plc, West Midlands
Technical Academy Northumberland Ltd.
TEDCO (Tyneside Economic Development Company)
Thurlestone Hotel, Devon
Transport and General Workers Union, Leeds Region
Tredragon Hotel, Cornwall
Tyneside Cinema
Tyneside TEC
Union of Construction, Allied Trades and Technicians, North East Region
Union of Shop Distributive and Allied Workers, North Eastern Division
UNISON, Yorkshire and Humberside Region
Village Retail Services Association, Dorset

Walnut Tree Hotel, Somerset
W Brewin and Co. Ltd., Leicestershire
Wellington and District Pre-school Learning Alliance, Somerset
West Midlands Low Pay Unit
Westmorland Motorway Services, Cumbria
White Horse Child Care Ltd., Wiltshire
Whitley Bay Hoteliers Association, Tyne and Wear
Yorkshire and Humberside Low Pay Unit

Northern Ireland

Balcas Ltd., Fermanagh
Coleraine Enterprise Agency
Federation of Small Businesses
Fermanagh District Council
Institute of Personnel and Development (Northern Ireland)
J L Grant and Co., Belfast
Killyhevlin Hotel, Fermanagh
Lodge Hotel, Coleraine
Low Pay Unit
Magherabuoy House Hotel, Coleraine
Mulholland and Bailie Ltd. Manufacturing, Belfast
Northern Ireland Economic Council
Northern Ireland Hotels Federation
Savile Row Shirt Company, Coleraine
S D Kells, Fermanagh
Worknet, Employment and Training Services, Belfast

Scotland

Ballachulish Hotel, Highland
Borders College
Botterills Convenience Stores, South Lanarkshire
Database Direct Ltd., Highland

David Sands, Perth and Kinross

ENABLE, Scottish Society for the Mentally Handicapped,
Glasgow

Federation of Small Businesses

Gold Star Cleaning Services, Aberdeen

Highfield Group Ltd., Edinburgh

Highlands and Islands Enterprise

Lochaber Ltd., Highland

Lochcarron of Scotland, Scottish Borders

Prince's Trust – Scotland

Sco-Fro (Lochaber) Ltd., Highland

Scottish Borders Enterprise

Scottish Enterprise

Scottish Licensed Trade Association

Scottish Trades Union Congress

Wales

Capper and Co. Ltd., Rhondda, Cynon, Taff

Federation of Small Businesses, North Wales and
Chester Region

GRW Security Services Ltd., Swansea

Heritage Park Hotel, Rhondda, Cynon, Taff

NACAB (Wales)

Neath Citizens Advice Bureau

Neath Port Talbot County Borough Council

OCS Cleaning Wales Ltd., Cardiff

Qualifications, Curriculum and Assessment Authority
for Wales

Welsh Development Agency

Welsh Mountain Zoo, Conwy

Welsh Tourist Board

Appendix 2 Official Data Sources

- 1 While research and consultation are invaluable, official data also have an important role to play in assessing the overall impact of the National Minimum Wage. Earnings data will provide an estimate of the number of people who benefited directly and any changes in wage costs. Other labour market data will be used to measure the impact on employment, unemployment and productivity.
- 2 We highlighted the problems with official earnings data in our first report. Since then we have continued to work with the Office for National Statistics (ONS) to improve the quality of available information. The ONS has made significant progress, but the results of its most recent work will not be available until 2000. In any case, the latest data reflect a period very soon after implementation and so it is too early to provide a precise estimate of the impact of the minimum wage.
- 3 This appendix provides a summary of the early post-implementation data and delivers our first cautious assessment of the number of beneficiaries and the cost of the minimum wage. The appendix also includes a discussion of which data should be studied in the medium and long term to provide a fuller evaluation of the impact of the minimum wage.

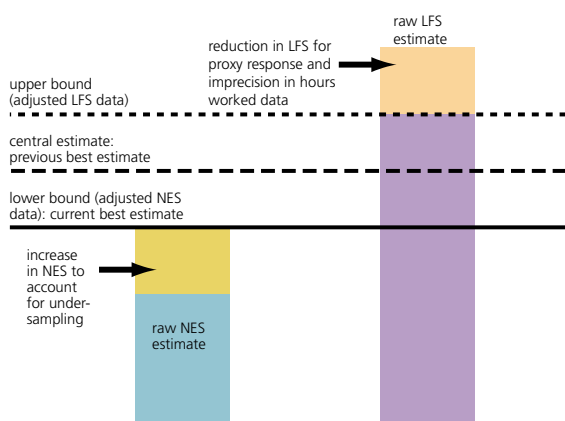
Appraisal of Earnings Data

- 4 We summarised the official sources of earnings data in the first report and in the Low Pay Commission Occasional Paper 1, *Developing Official Data on Low Pay* (1999). We concluded, following advice from ONS, that the appropriate sources to use in measuring the impact of the minimum wage on earnings were the New Earnings Survey (NES) and Labour Force Survey (LFS).
- 5 The NES is the primary source of earnings data in the UK and provides very detailed distributional information for industry sectors, specific occupations and small areas. Data are precise, as they are collected directly from payroll records. In addition, the NES, has a longitudinal element which provides information about the changes of individuals' earnings over time.
- 6 The LFS is the main source of labour market data in the UK and can provide detailed cross-sectional information for a large number of social characteristics. The quarterly frequency of the survey allows short-term changes to be tracked and earnings patterns in seasonal employment to be highlighted.
- 7 But neither the NES nor the LFS alone provides an accurate measure of low pay. The NES is based broadly on a sample of individuals who are part of the Pay-As-You-Earn (PAYE) tax scheme. Consequently, a large number of low-paid employees are excluded. Earnings and hours estimates from the LFS are less precise, particularly those from proxy respondents. This leads to a degree of bias in derived hourly earnings estimates. As a result, estimates of low pay incidence are too high.
- 8 In order to provide a single estimate of low pay incidence, the ONS developed a methodology that adjusted data in the two main surveys. The LFS estimate of low pay incidence was reduced to correct for the under-statement of hourly earnings caused by proxy response and the general imprecision in estimates of hours worked. The NES sample estimate was supplemented by adjusted LFS data for employees below the PAYE threshold.

- 9 This methodology, which is summarised in Figure A2.1, produced a reduced range of estimates. The ONS advised that, until further development work was carried out, the centre of the range should be taken as the best point estimate of low pay incidence. We used this advice in our first report to estimate the likely number of beneficiaries of the minimum wage and the related costs. Current ONS advice is that the best estimate of low pay incidence is now more likely to be towards the bottom of the adjusted range. Hence the number of beneficiaries is also likely to be lower than originally estimated.

Figure A2.1

Summary of ONS Methodology for Low-pay Incidence Estimation



- 10 The methodology may be subject to further revision pending the results of ongoing development work in the ONS. A major component of this work is the analysis and quality assurance of a new question in the LFS which asks respondents directly about their hourly rate of pay. Together with a parallel project to examine the level of measurement error in the current LFS hourly earnings data, this should improve the precision of existing LFS hourly earnings estimates. A larger project to regress all LFS data to revised population estimates should be completed some time in 2000. There is also some development work being undertaken on the NES data, including an examination of the proportion of the NES sample which is paid below the PAYE threshold but not used in current low pay estimates. This work should

provide a better measure of the actual level of NES coverage. The ONS is also looking at a methodology to correct additional bias in the NES caused by non-response. We discussed the need for further developments in Occasional Paper 1 and thoroughly support all of the ongoing work. It is important to have reliable complementary information from both employer and household sources if low pay is to be fully understood.

Estimating the Number of Workers Entitled to Higher Pay

- 11 The last estimate of low pay incidence on the ONS methodology for a period prior to the introduction of the minimum wage is for Spring 1998. It is likely, however, that in the period leading up to April 1999 some employees would be brought above the minimum threshold as a result of natural wage growth, either through a pay settlement or by moving jobs. In the first report we took a cautious approach and assumed that any natural wage growth would be in line with target underlying inflation of 2.5 per cent. Hence we thought that an estimate of employees earning below £3.50 per hour (£2.90 for 18–21 year olds) in Spring 1998 represented a better assessment of the likely number of beneficiaries. This assumption, together with the ONS advice at the time to use the mid-point of its adjusted range, gave an estimate of 1.9 million employees directly entitled to higher pay.
- 12 There is some evidence that natural wage growth, even among the low paid, was faster than inflation. But recent acceleration in wage growth for the low paid may be due to anticipatory action by employers. Generally, employment in low-paying sectors continued to grow in the months leading up to April; this may also have increased the number of potential beneficiaries. On balance, our original assumption appears reasonable. But the latest ONS advice to use the lower bound of its adjusted range of low pay incidence estimates, produces a revised estimate of the number of workers directly entitled to higher pay of 1.7 million.

- 13 We noted above that the ONS methodology may be subject to further revision. To give us some idea of the extent of any possible revisions to the existing low pay estimates we looked more closely at the current estimates. We took as our starting point the latest ONS advice, which points towards the raw NES data being a better measure of low pay incidence than was indicated at the time of our first report.
- 14 The current methodology attempts to correct for bias in the NES caused by the under-sampling of low-paid employees by replacing data for all those employees below the PAYE threshold with LFS data. But almost a tenth of the NES sample is actually made up of employees who are paid below the PAYE threshold. The exact proportion of employees represented by the NES sample frame is difficult to estimate. The LFS, however, suggests that 17 per cent of employees earned less than the PAYE threshold in Spring 1999 compared with the NES estimate of 10 per cent. The difference between these two estimates suggests that the NES misses just 7 per cent of all employees.
- 15 While some employees above the PAYE threshold may also be outside the scope of the NES if they are in less formal employment, we demonstrated in Appendix 2 of our first report, NES and LFS estimates of low pay incidence above the PAYE threshold are much closer. We also discussed in Occasional Paper 1 that there may be additional bias in the NES caused by greater non-response in low-paying industries and small businesses. As part of its ongoing development work the ONS has developed a methodology which compensates for this bias by grossing the NES data to estimates of employment in the full sample frame. Preliminary results show that the effect of this bias is small.
- 16 It seems possible, therefore, that the true range of estimates of low pay incidence extends below the current ONS lower bound. With a large proportion of low-paid employees still outside the scope of the NES, however, the true level may well be within the existing range. We conclude that the most likely outcome of any ONS work will be a revised range of estimates which represent a downward shift in the existing range. It is to be hoped that any development work will also lead to a narrower range, thereby reducing the uncertainty surrounding the level of low pay in the UK. Pending this work, the current ONS advice that the best estimate of low pay incidence is towards the lower bound of its existing range is reasonable. Our assessment is that the current best estimate of employees directly entitled to higher pay as a result of the minimum wage is around 1.7 million.
- 17 Our own most recent work, and ONS advice, leads us to confirm that the NES is a more reliable source of low pay data than previously thought. In the short term this allows us to be confident that the April 1999 NES data are a reliable guide to the initial impact of the minimum wage. Looking towards the future, it is clear that the data on employees below the PAYE threshold are a potentially rich source of information which could be better used. We welcome the ONS initiative to look more closely at those employees in the NES who are below the PAYE threshold. We know that many are included because they work for large employers who supply data for all employees with relevant National Insurance numbers. But these represent only a small proportion of all sub-PAYE employees in the NES. It is important that we understand how other low-paid employees are captured in the NES. It is possible that the introduction of the Working Families' Tax Credit, and perhaps the minimum wage itself, may in time actually increase the coverage of NES as more people are brought into the administrative tax system.

Estimating Compliance

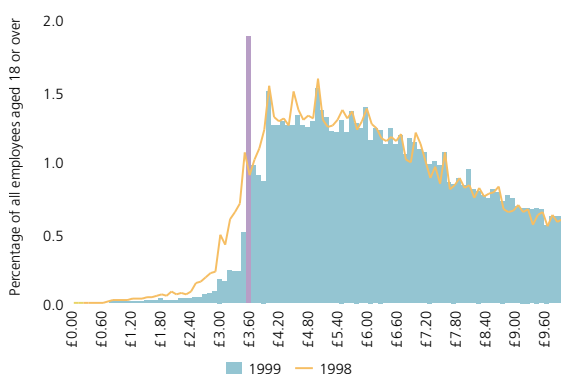
- 18 There is not yet an ONS estimate of low pay incidence for a period entirely post-minimum wage implementation. The estimate for Spring 1999 shows a fall of 700,000 in the number of employees earning less than the minimum rates. But this figure covers March to May which straddles the date of the introduction of the minimum wage. In addition, the results of the ONS development work will not

be known until 2000. In this section we examine the latest NES and LFS data and summarise the initial findings.

- 19 The 1999 NES collected data for the pay period which included 14 April and, for the majority of employees, it should represent the first full pay period following the introduction of the minimum wage. Indeed, the NES shows a significant shift in the hourly earnings distribution. The adult minimum is now clearly seen to be the modal wage. In all, the proportion of the sample earning below the minimum rates in the NES fell by two-thirds in the year to April 1999, although some of this will be due to natural wage growth.

Figure A2.2

NES Hourly Earnings Distribution, April 1998 and 1999



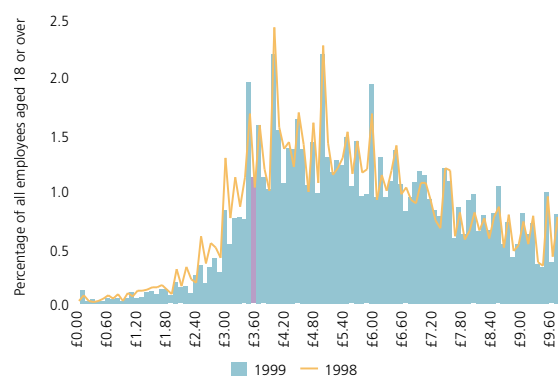
Source: NES, April 1998, 1999

- 20 The latest LFS data from the summer period (June to August 1999) should be clear of the majority of implementation effects. But as Figure A2.3 shows, while there appears to have been some shift in the distribution since last year, it is much less marked than in the NES data. There is little evidence of a minimum wage effect. This is in direct contrast to the evidence we have gathered as part of our research and consultation programmes. It is possible that the lack of movement in the LFS data may be a lag effect in the data caused by respondents taking time to adjust to new pay arrangements or hours. There has also been continued growth in low-paying industry employment which may have

increased the number of employees at the bottom of the distribution. Future quarters' data may provide a clearer picture. For this report, however, we note the current ONS advice to use the lower bound of its adjusted range places less weight on the LFS data. We conclude that there are problems with using the current derived LFS hourly earnings data to measure the impact of the minimum wage.

Figure A2.3

LFS Hourly Earnings Distribution, Summer 1998 and 1999



Source: LFS Summer, 1998, 1999

- 21 In any case, imprecision in earnings and hours estimates have always made it difficult to draw conclusions from the LFS about numbers or proportions earning below precise monetary thresholds. We thus welcome the ONS work to estimate measurement error in the LFS and the introduction of the new hourly rate question which appeared first in the Spring 1999 LFS. Together with the work to regress the LFS data to revised population estimates, these developments should make the LFS a more reliable source of information.
- 22 For this report we noted that the latest ONS advice points towards the raw NES data being a better measure of low pay incidence than was previously thought. This is confirmed by our own research. Hence, we consider the 1999 NES to be the best source of post-implementation earnings data currently available. The first NES to be completely

- free of implementation effects, however, will not be published until Autumn 2000. Until then it is difficult to make any precise estimates about compliance levels. Even so, early signs are encouraging.
- 23 In Spring 1998, ONS estimates show that there were 22.9 million employees aged 18 or over. In Paragraph 14 we noted that the NES could cover over 90 per cent of these employees. The 1998 NES showed that around 4 per cent of the raw NES sample earned less than the deflated minimum rates. Hence we calculate that the NES sample frame represents around 900,000 employees directly entitled to higher pay as a result of the minimum wage.
- 24 The 1999 NES showed that the proportion of employees in the sample earning below the minimum wage rates had fallen by two-thirds from the 1998 level. Taking into account natural wage growth, we estimate that this shows around half a million employees represented by the NES sample had benefited directly by mid-April. We can also identify a large number of individuals who were paid below the minimum wage in 1998 and who were also present in the 1999 survey. Of these, 75 per cent are now being paid the minimum wage. This suggests a higher level of compliance than the main survey. Unfortunately, we do not have any information about those employees who left the sample between 1998 and 1999. But many will re-enter the sample in 2000 and it will be possible to provide a better assessment. We consider this panel data to be extremely important in evaluating the impact of the minimum wage.
- 25 We estimate that around 800,000 employees who were directly entitled to higher pay may be outside of the NES sample frame. These employees are more likely to be in marginal employment; they are also more likely to be the victims of non-compliance. Early results from the LFS show that there has been little movement in earnings for these employees, although we are uncertain about the quality of these data. It is probable, therefore,
- that overall compliance in April was less than the proportion indicated by the NES.
- 26 Our work suggests, however, that the number of workers benefiting directly from the minimum wage is now substantially higher than indicated by the April 1999 NES data. For some employees the data may partly relate to March and, for others, may not fully incorporate pay settlements awarded on or around 1 April. In addition to some high profile cases of delayed payment, we know of other employers who did not implement the minimum wage until later in the year. Compliance has also improved as employee awareness has increased. The Government evidence outlines how compliance has improved as enforcement procedures have bedded down and research shows intervention by advice organisations has led to compliance in some individual cases. A large number of employees outside the NES sample frame, therefore, will also have seen wage increases to at least the level of the minimum wage. The NES also offers some evidence that, in general, early compliance levels were relatively uniform. The fall in the proportion of NES employees below the PAYE threshold who also earned less than the minimum wage was equivalent to the overall fall of two-thirds.
- 27 Remember also, that not all employees aged 22 or over are entitled to the full minimum wage. The minimum wage for workers on accredited training schemes for the first six months of a new job with a new employer is £3.20 per hour. In addition, part of the cost of accommodation for live-in employees can be offset against the minimum wage. Because these employees cannot be separately identified in either the NES or the LFS, the data will always show a non-negligible proportion of employees being paid below any minimum wage rates.
- 28 These are just some reasons why official earnings data cannot be used as precise measures of compliance. The data are collected for purposes other than minimum wage enforcement. The LFS, as a household survey, is also subject to a large degree

of imprecision. Even the NES will be subject to some degree of measurement error. During the operation of the Wages Councils the NES showed a substantial number of employees below the agreed rates, only part of which could be explained by non-compliance. It is likely, therefore, that, even after revision to incorporate ongoing development work, the ONS data for 2000 will still show a large number of employees earning less than the minimum wage rates. This should not be interpreted as an equivalent level of non-compliance. We note, for example, that official earnings estimates in the United States and France show significant numbers of employees paid below the minimum wage, yet compliance is considered close to universal in both countries.

- 29 In summary we conclude that the total number of employees directly entitled to higher pay was smaller than originally forecast and that compliance is not universal. Our own research leads us to believe that a current best estimate of the total number of employees entitled to higher pay is around 1.7 million. It remains too early to provide an accurate assessment of compliance levels.

Costing the Minimum Wage

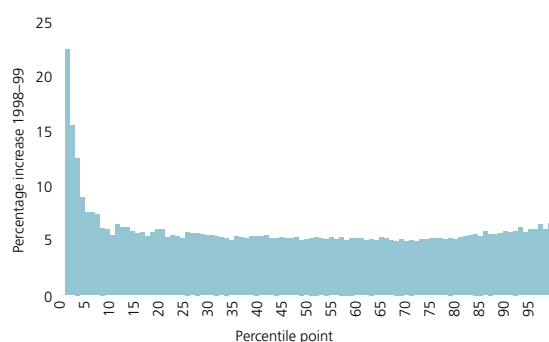
- 30 In addition to our original estimate of the number of likely beneficiaries in our first report, we used the revised ONS estimates of low pay incidence to calculate that the potential direct cost of the minimum wage would be 0.6 per cent of the UK wages bill.
- 31 The number of employees directly entitled to higher pay is lower than we originally forecast, and compliance is not universal. Hence the direct cost of the minimum wage so far is less than our original estimate of the potential effect. Our original calculation used a cautious assumption that earnings would grow only as fast as inflation. Because average earnings growth over the last two years has been larger than inflation the current wage bill is slightly larger than we had forecast. The overall wage bill has also grown as a result of continued employment growth and there is

evidence of a reduction in hours worked by affected employees. All these factors mean that the direct cost of the wage bill is further reduced from our original estimate.

- 32 It is possible to provide some assessment of the direct and indirect cost of the minimum wage using official data. The NES, for example, demonstrates that knock-on effects appear to have been relatively small. From Figure A2.4 we see that wage growth declines to around the lowest decile and then picks up again slightly to the lowest quintile before flattening out. The value of the lowest quintile on the NES is just under £5.00 per hour. We note from our own postal survey of firms in low-paying sectors (see Appendix 5) that only a fifth said they would raise pay for employees above £3.60 to restore differentials reduced by the minimum wage. Of these, three-quarters would not raise pay above £5.00. Thus at the level of the whole economy, we consider any effect the minimum wage has had on differentials beyond £5.00 to be negligible.

Figure A2.4

Percentile Growth, NES Hourly Earnings, April 1998–1999



Source: NES, April 1998, 1999

- 33 To provide an estimated cost of the minimum wage on the wage bill so far, we used the NES to calculate an alternative wage bill which may have reflected earnings growth in the absence of a minimum wage. We reduced the increases for those employees in the lowest quintile of the 1998 NES distribution to reflect the average increases for this group over the previous five years. This produced a

wage bill 0.3 per cent lower than the actual 1999 figure, adjusted for changes in employment and hours. While this may be considered too low due to undersampling of low-paid employees in the NES, we outlined in Appendix 2 of our first report why the NES provides a reasonably accurate measure of wage bill costs. So, even allowing for under-sampling in the NES, we calculate that the total cost of the minimum wage by April 1999, including direct and indirect effects, was around 0.4 per cent of the total wage bill. Compliance has increased since April and so the direct cost of the minimum wage will also have grown. Employment has also continued to grow in low-paying industry sectors. The precise effects are uncertain but our judgment, together with early NES data, suggests that the total cost of the minimum wage so far is around 0.5 per cent of the current wage bill.

Average Pay Rises Resulting From the Minimum Wage

- 34 We estimated in our first report that the average pay rise for affected employees would be around 30 per cent. This calculation was based on the revised ONS distribution of pay below the minimum wage. But the raw NES and LFS show similar figures.
- 35 It is not straightforward to measure the actual average pay rise for those directly affected. As before, pay increases will be a mixture of natural wage inflation and minimum wage effects.

Published NES figures are also difficult to interpret. Lowest decile figures, for example, refer to the earnings level under which 10 per cent of the sample fall, rather than the average earnings of the bottom 10 per cent. In any case, as Figure A2.4 shows, the largest increases were for employees earning well below the lowest decile figure. Further analysis shows, however, that there were some significant earnings increases among the very lowest paid. For example, average earnings of part-time employees in the bottom 5 per cent of the distribution rose by 30 per cent in the year to April 1999.

- 36 The nature of the NES allows us to calculate actual pay rises for individuals who appeared in both the 1998 and 1999 samples. Moreover, it allows us to calculate the average pay increase for those employees in both surveys who were earning less than the minimum rates in 1998. Over half of low-paid employees in the 1998 sample remained in the NES in 1999. Of these, over three-quarters are now being paid at least the minimum wage. Table A2.1 shows the average increase for the matched sample of employees who were below the minimum wage rates in 1998. These figures may include incremental pay awards for some employees and regular annual pay rises in addition to increases arising directly from the minimum wage. They do not necessarily indicate similar rises in weekly earnings.

Table A2.1

Increases in Hourly Earnings for Those Below Minimum Wage Rates in April 1998			
	Percentage now receiving at least National Minimum Wage	Percentage increase in mean hourly earnings 1998–99	Percentage increase in median hourly earnings 1998–99
Full-time male employees	68	37	25
Full-time female employees	73	42	15
Part-time male employees	76	24	22
Part-time female employees	78	28	13
All employees	75	31	18

Source: NES matched sample, April 1998, 1999

Future Use of Official Data in Minimum Wage Evaluation

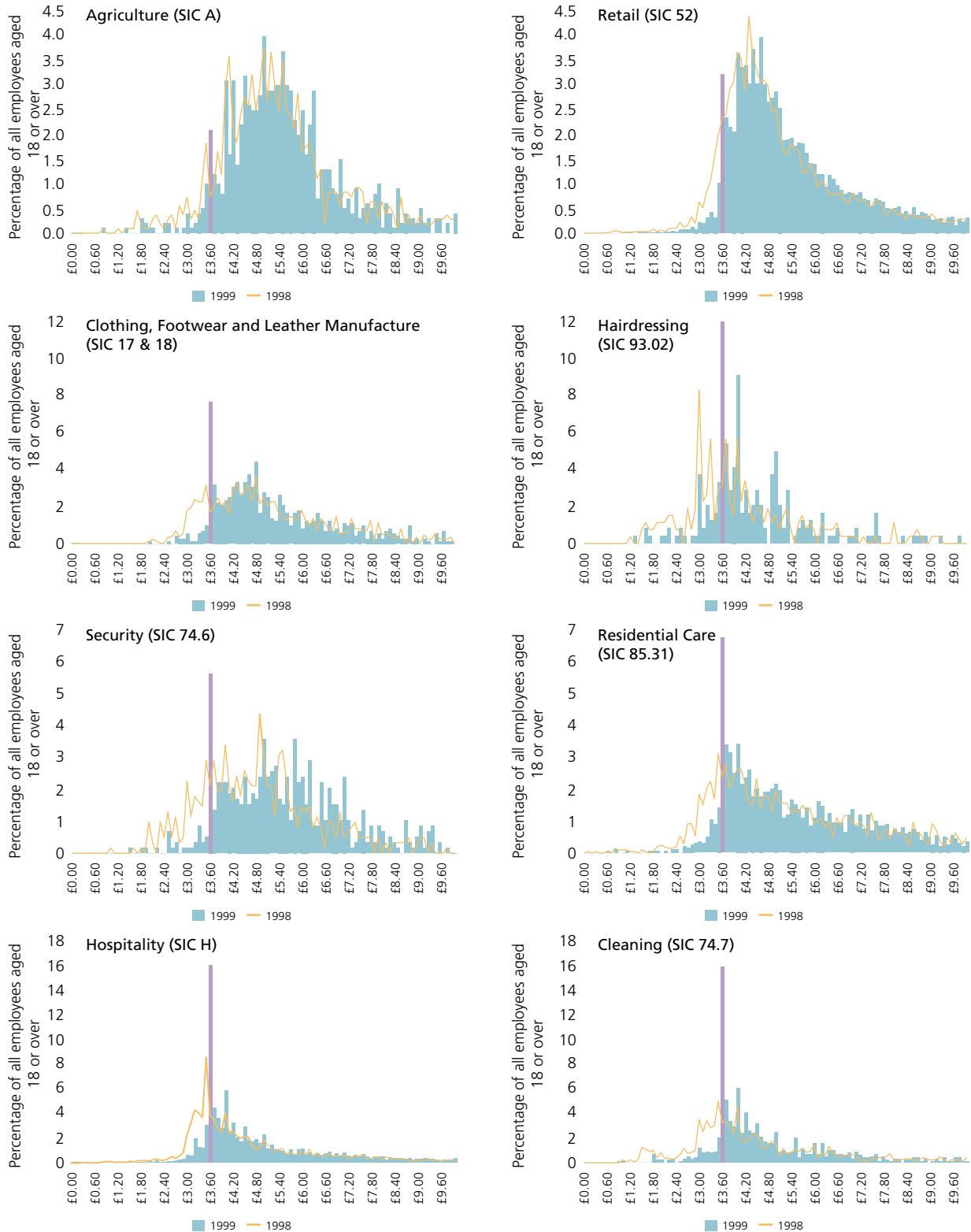
- 37 Currently, the primary interest in official data in measuring the impact of the minimum wage is to estimate the number and profile of workers who were directly affected. The focus of current development work is to improve estimates of low pay. But in the longer term, official data will provide a wide range of analyses which are equally important in providing a full assessment of the impact of the minimum wage.
- 38 In this section we outline some of the labour market and other official data which are likely to be key to the monitoring process in the future. We also present time-series analyses for some key indicators. Most of these are likely to be dominated by external factors but should be followed to check for any possible minimum wage effect. The latest data only reflect a period shortly after the introduction of the minimum wage and can be considered as setting the baseline for future analyses. In some cases, the precise baseline figure may not be in April. There will have been some anticipatory action before then which means that in some cases the baseline date may be earlier. On the other hand, delays in compliance will result in effects taking longer to come through. Where possible the time series are presented from 1984 which represents the first year of the annual LFS (now quarterly) and covers a full economic cycle.

Earnings

- 39 It is instructive, especially in international comparison of minimum wages, to examine how minimum wage rates compare to median earnings. There is still some uncertainty in the data and we do not know exactly how the UK rate compares. But the NES is likely to offer a reasonable guide, particularly in relation to full-time earnings. In April 1999 the NES shows that £3.60 is equivalent to 40 per cent of full-time male median hourly earnings and 43 per cent of all full-time hourly earnings. These figures do not, however, take into account the definition of the minimum wage, which excludes certain earnings components. If calculated on a similar basis, the minimum wage would represent a slightly higher proportion of any median figure.
- 40 Our report demonstrates the importance of the NES in examining the impact of the minimum wage on low-paying sectors, and a summary of industrial hourly earnings distributions is also presented in Figure A2.5 (overleaf). The LFS permits some industrial analyses, but there are inconsistencies in classification between the two surveys and the NES is considered more reliable, particularly at the detailed level. Occupational and geographical classifications are more consistent in the two surveys, but the larger sample size of the NES again means that it should generally be preferred.

Figure A2.5

Hourly Earnings Distribution in Low-paying Sectors



Source: NES, April 1998, 1999 (Note different scales on each horizontal pair of charts)

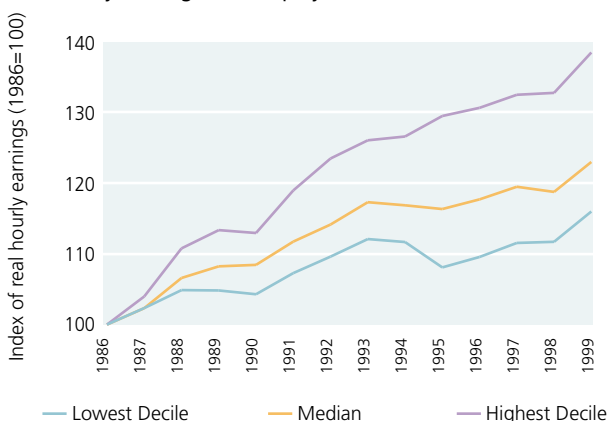
41 The nature of the NES sample frame, in which the majority in the sample are surveyed in consecutive years, also means that it offers reliable time-series information (Figure A2.6). In particular, the NES can be used to provide longitudinal information about the same individuals over a period of time. This information can be linked to other sources, such as JUVOS unemployment records, to give work histories. This could provide an important insight into the employment effects of the minimum wage. We see this as an important area of research in the coming years.

42 The NES also provides detailed information about the components of pay. This is important when examining the pay structures of the low paid. We used this information extensively in the Low Pay Commission Occasional Paper 3, *Pay Structures and the Minimum Wage* (1999) and have updated much of the material in Appendix 4.

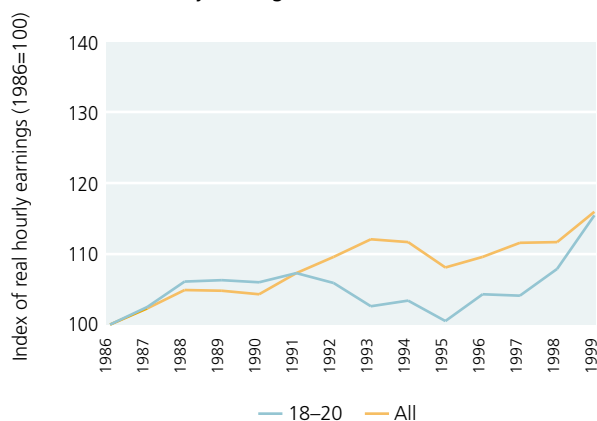
Figure A2.6

Hourly Earnings Growth, 1986–1999

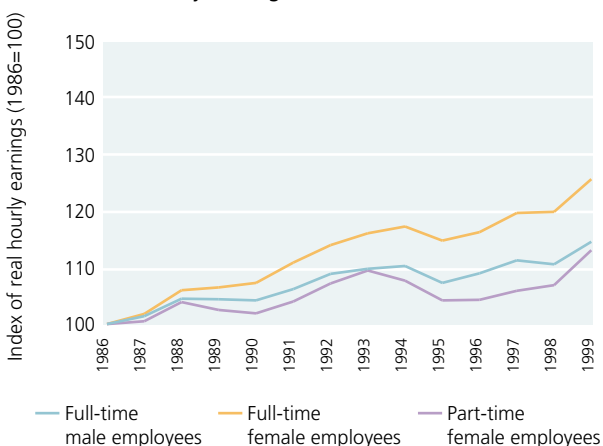
Real Hourly Earnings – All Employees



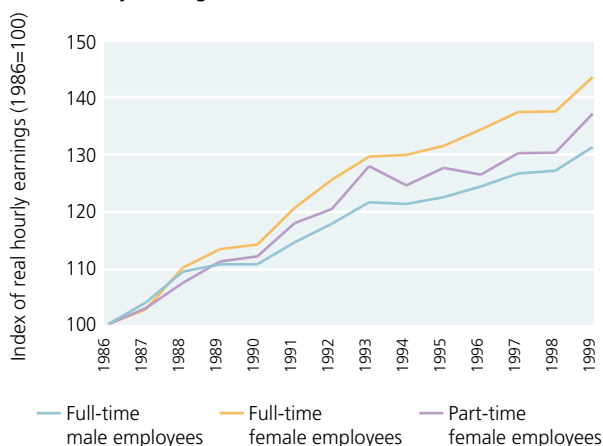
Lowest Decile Hourly Earnings



Lowest Decile Hourly Earnings of Men and Women



Mean Hourly Earnings of Men and Women



Source: NES

- 43 While there appear to be some problems in using the LFS to examine earnings movements around precise monetary thresholds, the LFS can still serve as a useful alternative to monitor changes in the earnings distribution. In addition, because it is conducted quarterly, it can provide useful short-term indications of earnings movements. The LFS is the only source of information about a large number of demographic and labour market characteristics and their role as earnings determinants. For example, it has data on participation in education or training and qualification levels which are of particular concern when examining the earnings of young people. The LFS also allows lone parents and ethnic minority workers to be identified and, together with other household surveys, will perform an important role in monitoring the impact of the minimum wage on their income levels.
- 44 Outside the NES and LFS the main source of earnings data in the UK is the Average Earnings Index (AEI). It is not possible to extract information on low-paid individuals from the AEI but the series does provide the most timely indicator of earnings movements. It is also possible to examine earnings movements in some key low-paying sectors. The series has recently undergone a fundamental review process which has improved the quality of available information.

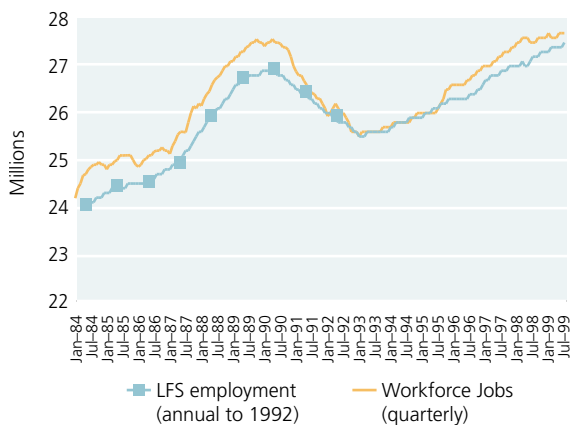
Employment

- 45 As with earnings, there are two principal sources of employment information: the LFS and employer surveys (Workforce Jobs series). The two sources measure different things. The LFS measures principally the number of people in employment, while the employer surveys count the number of jobs in the economy. The LFS also provides a measure of the number of people with second jobs, which can provide an alternative estimate of jobs. The ONS advises that the LFS provides a better idea of the extent of work being performed in the UK. The LFS is the only source of detailed information about social and labour market characteristics and the main source of information on self-employment and homeworking. As for earnings, however, the employer surveys provide a more accurate industrial breakdown than the LFS.
- 46 There are a number of time series of interest when examining the impact of the minimum wage on employment. Employment levels provide the easiest means of examining trends in growth, for example, in different industry sectors. But overall employment levels, particularly among different age groups, are affected by population changes. Hence it is also of interest to examine employment rates, the proportion of the population in employment. Similarly, for industry employment performance it is useful to analyse the share of total employment in each sector.
- 47 Rather than look at overall employment levels, interpretation of which is complicated by the increasing proportion of part-time jobs, it is useful to examine the total number of hours worked in the economy. The main source of this information is the LFS. We have already noted that estimates of hours worked are subject to precision problems, but these problems are less important when examining trends rather than levels. The NES also measures paid hours of work but, because it only refers to a particular week in April, it does not pick up many important seasonal patterns, for example, in retail where hours may increase near to Christmas, and hospitality where hours will increase over the summer months. A number of different employment series are presented at Figure A2.7.

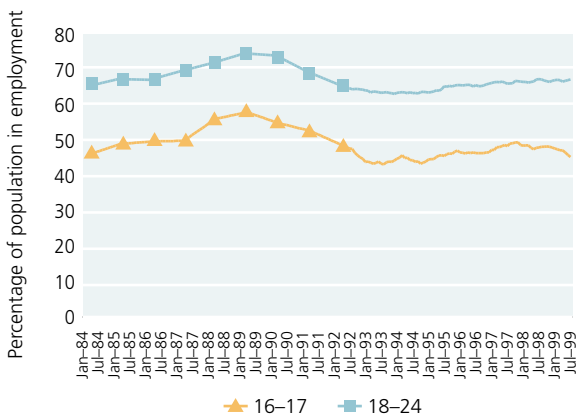
Figure A2.7

Patterns of Employment, 1984–1999

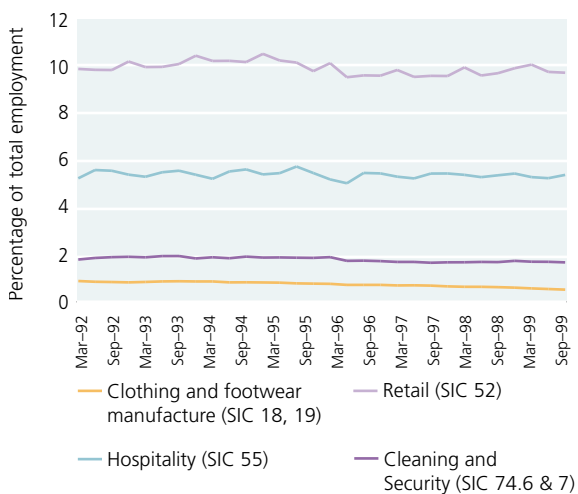
Employment: LFS and Workforce Jobs



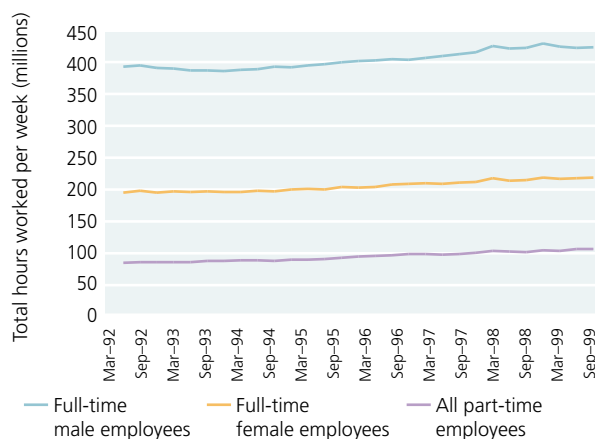
Employment Rates for Young People



Employment Share of Low-paying Sectors



Total Hours Worked Per Week



Source: NES

Unemployment

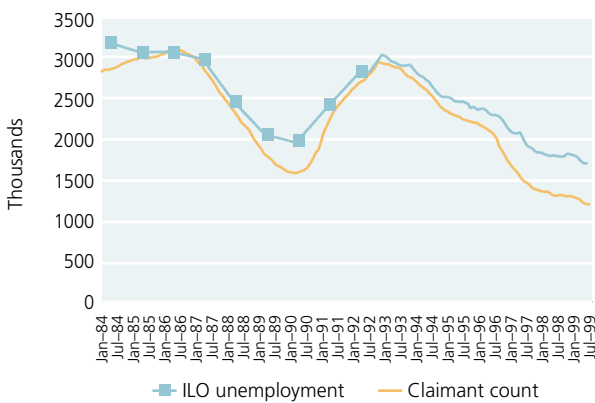
48 The ONS preferred headline measure of unemployment at national and regional level is the LFS measure, based on the International Labour Organisation's (ILO) definition. The alternative measure, the claimant count, consists of all people who are claiming unemployment-related benefits. The ILO estimate provides a more complete measure of unemployment, especially for women. It is also better suited to international comparison. The claimant count is more timely, and can provide very detailed analysis by, for example, industry and occupation in last job and for very small areas.

49 In the context of the minimum wage, unemployment data for different age groups are most likely to be of interest. As with employment, it is useful to examine both unemployment rates and shares to allow for population changes. It is also possible that the minimum wage may improve work incentives. The monitoring of activity rates is thus worthwhile. We noted earlier that the linking of panel unemployment and earnings data will provide important research material. A number of unemployment series are shown in Figure A2.8.

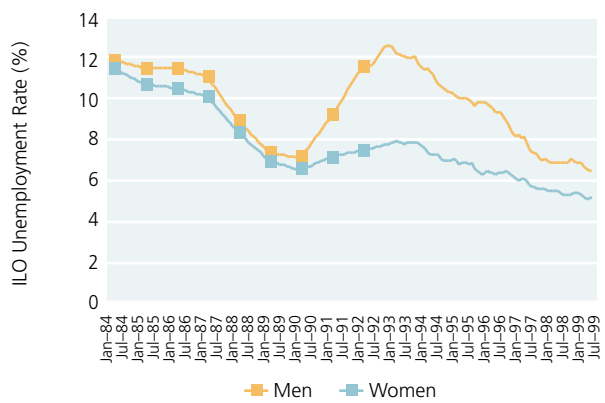
Figure A2.8

Patterns of Unemployment, 1984–1999

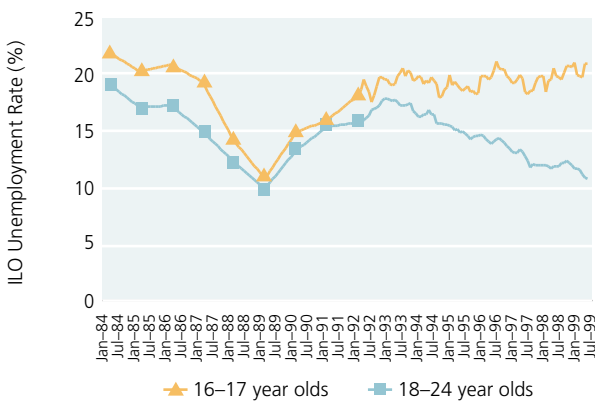
Claimant Count and ILO Unemployment



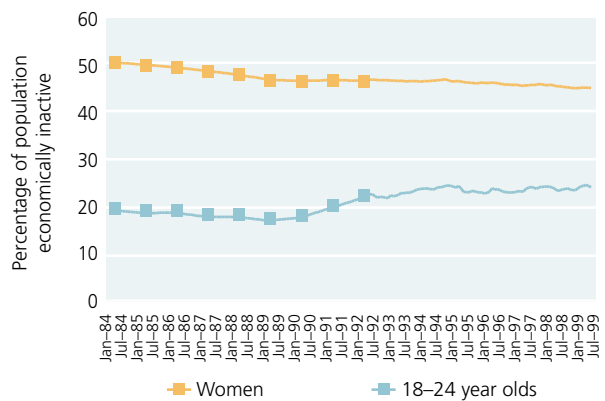
ILO Unemployment Rates for Men and Women



ILO Unemployment Rates for Young People



Inactivity Rates of Women and Young People



Source: LFS (except Claimant Count)

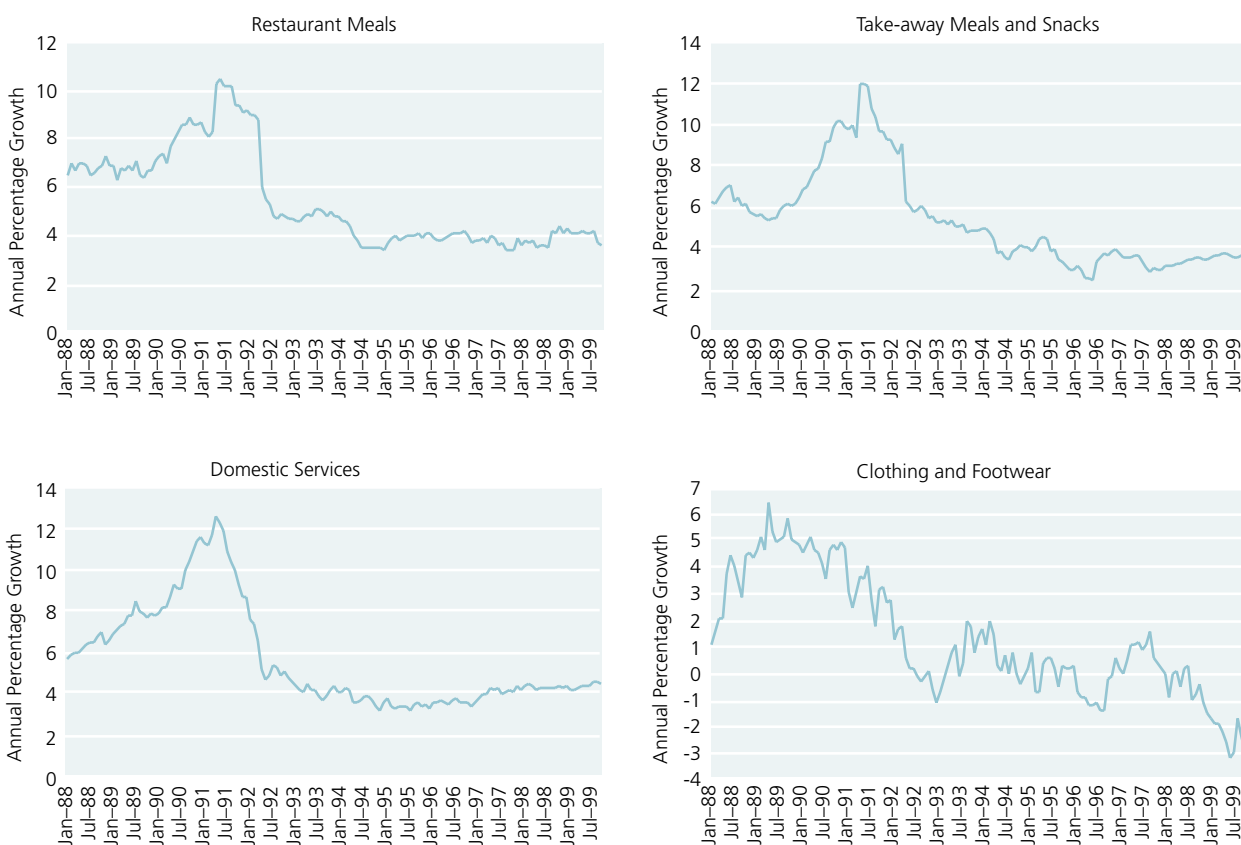
Prices

50 The key indicator of inflation in the UK is the Retail Prices Index. This timely and comprehensive series measures the change in the prices of goods and services bought for the purpose of consumption by the vast majority of households in the UK. The general index includes virtually all types of household spending. It is possible that, if the minimum wage increases income significantly for certain households, spending on certain items will

51 Changes in the prices of goods and services produced by low-paid sectors may also offset changes in labour costs. Hence it is of interest to examine price trends in areas such as hairdressing and take-away meals. Figure A2.9 shows recent trends in prices for a number of relevant products.

Figure A2.9

Retail Price Growth, 1988–1999



Source: Retail Prices Index, ONS

- 52 ONS also publishes detailed estimates of changes in producer prices in the manufacturing sector. Recently the amount of information available about service-sector prices, for example, prices of contract cleaning and security, has improved and this is likely to be of more interest when examining the impact of the minimum wage.

Sampling Errors

- 53 All estimates from sample surveys such as the NES and LFS are subject to a degree of survey error. This further increases the uncertainty surrounding estimates from these surveys. Sampling variability also affects estimates of change as well as estimates of levels. Typically, quarterly changes in LFS variables are small and have wide confidence limits, so it is often difficult to assess the direction of any change or whether there has been a change at all. This is important in measuring changes in, for example, employment or unemployment among the specific groups of workers most likely to be affected by the minimum wage. Many effects of the minimum wage on the labour market will be smaller than the uncertainty in the data. A more detailed discussion of the effects of sampling error is contained in our Occasional Paper 1.

Conclusion

- 54 The full impact of the minimum wage will take some time to show in the official data. But, in the longer term, these data will help to provide a measure of the overall effects of the legislation. Many of the effects will be dynamic and complex and it is important that official statistics are robust. The earnings data are particularly important. Ongoing development work to improve the quality of both the NES and LFS will give more reliable estimates of the level and make-up of low pay in the UK. These will provide a better guide to the impact of the minimum wage.

Appendix 3

The National Minimum Wage and the Tax and Benefits System

- 1 One of the Government's major aims is to increase labour market participation by improving incentives to work. As we highlighted in our first report, while the National Minimum Wage is a significant step towards improving the incomes of low-paid workers, it should not be considered in isolation. It is part of a package of wider measures, such as the introduction of the Working Families' Tax Credit and the reform of National Insurance, aimed at improving support for low-paid families and thus making work pay.
- 2 This appendix sets out briefly how the tax and benefits system currently operates and describes the measures set out in the 1999 Budget which will take effect over the next two years. It then considers the effect of the National Minimum Wage and the tax and benefits system on improving the incomes of the low paid and increasing incentives to work.
- 3 Income tax is currently levied at a starter rate of 10 per cent on earnings which exceed the personal tax allowance, and then at rates of 23 per cent and 40 per cent respectively as earnings increase (see Table A3.1). While married couples and certain individuals, such as blind people, are entitled to an additional allowance, tax liability for most single low-paid workers starts when their earnings reach £83 per week or £4,335 per year.

Income Tax

Table A3.1

Income Tax Allowances and Rates, 1999–2000	
Tax Allowances	Annual Allowance
Personal allowance	£4,335
Married couple's allowance (allowable in addition to the two personal allowances applicable to a couple)	
Additional personal allowance (allowable where the individual is single but has a child, or where one member of a couple is ill and unable to work)	£1,970
Widow's bereavement allowance (allowable for the year of bereavement and the following year)	
Blind person's allowance	£1,330

Notes: Since April 1994, the married couple's allowance, additional personal allowance and widow's bereavement allowance have attracted a fixed rate of tax relief against the overall tax liability. This is 10 per cent for 1999–2000. Its maximum worth is £1,970 x 10 per cent = £197.00 per year which is deducted from the tax due. The value of each allowance is a maximum: it is only available where the individual has sufficient tax liability to use the full allowance.

Higher rates of personal and married couple's allowances apply for those aged 65–74 and 75 years and over, though these are subject to capping for high-income tax payers.

Rate of Income Tax	Annual Taxable Income Bands
10 per cent	up to £1,500
23 per cent	£1,501 – £28,000
40 per cent	Over £28,000

Source: HM Treasury

- 4 The reduction in the starting rate of income tax from 20 per cent to 10 per cent from April 1999 is in line with a Government commitment to reduce the tax burden on low-paid workers. The lower starter rate has the greatest impact on the lowest paid: 2.3 million people have had the tax bill on their earnings halved and over 1.7 million of these are low-paid workers. In addition, 300,000 people will have been taken out of the tax system as their income is below the tax threshold.
- 5 From April 2000, the 23 per cent basic rate of tax will be reduced to 22 per cent. But for some workers the effect will be offset to a certain extent by accompanying measures, such as removal of the married couple's allowance for people aged under 65 and of tax relief on mortgage interest payments. In April 2001, however, a new Children's Tax Credit will be introduced for families with at least one child. The credit will be payable to about 4.5 million families and will be worth up to £416 per year, substantially more than the £197 married couple's tax relief.

National Insurance Contributions

- 6 Changes to align the National Insurance and income tax systems, which were announced in the 1998 Budget, started to take effect in April 1999. The aims of these changes are to reduce the tax and National Insurance burden on the lowest-paid workers and, by helping to reduce the cost of employing workers, to encourage employers to create job opportunities for workers in this earnings group.
- 7 An employee is not liable for National Insurance Contributions (NICs) until earnings reach the 'lower earnings limit' of £66 per week. The rates of contribution which apply on earnings above this level are detailed in Table A3.2. Prior to April 1999, an employee had no liability for NICs until weekly earnings reached the lower earnings limit, but once that point was reached, contributions of 2 per cent then became payable on the first £64 as well as at 10 per cent on earnings between £64 and £465 per week. The abolition of the 2 per cent entry rate and the raising of the lower earnings limit means that all employees earning £66 per week and above are £1.32 per week better off, but proportionately greater gains go to the lowest paid.

Table A3.2

National Insurance Contributions, 1999–2000		
Total Weekly Earnings In Employment for Which National Insurance Liability Exists	Employee's Contribution	Employer's Contribution
0 – £65.99	Nil	Nil
£66.00 – £83.00 (£66.00 is termed the <i>lower earnings limit</i>)	10%	Nil
£83.00 – £500	10%	12.2%
Over £500	Nil	12.2%

Source: HM Treasury

Notes: Liability for National Insurance Contributions exists only where the earnings in that employment reach the lower earnings limit. Thus, where an individual has two jobs, paying £45 and £70 per week respectively, liability for NICs exists only on the earnings of the second job.

These rates apply where the worker belongs to the State Earnings-Related Pension Scheme (SERPS). If the worker is contracted out of SERPS into an occupational pension scheme, the employee's contribution is reduced to 8.4 per cent and the employer's contribution to 9.2 per cent. In addition, an employer rebate of 3 per cent on earnings between £66 and £83 is paid to the scheme. Slightly different rebate levels apply where the worker is contracted out into a money-purchase scheme.

- 8 Further changes are planned to assist low-paid employees. The lower earnings limit will be raised to £76 per week from April 2000, and in April 2001 it will be fully aligned with the single person's income tax allowance (projected to be £87 per week). This is designed to improve work incentives: it will particularly help lower-paid employees who earn too little to pay income tax, but are still liable for NICs. The measure will remove around a million employees, of whom nearly 800,000 will be women, from National Insurance liability, though some may choose to make voluntary contributions to maintain entitlement to social security benefits.
- 9 The employer does not become liable for NICs until the employee's earnings reach £83 per week – the level of the personal allowance for income tax purposes – but contributions are then levied at 12.2 per cent on earnings above £83.
- 10 For employers, the NIC burden will be reduced for workers earning up to £460 per week. Overall, it is estimated that employers will save more than £600 million in NICs in 1999–2000. In addition, administration will be eased as the single rate of 12.2 per cent removes the distortions which occurred in the previous system. Employers will benefit further from a cut in the rate of NICs to 11.7 per cent from April 2001.

In-work Benefits

Working Families' Tax Credit

- 11 It was announced in the 1998 Budget that, from October 1999, the Working Families' Tax Credit would replace Family Credit as the main source of in-work support for low-paid working families in which the main earner works for sixteen hours or more a week. The structure of the Working Families' Tax Credit, which is shown in Table A3.3, is similar to that of its predecessor, but both the earnings threshold, above which the credit is reduced on a tapered basis, and the taper itself are more generous than those which applied for Family Credit. And by enabling working families to retain the full value of maintenance payments, the Government aims to improve further the work incentives for poorer families.

Table A3.3

Structure of Working Families' Tax Credit		
Credits		£ Per Week
Basic credit (one payable per family)		52.30
Credits for each child	0–10 years	19.85
	11–15 years	20.90
	16–18 years	25.95
Disabled child credit		21.95
Extra credit for 30 hours work		11.05
Childcare Tax Credit, 70 per cent of:		
up to £100 childcare cost for one child:	maximum credit	70.00
up to £150 childcare cost for two or more children:	maximum credit	100.00
Taper		Percentage
Amount of credit withdrawn as a percentage of every £1 by which net income exceeds £90 per week.		55

Source: HM Treasury

Note: From April 2000 the credit for a child under 11 years will be equalised with that for a child over 11 years.

12 The Working Families' Tax Credit includes a childcare tax credit to assist working families which have to pay for childcare. Any lone parent working sixteen hours or more per week, and paying for qualifying childcare, can claim the childcare tax credit. Each partner in a working couple must work sixteen hours or more per week to qualify. The childcare tax credit is more generous than the childcare support offered under Family Credit, further improving the incomes of low-paid families. The following example illustrates both how the Working Families' Tax Credit is calculated and the impact that it has on the income of a typical family with two children.

13 Currently, payment of the Working Families' Tax Credit is made directly to the female partner, but from April 2000 it will be payable through the payroll, thus enhancing the link between work and financial reward (though couples in which one partner is not working can choose to receive payment direct from the Inland Revenue). It is estimated that, by 2001, about 1.4 million people will be receiving the Working Families' Tax Credit: around half a million more than would have been in receipt of Family Credit.

A couple, both working less than 30 hours per week, with two children aged 3 and 7, have take-home pay of £265 plus Child Benefit. They pay eligible childcare costs of £125 per week.

Take-home pay		£265.00
Working Families' Tax Credit (WFTC) credits:		
Basic tax credit	£52.30	
Child tax credit (age 3)	£19.85	
Child tax credit (age 7)	£19.85	
Childcare tax credit (70% of £125 weekly cost)	£87.50	
Maximum WFTC allowable	£179.50	
Less 55% of income in excess of £90 (£265-£90 = £175)	- £96.25	
WFTC payable	£83.25	£83.25
Net income with Working Families' Tax Credit		£348.25
Plus Child Benefit		£24.00
Total income		£372.25

Source: Inland Revenue

Disabled Person's Tax Credit

- 14 In October 1999, Disability Working Allowance was replaced by the Disabled Person's Tax Credit, which offers more generous support for disabled workers who work for sixteen hours or more a week. For couples, it has a similar structure of credit rates, income threshold and tapers to that for the Working Families' Tax Credit. For single workers, there is a lower income threshold. Where a single disabled person moves from social security benefit to full-time work at the National Minimum Wage of £3.60, the Disabled Person's Tax Credit provides a minimum income guarantee of £155 per week. Where the earner is part of a couple with a child under eleven, this guarantee rises to £230 per week.

Housing Benefit and Council Tax Benefit

- 15 Housing Benefit and Council Tax Benefit are non-contributory, income-related (means-tested), tax-free benefits which help people on low incomes meet the cost of rented accommodation and Council Tax. These benefits are not exclusively for working people, but are also available to groups such as pensioners and lone parents. Basic entitlement to Housing Benefit and Council Tax Benefit is calculated on the same basis as for the two main means-tested social security benefits: Income Support (IS) and income-based Jobseeker's Allowance (JSA(IB)). Where income exceeds the levels prescribed for

IS and JSA(IB), a 65 per cent taper operates for entitlement to Housing Benefit and a 20 per cent taper for Council Tax Benefit. Either benefit may be claimed individually and be paid as a single benefit, or may be claimed in addition to other in-work support like Working Families' Tax Credit.

Making Work Pay

Working Families

- 16 When taken together, the above measures and the changes to Child Benefit announced in the 1998 and 1999 Budgets should raise the income of working households by an average of £450 per year, with working families with children gaining an average of £740 per year. These measures together with the National Minimum Wage will guarantee a family with someone in full-time work a minimum income of £200 a week. One of the main effects of the new measures will be a reduction in the numbers of families affected by extremely high marginal taxation rates. Prior to October 1999, the cumulative effect of the tapers in the income-related in-work benefits resulted in some working families suffering marginal deduction rates of 97 per cent. As a consequence of the reforms, the numbers of families with marginal deduction rates of 70 per cent or more will fall by two-thirds from 700,000 to just over 200,000 (Table A3.4).

Table A3.4

The Combined Effects of the 1998 and 1999 Budget Reforms on High Marginal Tax and Benefit Withdrawal Rates

Marginal Deduction Rate	Before the Reforms (000s)	After the Reforms (000s)
100 per cent or more	5	0
90 per cent or more	115	15
80 per cent or more	255	175
70 per cent or more	715	230
60 per cent or more	730	950

Source: Government Evidence

Note: Figures are for families where at least one partner works 16 hours or more, and are based on estimated 1998–99 caseload and take-up rates.

Workers Over 50

17 When older workers re-enter work from unemployment they do so at wages which are, on average, 25 per cent below those in their previous job and this can act as a significant disincentive to return to work. To assist the over-50s to make the transition into work, particularly low-paid work, an employment credit was introduced in certain areas from October 1999, prior to national application in 2000. It is payable to those people over 50 who return to work after six months on social security benefit. For workers returning to full-time work, the credit is £60 per week, bringing a guaranteed

income of £175 per week, while for those moving into part-time work of sixteen hours or more, the credit is £40 per week. It is payable for the first year in the new job.

Impact on Household Incomes

18 We illustrate the overall effects of the National Minimum Wage and the changes to the tax and benefits system on family incomes in Tables A3.5 and A3.6. Table A3.5 shows the impact on a series of typical working households with children which gain from the minimum wage.

Table A3.5

The Impact of the National Minimum Wage on Weekly Incomes of Typical Families with Children				
	Take-home pay pre-minimum wage	Net income with Family Credit	Net income post-minimum wage, with Family Credit	Net income post-minimum wage, with Working Families' Tax Credit
	(Based on pre-NMW earnings of £2.75 per hour)	(Based on pre-NMW earnings of £2.75 per hour)	(Based on earnings of £3.60 per hour)	(Based on earnings of £3.60 per hour)
Example 1: Lone parent, 2 children under 11 years, works 16 hours per week, no childcare costs, pays rent of £83.20 and council tax of £10.10	£44.00	£148.10 (£78.51)	£161.70 (£66.95)	£173.60 (£64.83)
Example 2: Lone parent, as above, with child care costs of £75 per week	£44.00	£148.10 (£93.30)	£161.70 (£93.30)	£226.10 (£83.95)
Example 3: Married couple, 2 children under 11 years, one earner works 37 hours per week earning £2.75 per hour Rent of £83.20 and council tax of £10.10	£98.18	£201.06 (£4.39)	£208.37 (£2.93)	£231.70 (£0.14)

Source: HM Treasury

Note: Figures in brackets denote entitlement to Housing Benefit and Council Tax Benefit.

Table A3.6

Impact of the National Minimum Wage on Incomes of Second Earners and Single People		
	Take-home pay pre-National Minimum Wage	Take-home pay post-National Minimum Wage
Example 1: Married couple, 2 children under 11 years, 2 earners (first earner earns £265 per week; second earner earns £2.75 per hour working 20 hours per week). Pays rent of £83.20 and council tax of £10.10	£55.00 (Second earner only)	£71.40 (Second earner only)
Example 2: Single person, aged 18, working 37 hours per week, living at home (no housing costs)	£83.02	£103.74

Note: There was an error in paragraph 7.36 of the LPC's First Report, which stated that 'a married couple with one earner and two children might benefit by over £16 a week [as a consequence of Budget 1998 reforms]'. In fact, the gain of £16 a week would have been to the *second earner* in a family with two children with both adults working. (Final example in Table 7.2 of the First Report.)

- 19 Column 2 shows the net take-home pay for the worker on the basis of pre-National Minimum Wage earnings of £2.75 an hour, which was about the average hourly rate of pay for those earning below the National Minimum Wage in April 1998. Column 3 is the net weekly income for the household based on take-home pay plus Child Benefit and Family Credit. Column 4 illustrates the impact of raising the worker's gross earnings to the National Minimum Wage of £3.60, while the final column demonstrates the cumulative effect of the minimum wage and Working Families' Tax Credit. Of particular note is the significant increase for the lone parent with childcare costs (Example 2), which is due to the additional impact of the childcare tax credit.
- 20 These examples indicate that families with children gain considerably from the combined effect of the minimum wage and Working Families' Tax Credit. The emboldened figures do not, however, take account of the impact on other in-work benefits. All three illustrative families in Table A3.5 would qualify for Housing Benefit and Council Tax Benefit at the levels shown in brackets and both benefits would be eroded by an increase in income from other sources. In the case of Example 1, the minimum wage and Working Families' Tax Credit raise family income from £148.10 to £173.60, an increase of £25.50. But the gain to the overall family income is reduced to £11.82 by consequential reductions in Housing and Council Tax Benefits.
- 21 We also considered the effect of the minimum wage on the incomes of workers who did not qualify for in-work benefits such as Working Families' Tax Credit. Table A3.6 shows the significant impact on net earnings of a second earner in a two-earner family and of a single person receiving the young person's Development Rate. Each gains most of the increase as the only marginal deduction is restricted to income tax and National Insurance Contributions, and the level of liability for each of these was reduced from April 1999 as a consequence of 1998 Budget changes.
- 22 To further our understanding of the impact of the National Minimum Wage and the reforms of the tax and benefit system, we held a seminar in December 1998. Below we reproduce a summary of each of the three papers presented. The full texts, together with the comments of the discussants, were published in the Low Pay Commission's Occasional Paper 2, *The National Minimum Wage, Incomes and the Low Paid* (June, 1999).

- 23 Some critics have argued that a minimum wage is an ineffective way to tackle poverty. Most of the poor are pensioners or people in workless households who would not be directly affected by the minimum wage. But also many beneficiaries of the National Minimum Wage are working partners or teenagers living in reasonably wealthy households. Richard Dickens of the Centre for Economic Performance, London School of Economics shows in *Poverty, Low Pay and the National Minimum Wage* that this is an inaccurate picture of the link between low pay and poverty in the 1990s. The composition of the poor has changed over the last thirty years so that in-work poverty has become much more pervasive. While it is clear that a minimum wage cannot assist pensioners and the workless, the effect on poverty for those in work is quite strong. In addition, moves in and out of work mean that the minimum wage will help more individuals in poverty than is apparent in cross-section data. It should also be remembered that pensioners' current income is largely determined by their earnings over their working life, which may be enhanced by a minimum wage. Thus, while the National Minimum Wage is not going to eradicate poverty on its own, in conjunction with other policies it will have a significant impact on the fortunes of the working poor.
- 24 Amanda Gosling of the University of Essex and Institute for Fiscal Studies, in *Minimum Wages, the Tax System and Incentives to Work* assesses the first round consequences of the National Minimum Wage for work incentives and levels of in-work benefits. She finds that there are only small overall increases in in-work incomes, though the minimum wage will reduce dependency on benefits. The conclusions about the types of worker most affected are, however, more robust than predictions about the scale of the effect on in-work incomes, which are likely to be understated because of difficulties in imputing potential in-work incomes for unemployed people.
- 25 There is a small effect on the number of Working Families' Tax Credit and in-work benefit claimants as the minimum wage moves some low-paid workers out of entitlement. The number of people in receipt of Working Families' Tax Credit is predicted to fall by around 2.5 per cent, a relatively small effect as wages well over the National Minimum Wage are needed to move families off Working Families' Tax Credit. There is a larger effect on expenditure on in-work benefits, and it is predicted that the National Minimum Wage may reduce the cost of the Working Families' Tax Credit by around 6 per cent. No implications for public finances as a whole can be drawn, however, as they also depend on factors such as changes in VAT and corporation tax receipts.
- 26 Mark Stewart of the University of Warwick uses the British Household Panel Survey in his paper *The Dynamics of Low Pay and Low Income* to examine the following issues concerning the National Minimum Wage and the dynamics of low pay. Are there scarring effects of low pay? Does low pay itself cause future low pay? Is there a cycle of low pay and no pay? Are low-paid jobs stepping stones between unemployment and higher-paid work? What are the dynamics of the relationship between low pay and poverty? He concludes that there is considerable persistence in low pay. There is strong evidence of a cycle of low pay and no pay. The low paid are more likely to be out of work in the future; those out of work are more likely to be low paid on re-entry, and are even more likely to be so if they had been low paid prior to being out of work.
- 27 The hypothesis that low-paid jobs act as stepping stones to higher-paid jobs is not supported by the data. The evidence suggests that low-paid jobs are more likely to act as blind alleys than as stepping stones to positions higher up the pay distribution. The overlap between low pay and household poverty is not large on cross-sectional analyses. Around half of those classified as 'permanent' low paid are, however, in household poverty. The overlap between low pay and poverty is considerably greater over time than when viewed in a snapshot.

Conclusion

- 28 The National Minimum Wage is part of a package of measures to stimulate the labour market by improving in-work incomes and thus incentives to work. But the National Minimum Wage is only months old and some of the tax and benefits measures are yet to be introduced. Thus we cannot yet assess the impact which the reforms will have on incentives. It is clear, however, that in the immediate term further amendments to the structure of taxation will raise incomes, often substantially, for large numbers of low-paid workers.

Appendix 4

Pay Structures and the Low Paid

1 Our terms of reference for this report required us to consider the impact of the National Minimum Wage upon pay structures. Overall, the April 1999 NES data show there have been few significant recent changes to the composition of earnings as a result of the minimum wage. In the case of pay differentials, the evidence suggests that the impact of the National Minimum Wage has been contained within the bottom grades of pay structures, with little sign of pay restoration among higher grades. There is also little evidence that employers have made major changes to their remuneration systems, which suggests that the definition we recommended goes with the grain of pay systems and is working well. This appendix provides details on the composition of pay for the low paid, looks at the impact of the National Minimum Wage upon pay differentials and reviews changes in remuneration practices since its introduction. More information is available in the Low Pay Commission Occasional Paper 3, *Pay Structures and the Minimum Wage*.

2 The low paid are much less likely to have complicated payment structures than higher-paid workers. This reflects the fact that many, mainly female, low-paid workers are engaged in casual, temporary and part-time work, where payment tends to be a simple hourly rate for the hours worked and where there is less opportunity to earn additional payments. Nonetheless, there are significant sectors where low-paid workers earn overtime and payments by results (PBR). In these sectors, these additional payments can provide an important component of total earnings.

3 The definition of what remuneration components can and cannot be included in the National Minimum Wage was an important part of the deliberations in reaching our original

recommendations. We recommended a hybrid definition which included more than just basic rates but excluded certain remuneration components, such as premium payments, allowances and all benefits (except for a limited accommodation offset). In general, only 'standard' pay counts towards the minimum wage calculation. The National Minimum Wage Regulations (DTI, 1999a) set out more detailed legislative requirements for the application of the definition and the DTI publication, *A Detailed Guide to the National Minimum Wage*, provides guidance on its operation in practice.

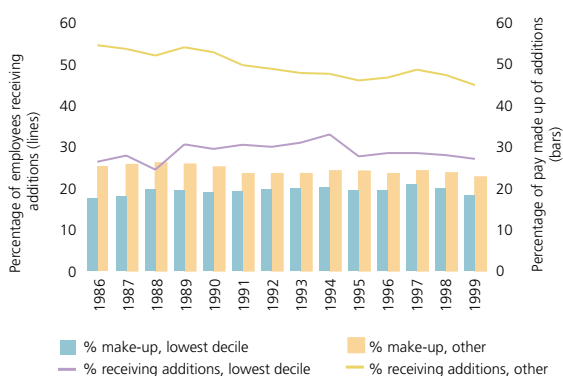
Pay Composition

4 The data presented here on the composition of earnings for the low paid are drawn from the New Earnings Survey (NES), the major source of information about the make-up of pay in the UK. We provide time-series data to show the patterns both before and shortly after the introduction of the National Minimum Wage. It should be noted that the time series in this appendix cover Great Britain only but that these are not likely to be greatly different to those for the UK. The figures are for all employees, both full-time and part-time. We use the lowest decile of average earnings (£4.80 per hour in April 1999) as the comparator over time and compare this with changes in earnings patterns for the rest (i.e. the other 90 per cent of earners). We have used the lowest decile because it is most likely to incorporate the vast majority of differential effects (see Appendix 2 for a discussion of the impact of the National Minimum Wage upon wage differentials). Further details of occupational differences are included in Occasional Paper 3.

- 5 We also took advantage of an opportunity to ask additional questions in the 1999 NES survey to collect information about earnings composition. This exercise confirmed our finding that the pay structures of the low paid tend to be relatively straightforward. This implies that the NES is a suitable source of data on pay structures in its present form. It should be noted, however, that the April 1999 figures from the NES may not reflect the full impact of the minimum wage. It will take at least another year's figures before the full effect upon pay composition and differentials will be evident. It is also important to note that the NES data, being a survey conducted in April, may miss seasonal fluctuations. For example, overtime payments in agriculture and hospitality are likely to increase in the Summer.
- 6 The proportion of lowest earners in receipt of additions to basic pay was slightly down on the previous year, but not significantly out of line with recent trends. In April 1999, the proportion for the lowest decile of earners was 26 per cent, compared with 44 per cent for the rest (i.e. the other 90 per cent of earners). Figure A4.1 shows the patterns for both the lowest decile and the rest of the distribution from 1986 to 1999.

Figure A4.1

Additions to Basic Pay: Incidence and Contribution to Total Earnings, 1986–1999

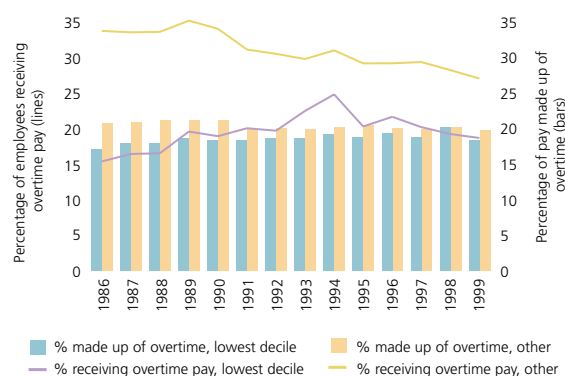


Source: NES, April 1986–1999.

- 7 Additions to basic pay are important for some low-paid workers. There has been some decline since 1997 in the proportion of pay made up by additions for lowest-decile workers, but the overall pattern is relatively flat. In April 1999, these additions constituted 18 per cent of total earnings for the lowest decile, compared with 22 per cent for the rest. Figure A4.2 shows the proportion of total pay made up by additions for those in receipt of them from 1986 to 1999.
- 8 Overtime is by far the most important pay addition for the low paid. Of those in the lowest decile of earners in April 1999, 18 per cent received overtime pay compared with around 27 per cent for the rest (see Figure A4.2).

Figure A4.2

Paid Overtime: Incidence and Contribution to Total Earnings, 1986–1999



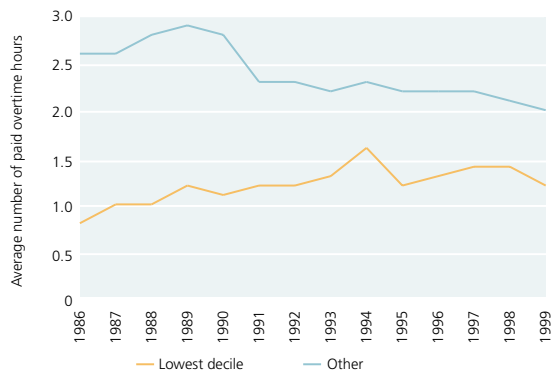
Source: NES, April 1986–1999.

- 9 For those in receipt of overtime pay, in April 1999 overtime earnings amounted to 18 per cent of total earnings for the lowest decile, which is similar to the average for the rest (see Figure A4.2). There has been a marked decline in those receiving overtime pay since 1994 for both the lowest decile and the rest. This may well reflect a general trend within reward systems towards increasing consolidation of overtime premia into basic pay and the tendency to treat all hours of work as the same, whether unsocial or not. It also may reflect the growing use of part-time labour in some sectors, so that many

employees cannot reach the threshold for overtime pay. For example, there has been some impact in the retail sector where the extension of opening hours, including Sunday trading, has changed the concept of ‘basic’ and ‘unsocial’ hours (IDS, 1999c), although the NES has not picked up any great changes in the pattern of earnings in this sector as yet. The NES data on overtime hours (Figure A4.3) shows that there has been a fall in overtime hours for the majority of earners from 1989 but a slight rise for lowest-decile workers until 1994. Since 1997 overtime hours for both groups have fallen. We discuss the industrial variations further below.

Figure A4.3

Average Number of Paid Overtime Hours, 1986–1999



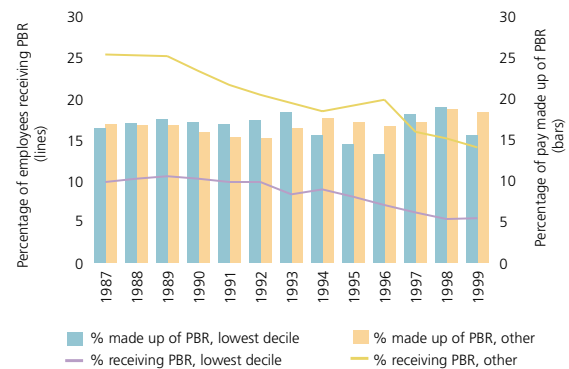
Source: NES, April 1986–1999

10 The proportion of low-paid employees in receipt of other identifiable components – shift pay, profit-related pay and other incentive pay – is small. Of these components, the most important is incentive pay, although low-paid workers appear to have less access to such payments than higher-paid workers. The proportion of employees in receipt of incentive payments or PBR in April 1999 was 5 per cent for the lowest decile and 14 per cent for the rest. There has been a continuing decline in PBR since 1987 for both the lowest decile and the rest. Figure A4.4 shows the pattern since 1987. For those in receipt of PBR, the proportion of total pay made up from PBR in April 1999 was 15 per cent for the lowest decile compared with 18 per cent for the

rest. There appears to have been a marked fall in the proportion for the lowest decile since 1998.

Figure A4.4

Payment-By-Results (PBR): Incidence and Contribution to Total Earnings, 1987–1999



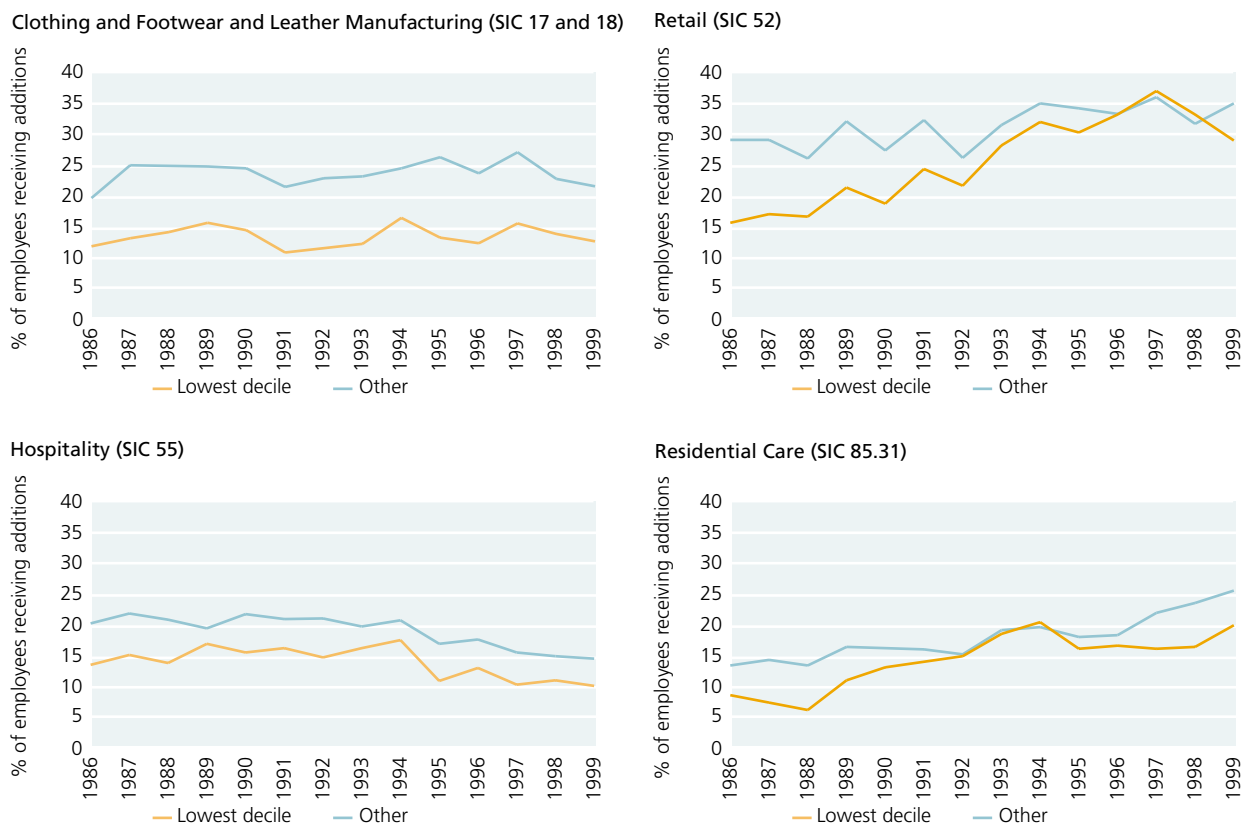
Source: NES, April 1987–1999

Industrial Variations

- 11 While pay structures in general can be complex and consist of many separate components, there are significant variations between industries and occupations. The major differences are in overtime pay and PBR. For example, the proportion of employees in receipt of overtime pay is higher in retail and residential care than in other sectors, while PBR is more common in clothing and footwear (reflecting piecework earnings) and hairdressing (reflecting tips and commission) than elsewhere.
- 12 The NES shows that overtime pay has fallen slightly in recent years in the hospitality sector while in clothing and footwear manufacture the pattern has remained flat. In retail there has been some growth in overtime, but the lowest decile of earners has seen a recent fall in overtime working. This may imply some reductions in hours or redefinition of hours eligible for premium payments for low-paid workers. In residential care the proportion in receipt of overtime pay has risen. Figure A4.5 shows the patterns for these four sectors.

Figure A4.5

Paid Overtime: Incidence in Low-paying Industries



Source: NES, April 1986–1999

- 13 In April 1999 around 30 per cent of lowest-decile employees in the retail industries received overtime payments. Further analysis reveals that, on average, overtime pay made up 19 per cent of total earnings for these workers. In residential care around 20 per cent of lowest-decile employees received overtime, which similarly made up around 19 per cent of total pay.
- 14 Incentive pay is an important component in the clothing and footwear manufacturing industry: in April 1999 PBR was paid to over 20 per cent of lowest-decile employees in clothing and footwear manufacturing and such payments made up 38 per cent of total earnings for those in receipt of them. Incentive pay is also important in hairdressing, which is indicative of tips paid through the payroll

or commission, although such payments are much less common among lowest-decile workers. The proportion receiving PBR among the upper nine deciles in hairdressing in April 1999 was 38 per cent while for the lowest decile it was only 12 per cent. This is because the lowest-decile workers in hairdressing salons are more likely to be undertaking support roles (such as washing hair) and hence not receiving commission or tips. For those in receipt of PBR in hairdressing, it made up around 12 per cent of earnings for the lowest-decile workers, but almost 30 per cent for the rest.

Impact upon Differentials

- 15 A major concern prior to the introduction of the National Minimum Wage was the potential impact on the differential between the lowest paid and those higher up the earnings distribution. As we show in Chapter 3, the impact of the National Minimum Wage on differentials has been relatively minor. The latest NES figures show clearly that the highest gains have been at the bottom of the distribution with relatively little impact higher up. This conclusion is supported by findings from our research programme. IDS said that it had 'not encountered much obvious discomfort regarding differentials which could not be addressed in a straightforward way' (IDS 1999b). Table A4.1 provides some examples of pay awards where the lowest rate had to be increased to the National Minimum Wage level. These awards demonstrate clearly that the increase for the lowest grade has been higher than that for those in more senior grades, indicating that differentials have been eroded but that full restoration has not occurred.
- 16 In organisations where pay is determined through collective bargaining with trade unions, the minimum wage appears to have been manageable within the annual negotiated settlement. IDS found that no major trade union had campaigned for restoration of lost differentials. It commented that 'though calls for restoration of differentials by other workers were widely predicted and anticipated, none have yet materialised to our knowledge' (IDS, 1999c).
- 17 In organisations where pay is determined through management discretion alone, the minimum grade rates have sometimes been increased to comply with the law but the rest of the grade rates have remained unchanged. In some organisations there has been a general 'tidying up' of pay structures with the abolition of the lowest grade rate or minimum scale point, which may not have contained any workers anyway. For example, research (IDS, 1999b) indicated that at Thomas Cook the minimum grade rate was raised to £7,020 per year (£3.60 per hour) from 1 January 1999 but other rates remained unchanged. At Thomson Holidays the lowest scale points were taken to within range of the National Minimum Wage in recent pay reviews but with no change to pay scales. These were further increased to the level of the minimum wage from 1 April 1999 but other scales were left unchanged. Thomson Holidays reported, however, that there was no pay bill impact because there were no staff on these scale points.
- 18 The reasons for the absence of impact upon differentials are complex. A key factor is the prudent level at which the National Minimum Wage was set, which meant that many organisations could adjust their lowest pay rates without any great disruption to higher-paid grade rates. In some businesses there was a wide enough gap between the pay levels of the non-managerial staff and managerial staff that there was no danger of any differentials impact (for example where all non-managerial workers were earning below £5 per hour).
- 19 There have also been changes to grading systems in recent years which might be a contributory factor. According to the IDS research, 'in a number of key industries and companies, pay structures have changed out of all recognition in recent years so that, often, preconceptions of what pay structures look like can be a bit out of touch' (IDS, 1999c). In many sectors, rigid hierarchical pay structures are a thing of the past and grade rates may often only consist of a minimum level with no ceiling. This allows local managers to decide the pay levels for individual staff. The pay ranges within grades can also be wide and pay ranges may well overlap. For example, at Greenalls Hotels 'the differentials between the lowest-paid and the higher levels of the pay structure are large enough for there to be absolutely no repercussions' while at St David's Hotels the eight grade scales overlap each other and grade rates are determined by the market and cost of living factors, rather than some fixed pay relationship (IDS, 1999c).

Table A4.1

Impact of Increases for Lowest Grades Upon Pay Differentials					
Organisation	Grade	Old rate	New rate	Inc £ per hour	Inc %
Agricultural Wages Board (England and Wales)	Casual worker aged 19 and over	3.21	3.60*	0.39	12.1
	Standard worker aged 19 and over (Increase phased in over extended period)	4.26	4.26*	0.00	0.0
Agricultural Wages Board (Scotland)	Adult general worker (less than 13 weeks)	3.20	3.60*	0.40	12.5
	(more than 13 weeks)	4.26	4.33*	0.07	1.6
Environmental Engineering Industry	Grade 1	3.06	3.60	0.54	17.6
	Grade 2	3.43	3.60	0.17	4.9
	Grade 3	3.80	4.00	0.20	5.3
Footwear Distribution Industry	Sales staff age 18	2.71	3.00	0.29	10.7
	Sales staff age 21	3.58	3.66	0.08	2.2
KFC Restaurants	New starter	3.30	3.63	0.33	10.0
	Team leader	4.40 to	4.77 to	0.37	8.4
		4.70	5.10	0.40	8.5
Light Metal Trades Industry	Labourer	3.35	3.60	0.25	7.5
	Moulder	4.45	4.56	0.11	2.5
McDonald's Restaurants	Crew aged 18	3.50 to	3.60 to	0.10	2.8
		4.85	4.95	0.10	2.1
	Shift manager	4.30 to	4.40 to	0.10	2.3
		6.70	6.80	0.10	1.5
Motor Trade Industry	Workshop technician grade E	3.28	3.60	0.32	9.8
	Skilled mechanic grade A	4.68	4.84	0.16	3.4
Ready-mixed Concrete Industry	Dumper and shovel loading driver	3.47	3.60	0.13	3.7
	Driver (four axles or over)	4.02	4.14	0.12	3.0
Registered Clubs' Association	Other worker 18+	3.44	3.60	0.16	4.6
	Steward (category 3)	4.36	4.52	0.16	3.7
Select Service Partner Retail Catering	Sales assistant 1	3.30	3.60	0.30	9.1
	Senior supervisor (Provincial rates)	4.50	4.64	0.14	3.1
Thomas Cook	Messenger (Note: few workers actually on this rate)	2.75	3.60	0.85	30.9
	Supervisor	5.11	5.11	0.00	0.0
Wm Morrison Supermarkets	Students and temporary employees aged 18	2.91 (starter)	3.63 (starter)	0.72	24.7
		3.07 (estab)	3.78 (estab)	0.71	23.1
	Skilled Butcher	5.07	5.21	0.14	2.8
Wolverhampton & Dudley Breweries	Bar staff	3.15	3.60	0.45	14.3
	Supervisor	4.20	4.40	0.20	4.8

*Effective from 1 April 1999. Further increase from June 1999.

Table A4.1 (continued)

Impact of Increases for Lowest Grades Upon Pay Differentials	
Other Minima Increased	
Leather Producing Industry	Industry minimum rate increased from £3.40 to £3.69 per hour with effect from 1 July 1999. Individual companies within the industry have been paying the minimum since April 1999. Actual hourly earnings are usually higher because of piecework. Separate juvenile rates paid to under-18s.
Royal Clifton Hotel	5.9 per cent increase to minimum rate from 1 April 1999, for employees over 22 years old. Minimum youth rate of £3 per hour paid to employees aged 18 to 21.
Jarvis Hotels	Minimum rates increased by larger amount in each annual pay review from 1997. Minimum rate of £3.60 per hour introduced for employees over 22 years old from 1 April 1999. Probationary rates (95 per cent of the full rate) apply for first 12 weeks of employment. Pay review in September 1999 increased minimum rates by a further 3 per cent.
Greenalls Hotels	The company minimum was increased by 5.4 per cent, from £3.67 to £3.87 per hour with effect from 1 October 1998. This minimum rate applies to all the group's hotels in Great Britain.
JD Wetherspoon Pubs	From 1 May 1998 there was a provincial minimum rate of £3.50 per hour, a higher provincial rate of £3.75 per hour and a London West End rate of £4 per hour. From 1 April 1999, the provincial minimum rate was increased from £3.50 to £3.75. There is now a single minimum rate of £3.75 per hour and the company no longer sets higher minimum rates for other locations.
Century Inns	From 1 October 1998, the minimum rate for bar staff was raised from £3.25 to £3.45 per hour. Paid holiday entitlement was also introduced for a third of the workforce, within an overall pay bill increase of 3.5 per cent. The minimum rate was raised again to £3.60 an hour from 1 April 1999.
Wendy's Hamburgers	From 4 January 1999 the minimum rate was increased from £3.35 to £3.45 per hour. From 1 April 1999, this was again increased to £3.60 per hour. Note: this company has recently announced the closure of its ten directly owned restaurants in the UK. Franchised outlets will continue to trade.

Source: Quarterly Report to the Low Pay Commission (IDS, 1999c).

20 There is also increasing use of 'broad banded' grading systems, where there are a relatively small number of grades with very large pay ranges. These can accommodate pay progression without the necessity for promotion to a higher grade. Such broad banded systems are common where organisations have moved to flatter organisational shapes, with layers of supervisory staff being stripped out of the structure. Such broad bands also

allow much more management discretion over the pay level at which staff are recruited and the speed of progression through the band. Hence differentials have much less importance. Even where employers have reported problems with differentials, on further investigation it has been found that few or no employees were located in the lowest grade, so that the impact has been small.

- 21 In the past, pressure to maintain differentials has come partly from trade unions during pay negotiations. But it is now the case that collective bargaining only covers a minority of the workforce (41 per cent according to the 1998 Workplace Employee Relations Survey, which covered 3,000 workplaces with ten or more employees). Moreover, trade union membership is less common among the low paid, particularly so in sectors such as hospitality and retail where low pay is prevalent. According to the Labour Force Survey (Autumn 1998 figures), only 9 per cent of all those earning below £3.50 per hour (equivalent to £3.60 at April 1999) were union members and only 11 per cent had their pay and conditions negotiated by a union. Collective bargaining covered only 7 per cent of employees in hotels and restaurants; 9 per cent in agriculture, forestry and fishing; 12 per cent in real estate and business services; and 14 per cent in wholesale and retail (Bland, 1999). Because in many organisations pay is now much more subject to management discretion, the issue of differentials relates more to labour market pressures than to union demands; for example, staff may leave because they are disgruntled with the erosion of their pay lead over other staff. But we have found only very limited evidence of this happening as a result of the minimum wage.
- Pay Structure Changes**
- 22 The way the National Minimum Wage was defined had the potential to change pay structures, as employers could seek to change the composition of the pay package to take maximum advantage of the components which counted towards the minimum wage calculation. For example, consolidation of non-allowable items, such as overtime premia and special allowances, into basic pay was one way employers could reduce the cost of the National Minimum Wage, although there was a clear risk of a claim for detriment from employees if these changes were imposed without agreement.
- 23 There appear to have been few changes to pay structures as a result of the National Minimum Wage. Within medium to large-sized organisations, where pay awards are monitored, IDS found examples of the withdrawal of paid meal breaks and consolidation of the value of luncheon vouchers into basic pay. There were also examples of changes in travelling time payments in some sectors, with the replacement of lump sum travel allowances by an hourly minimum rate. There was also limited evidence that some employers had changed their arrangements concerning accommodation. Some had increased their charges to the maximum fifty pence per hour (£19.95 per week) allowed under the National Minimum Wage regulations while others had had to reduce their charges to that level. At one restaurant chain quoted in the IDS research, the arrangements for tips were changed just prior to April 1999 to allow tips taken through credit card bills to be offset against the minimum wage, as allowed in the Regulations.
- 24 The picture among small organisations, where research is more difficult to conduct, is less clear. The research carried out by the Associations of Citizens Advice Bureaux and the Low Pay Unit found that a small number of individual workers had experienced some detriment to their terms and conditions as a result of the National Minimum Wage. For example, some had had overtime premia withdrawn while others had been asked to work unpaid overtime. Some had had allowances consolidated or payment for meal breaks withdrawn. Research for the Commission by Gray and Heyes on the impact of the minimum wage upon the West Yorkshire textiles and clothing industries found some examples of employers reducing paid breaks, overtime working, bonuses and premia.
- 25 There is little evidence from our research that pieceworking systems have been greatly affected. Research for the Commission by Undy et al. (1999) on sixty-six firms in the clothing, knitwear and footwear industries indicated that most pieceworkers were able to earn on average more

per hour than the National Minimum Wage, but there might be some disincentive effect for poor performers who could now earn £3.60 per hour without the extra effort previously required. The research reported that the impact upon payment systems was much more pronounced in some firms than others. In particular, firms in Northern Ireland and a small number of employers in Leicestershire and Nottinghamshire were more concerned about the impact upon piecework systems than others in the sector. There was some evidence that many of the workers earning below the minimum wage were largely support staff, such as catering staff, cleaners, security staff and packers, who do not have access to incentive pay. Some firms are moving to new teamwork systems of production under which workers receive a bonus based on team performance rather than an individual piecework rate, although others report that such innovations have not been successful.

- 26 Overall, however, the research by Undy et al. (1999) found 'the great majority of firms continuing with their existing piecework arrangements untouched by the National Minimum Wage'. The main ways in which employers were coping with any disincentive effect of the minimum wage was to tighten up on performance management, to improve training and to raise the performance level required to achieve the incentive (for example from 80 per cent to 90 per cent of standard performance). In some cases, nevertheless, there is some impact upon employment as poor performers are dismissed if they cannot achieve the required improvement in performance.

Appendix 5

Low Pay Commission Research Projects

- 1 In order to meet our terms of reference, we commissioned research projects and undertook our own survey of low-paying businesses. We covered three main areas:
 - The impact of the minimum wage on businesses, for example on pay differentials, employment, competitiveness, and training and development.
 - The effects for particular groups such as young people (with a particular focus on 21 year olds), women, homeworkers, and people with disabilities.
 - Compliance and enforcement.

This appendix outlines the research projects which we commissioned and the postal survey which we conducted.

Commissioned Research Projects
- 2 The Commission had a research budget of £50,000 in 1998–99 and a further £100,000 in 1999–2000. An article in the January 1999 issue of *Labour Market Trends* summarised the research programme and invited expressions of interest from organisations to undertake research on the National Minimum Wage. A similar document was placed on our website. In addition, an article calling for expressions of interest was published in the *British Universities' Industrial Relations Association Newsletter* (Bain and Brown, 1999).
- 3 Initial bids were considered in November 1998 and a further round of bids was considered in February 1999. The meetings had an independent chairman from the Department of Trade and Industry. Bids were ranked according to a number of criteria: their relevance to the Commission's terms of reference, the quality of the research proposal and value for money.
- 4 In total, nineteen projects were selected. These covered particular sectors where low pay is common (for example retail, hospitality, clothing and footwear, social care and the voluntary sector); changes in pay and benefits systems; small firms; compliance and enforcement; and the effects on particular groups (for example young people, homeworkers, people with disabilities). In addition, the Commission provided a contribution to the funding of four local projects (one in Humberside, two in Leicestershire and one in Lincolnshire).
- 5 The projects involved the collection of new data through surveys and case-studies and the analysis of existing material. In some cases, the projects were undertaken by specialist research organisations; in others, they were conducted by those with knowledge and experience of particular sectors or occupational groups, which was important in accessing information about the effects on employees.
- 6 The effects of the National Minimum Wage will take some time to appear in official statistics, and longer-term research will be needed to identify the full economic effects. The information provided by our research programme provides initial, up-to-date assessments of the introductory effects of the minimum wage. Together with our other work, they have provided valuable supporting evidence to inform our second report. Brief descriptions of the projects, including the main findings, are shown in Table A5.1 overleaf.

Table A5.1

Low Pay Commission Commissioned Research Projects			
Contractor	Aims and Objectives	Methodology and Timing	Results
Association for Supported Employment	To assess the impact of the National Minimum Wage on the employment and pay of people with disabilities.	Survey of 33 agencies involved in provision of support to people with disabilities; interviews with agency workers, disabled workers and their employers. July–November 1999.	No impact on those already being paid at or above minimum wage levels. The majority of Income Support (IS) recipients reduced their hours to keep earnings within disregarded level.
Citizens Advice Scotland	To monitor the experiences of CABx clients in relation to the introduction of the National Minimum Wage. To examine: awareness of CABx clients; adequacy of pay-related information provided by employers; wider impact of changes to clients' pay and conditions; and effectiveness of any follow-up action.	Monitoring of 150 cases supplemented by questionnaire. March–August 1999.	National Minimum Wage enquiries only small proportion of employment enquiries. Awareness of main rate is generally high but some confusion about other aspects of legislation and enforcement procedures. Clients used CABx for basic information but mostly to find out how to pursue denied rights. Information from employers often neither accurate nor lawful. Evidence of detriment and that clients unwilling to take action due to fear of possible consequences.
P. Edwards (Industrial Relations Research Unit, University of Warwick)	To examine managerial responses to the National Minimum Wage, particularly in respect of pay structures, work organisation, training and non-compliance.	Six in-depth case studies conducted by Warwick University and Cardiff Business School MA students. June–September 1999.	Several of the firms studied had absorbed the costs of the minimum wage relatively easily. Firms in similar market positions can respond differently, but further development of skills and productivity needs to be tackled. Research in Britain and France found cases of evasion. One study found that the minimum wage had not had adverse effects on the New Deal.
A. Gray and J. Heyes (Leeds University Business School)	To study the impact of the National Minimum Wage on the organisation of work and production, pay differentials and earnings distribution in the clothing and textiles industries in West Yorkshire.	Questionnaire survey of 168 firms and 213 workers. Supplemented by interview and case study evidence. March–September 1999.	Pay increased in 35 per cent of firms as a consequence of the National Minimum Wage, mostly in firms in the clothing sector which employed fewer than 100 people. In just over a quarter of these firms, employment of workers affected had been reduced. But, overall, international competition and exchange rates were more important factors than the minimum wage for the clothing sector.
A. Hughes, S. F. Wilkinson and A. Bullock (Economic and Social Research Council Centre for Business Research, Cambridge University)	To examine the impact of the National Minimum Wage on firms in respect of training, labour substitution, internal wage differentials and competitive positioning.	Added questions to existing biennial survey of businesses (75 per cent with under 50 workers); boosted sample from cleaning and security. Survey conducted June–October; 1,562 useable responses. February 1999–March 2000.	Emerging findings: no evidence of substitution of younger workers. Some small positive effects on training for small and medium-sized firms but not for micro-firms. Sizeable minority of firms have responded to the National Minimum Wage by attempting to improve competitive performance.

Table A5.1 (continued)

Low Pay Commission Commissioned Research Projects			
Contractor	Aims and Objectives	Methodology and Timing	Results
Humberside Law Centre	To identify problems experienced by workers in the Hull area in receiving the National Minimum Wage.	Statistical analysis of queries received (telephone and personal callers) with a sample, covering a range of cases, subsequently interviewed. March–June 1999.	Volume of complaints less than expected. Clients unlikely to pursue cases without support. Evidence of hours being cut. Difficult to apply regulations to homeworkers and commission agents. Care homes (sleeping time rates) and security workers source of greatest number of complaints, followed by cleaners and hairdressers.
Incomes Data Services Ltd.	To review the impact of the National Minimum Wage on organisations, covering changes in pay and benefits systems for low paid, impact on grading structures, staffing levels and other business effects.	Added questions on the minimum wage to regular monitoring of pay awards plus additional survey coverage of sectors where low pay prevalent. Presented four quarterly reports. April–December 1999.	Only minor adjustments were required by most organisations surveyed to deal with the minimum wage. Many had prepared in advance by raising minimum rates in stages. No significant evidence of restoration of differentials. Limited use of the Development Rate. Moves away from age-related pay as grading systems become more flexible. Little animosity to minimum wage among employers.
Industrial Relations Services Ltd.	To review young workers' pay and payment structures. Specific focus on retail and hospitality sectors.	Additional questions in existing annual cross-sectoral employer survey with boosted coverage of hospitality and retail sectors and smaller businesses. 474 responses (response rate of 15 per cent). Follow-up case studies with 25 employers paying below National Minimum Wage rates. December 1998–June 1999.	Over 6 in 10 employers using age-related pay systems paid 'adult' rates at age 18; appeared to be little negative impact on the recruitment of 18–21 year olds or those aged 22 and above.
Industrial Relations Services Ltd.	To identify impact of the National Minimum Wage on pay arrangements and employment practices, particularly in respect of young workers.	Case studies in ten firms identified from previous survey as paying young workers around NMW levels. July–October 1999.	Rises in wage costs led to greater focus on efficiency. Little restoration of differentials. Nominal age rates often over-ridden by management prerogative. Young people's pay increased with only slight negative consequences for their employment.
Leicester City Council/ Leicester County Council/ Leicestershire TEC	To assess impact of the National Minimum Wage on employment, pay levels and differentials, and use of accredited training in Leicester and Leicestershire area.	Additional questions to a regular 6-monthly survey of businesses. Responses from 754 firms. May 1999.	Most businesses were able to manage the National Minimum Wage. Less than 20 per cent had to increase wage levels. Less than 2 per cent had to reduce staffing levels. Few firms plan to use the Development Rate for workers aged 22 and above.

Table A5.1 (continued)

Low Pay Commission Commissioned Research Projects			
Contractor	Aims and Objectives	Methodology and Timing	Results
Leicester City Council Low Pay Campaign	To identify types of issue giving rise to complaints about non-compliance and action taken to resolve complaints.	Questionnaire survey of clients to advice agencies. Responses from 37 clients. April–July 1999.	Three-quarters of enquiries related to underpayment of the National Minimum Wage. Half of these were from textile workers. More complaints about underpayment from part-time workers (16) than from full-time workers (14) or apprentices/trainees (6). Nine out of eighteen cases followed up after initial inquiry showed employer had agreed to pay the minimum wage.
Lincolnshire Economic Development Services' Research Unit	To assess impact of National Minimum Wage on businesses in Lincolnshire and employers' responses.	Questions included in annual survey of employers (588 responses), stratified to reflect employment structure in Lincolnshire. June–July 1999.	Overall, the National Minimum Wage is proving very positive for the local economy. Little evidence of any negative impact of Development Rate for 18–21 year olds.
Low Pay Network	To examine impact of National Minimum Wage on young workers. Focus on treatment (pay and other employer practices) of 16–17 year olds and 18–21 year olds.	Uses data from Jobcentres and Careers Services collected on introduction of National Minimum Wage and several months afterwards. Case-study material provided by callers to Low Pay Network telephone helplines. February 1999–March 2000.	Surveys suggest that over 90 per cent of people are aware the minimum wage has come into force; nearer 75 per cent know the different rates. Of those giving details of pay, 7 out of 10 jobs in Jobcentres were advertised at more than £3.60 per hour, 40 per cent at over £4.00 per hour. Very few jobs advertised at 18–21 rate.
Low Pay Unit, London	To evaluate the implementation of the National Minimum Wage over the period of its introduction; investigation of key areas of difficulty arising from implementation for low-paid workers.	Study of 45 workers paid less than minimum wage who approached the Low Pay Unit's Employment Rights Advice Service about entitlement. Participants interviewed twice. April–August 1999.	Most respondents received minimum by time of second interview. But nearly half affected by enforcement issues of initial non-payment, underpayment, dismissal or detriment. Overall, awareness high and blatant non-payment rare.
R. Lucas and M. Langlois (Manchester Metropolitan University)	To investigate how firms in clothing/hospitality sectors are planning for the National Minimum Wage; focus on small/medium-sized firms; continuity and change from a December 1997 study.	Follow-up telephone interviews with 30 firms from across GB (16 hospitality and 14 clothing) previously interviewed. September–December 1998.	Hospitality employers, generally small businesses, expected little impact on wage costs as few workers employed and not all below minimum rates. Bigger impact expected in clothing because larger numbers of employees but better prepared than hospitality for implementation. Pay scales job-related rather than age-related. Little training offered so most firms would not use Development Rate.

Table A5.1 (continued)

Low Pay Commission Commissioned Research Projects			
Contractor	Aims and Objectives	Methodology and Timing	Results
R. Lucas and M. Langlois (Manchester Metropolitan University)	To examine the impact of the National Minimum Wage on firms' youth employment policies; knock-on effects for whole workforce; implications for employment practices in respect of older workers.	Postal questionnaire in Manchester South and Cheshire area across industry sub-sectors for representative 150 firm sample. In-depth interviews with 31 employers. April 1999–early 2000.	No change in treatment of workers under age 22. Most employers paid adult rate at age 18 or age 21. No overall impact on the employment of young people in hospitality. A number of employers in retail were intending to increase employment of young people, but generally unrelated to the minimum wage. Employment policies affected by local labour market, desired employee attributes and legislative requirements.
R. McNabb and K. Whitfield (Cardiff Business School)	To examine the characteristics of firms directly affected by the National Minimum Wage.	Used econometric techniques to examine data from the 1998 Workplace Employee Relations Survey, focusing both on supply-side factors (for example qualifications, experience) and demand-side factors (for example firm size, market characteristics). January–June 1999.	Low pay is generally more prevalent in small and medium-sized establishments (though the link between work unit size and low pay is more complex than previous research has suggested), where there is no or low collective bargaining coverage, and where there is a high degree of competition in the product market. Women more likely to face low wages even where they worked in jobs mainly done by men.
National Association of Citizens Advice Bureaux (CABx)	To identify the experiences of CABx clients in England and Wales in relation to the introduction of the National Minimum Wage; to examine awareness, problems arising from non-payment and the effectiveness of any follow-up action.	CABx monitoring data supplemented by questionnaire exercises. In total, 1,000 cases and 850 survey questionnaires examined. May–August 1999.	High response rate from CABx. Some evidence of tail-off in demand for information in later survey. Little evidence of poor awareness. Some evidence that employers are using knowledge to avoid payment. Non-compliance is compounded by failure of employers to meet other statutory duties.
National Council for Voluntary Organisations (NCVO)	To assess impact of National Minimum Wage on voluntary sector (costs, pay and benefits structures, staffing, volunteering and service provision). Jointly funded by NCVO and LPC.	15 in-depth case studies of voluntary sector organisations of various sizes and four service/contract providers. May–September 1999.	Generally positive view of the National Minimum Wage. Many voluntary organisations had prepared well in advance by raising their minimum rates in stages. Some had found the result was improved recruitment and retention. Concern was expressed about the level of the accommodation offset, the impact upon genuine volunteers and the issue of local government funding of contracts.

Table A5.1 (continued)

Low Pay Commission Commissioned Research Projects			
Contractor	Aims and Objectives	Methodology and Timing	Results
National Group on Homeworking (NGH)	To identify the impact of the National Minimum Wage on homeworkers' pay and employment conditions; knowledge of basic entitlements; particular focus on ethnic minority workers.	Accessed around 100 homeworkers through National Group on Homeworking helpline/projects; short questionnaire; follow-up interviews with 30 homeworkers face-to-face and 22 on telephone. April–November 1999.	Some homeworkers had seen their pay rise but nearly half had not. No routine use of the 'fair agreement'. Many homeworkers, particularly from ethnic minorities, were unaware of the minimum wage. Access to information and advice key.
Northern Ireland Association of Citizens Advice Bureaux (CABx)	To record the experiences of CABx clients in Northern Ireland in relation to the introduction of the National Minimum Wage; to examine the issues raised by clients and how they were pursued by both formal and informal means.	CABx monitoring information supplemented by general evidence from 92 client case-sheets on minimum wage enquiries and detailed information from 52 cases. June–October 1999.	High demand for information and advice immediately before, during and immediately after implementation declined over time. Some evidence of non-compliance, including changes to contracted hours and breaks. A third of enquiries examined concerned workers not being paid the minimum wage. A quarter of enquiries were about the Development Rate for young people.
Pay and Workforce Research	To study the impact of the National Minimum Wage in independent healthcare sector and to investigate employers' responses. Specific focus on recruitment and retention of staff.	Included questions on minimum wage issues in annual survey of pay rates for care home support workers. 415 responses. May–October 1999.	Increases in pay ranged from 8 per cent to 14 per cent according to type of organisation. Some evidence of consolidation of pay components, reductions in staff levels and reductions in hours. There had also been reductions in services to residents and the postponement of capital investment.
R. Undy, I. Kessler and M. Thompson (Oxford Institute for Employee Relations, Templeton College, Oxford)	To identify effects of the National Minimum Wage on pay structures in the clothing, knitwear and footwear industries.	66 case studies of firms of varying size, location and labour market. Main geographical areas were Leicestershire, Nottinghamshire and Northern Ireland. January–October 1999.	Limited number of companies paid less than £3.60. In those that did, this usually involved very small numbers of employees. Incentive schemes (usually piecework) were mostly above £3.60. Some disincentive effect upon poor performers. Minimal impact on differentials and employment levels. Other factors more important for sectors: for example high value of pound, competition from overseas.

Low Pay Commission Surveys of Low-paying Firms

Background

- 7 In December 1998 we conducted a postal survey of firms to establish a baseline for assessing how firms adapt to the National Minimum Wage. The survey targeted firms which were likely to make adjustments because of the minimum rates, using a sample provided by trade associations. They covered retail (Retail Trade Alliance), hospitality (British Hospitality Association, the Brewers and Licensed Retailers Association and Business in Sport and Leisure) and business services (Business Services Association and the Cleaning and Support Services Association). We also surveyed firms in all industry sectors using samples provided by the Yorkshire and Humberside Low Pay Unit, Leicester City Council, Leicestershire County Council and Leicestershire Training and Enterprise Council. A copy of the questionnaire is included at the end of this appendix.
- 8 We received over two thousand replies, covering half a million workers. Nine hundred firms in the sample had fewer than twenty-five employees each. The replies included 568 firms (28 per cent) who indicated that they would be directly affected by the minimum wage. A further 413 firms (21 per cent) said that they would be indirectly affected. We found 169 firms (8 per cent) paying 18–21 year olds below the young worker's Development Rate of £3 per hour.
- 9 The results of this first survey were generally supportive of the observations in our First Report. On pay differentials, for example, our report argued that the effects would be limited and localised, petering out in the bottom half of the earnings distribution. The survey provided direct evidence supporting that view. Four-fifths of businesses said that the minimum wage would have no impact on pay differentials. Only 6 per cent of all businesses in the survey expected to raise pay for those earning more than £5.00 per hour.
- 10 The survey also provided evidence that the costs to business of the minimum wage were generally manageable. A quarter of all businesses directly affected expected pay bill increases of under 2.5 per cent as a result of implementing the minimum wage. A fifth of those directly affected expected increases of over 10 per cent. Over a half of those businesses indirectly affected expected no increase in the pay bill.
- 11 About 65 per cent of those directly affected by the minimum wage planned to control labour costs to cope; about 54 per cent planned to make changes to work organisation. A fifth of those directly affected planned to increase investment in development and training.
- 12 Nearly a third of firms affected believed the National Minimum Wage would significantly reduce profits. A fifth said that they would reduce staffing levels. Major change appeared more likely among firms facing higher increases in the pay bill.
- 13 The survey also indicated a wide range of planned responses to the new policy: changes in pay/benefits structure, reductions in hours or jobs, and increasing prices were each indicated by around a tenth of the sample.
- 14 Patterns of responses by industry sector generally supported our understanding of the industries. Distinctive features included:
- Cleaning and security companies were more inclined to react by putting up prices than reduce profits;
 - Hospitality employers were more likely to change their pay/benefits structure and/or raise prices;
 - Retail businesses were more inclined to reduce profits, and more likely to reduce working hours than jobs.

Follow-up Survey

15 In September–October 1999 we conducted a follow-up survey to examine the action taken by firms six months after the National Minimum Wage had been introduced. This survey focused on employers in low-paying sectors, primarily those members of the Retail Trade Alliance (RTA) and British Hospitality Association (BHA), who indicated in the first survey that they would have to raise their pay bill because of the National Minimum Wage. It also included all trade association members in the baseline survey which employed young people. In total, 603 firms were selected for the follow-up survey and 360 firms responded, a 60 per cent response rate. The follow-up questionnaire is also reproduced at the end of this appendix. The responses are summarised in Table A5.2.

Table A5.2

Response to Follow-up Survey			
Selected Sample	Sent	Received	Response Rate
BHA	235	145	62%
RTA	313	193	62%
Other	55	22	40%
<i>All</i>	<i>603</i>	<i>360</i>	<i>60%</i>

16 The survey asked firms to quantify the impact of the National Minimum Wage on their pay bill and on pay differentials. It also asked about actions taken in response to the National Minimum Wage. A summary of the main results is given below.

17 Around three-quarters of respondents in the follow-up survey confirmed that they had been directly affected by the National Minimum Wage, slightly less than the baseline survey anticipated. The proportion of firms which had been directly affected was slightly higher for the RTA (76 per cent) than for the BHA (69 per cent).

Pay Bill Effects

18 Over 85 per cent of respondents indicated that the pay bill increase arising from the National Minimum Wage was at most 10 per cent. The average increase was between 5 and 10 per cent (see Table A5.3). Drawing comparisons with the baseline survey (Table A5.4), just over half of those who responded to both surveys gave estimates within the same range, a third indicated that the actual impact was greater than predicted, with a sixth indicating a smaller effect.

Table A5.3

Increase in Pay Bill as a Result of the National Minimum Wage				
Increase in Pay Bill	0%	0–5%	5–10%	>10%
% of Sample				
BHA	23	34	33	10
RTA	11	26	48	15
Other	10	33	43	10
<i>All</i>	<i>16</i>	<i>30</i>	<i>41</i>	<i>13</i>

Table A5.4

Difference in Pay Bill Estimates: Follow-up Versus Baseline Survey			
Increase in Pay Bill	Same	Less	More
% of Sample			
BHA	55	17	28
RTA	52	15	33
Other	38	31	31
<i>All</i>	<i>52</i>	<i>17</i>	<i>31</i>

Differential Effects

19 Just under a third of firms which were directly affected indicated that they had increased pay for those above the minimum rates. The figure was higher for the RTA than for the BHA. Pay restoration was generally constrained within the bottom of the earnings distribution. Around three-quarters of firms which raised pay above the minimum rates did not do so above £5.00 per hour, and over 85 per cent of firms did not raise pay levels beyond £6.00 per hour.

20 Benefits to Business of the Minimum Wage

A relatively small number of firms in the sample indicated that the minimum wage had led to benefits in terms of turnover (9 per cent of firms), staff motivation (11 per cent of firms) and vacancy filling (6 per cent of firms). In most cases

where benefits occurred they had been slight (see Table A5.5). There appear to have been greater benefits within the hospitality industry than among smaller retailers.

Table A5.5

Has the National Minimum Wage Led to Any Benefits to Business?						
Benefit:	Turnover		Motivation		Vacancy Filling	
	Significant	Slight	Significant	Slight	Significant	Slight
BHA	–	12	1	14	1	8
RTA	2	7	1	6	1	3
Other	–	10	–	19	–	5
<i>All</i>	<i>1</i>	<i>8</i>	<i>1</i>	<i>10</i>	<i>1</i>	<i>5</i>

21 Changes Arising as a Result of the Minimum Wage

Firms undertook a wide range of adjustments in response to the National Minimum Wage. The majority of respondents had made some adjustments to improve productivity as a result of the minimum wage (Table A5.6). The most widely adopted adjustment was to tighten

control of labour costs (67 per cent of firms), followed by changes to work organisation (59 per cent). A significant proportion of respondents had improved the quality of service (31 per cent), increased the use of technology (33 per cent) or increased investment in training (29 per cent).

Table A5.6

Actions Taken to Improve Productivity as a Result of the National Minimum Wage											
Action:	Changed Work Organisation		Tightened Control of Labour Costs		Increased Investment in Training and Development		Increased Use of Technology		Improved Quality of Service		
	Sig.	Slight	Sig.	Slight	Sig.	Slight	Sig.	Slight	Sig.	Slight	
Degree of effect (Sig. = significant)	% of Sample										
BHA	20	29	33	28	7	25	5	21	5	25	
RTA	30	34	40	29	5	21	11	28	11	27	
Other	14	32	33	38	5	24	10	14	10	32	
<i>All</i>	<i>25</i>	<i>32</i>	<i>37</i>	<i>29</i>	<i>6</i>	<i>23</i>	<i>9</i>	<i>24</i>	<i>4</i>	<i>27</i>	

- 22 Almost all affected firms claimed to have had reduced profits as a result of the minimum wage, two-fifths of them significantly. Some 16 per cent of respondents said that staffing levels had been significantly affected, while 13 per cent reported a reduction in working hours (Table A5.7). Some 15 per cent of firms stated that prices had risen significantly.

Table A5.7

Economic Effects of the National Minimum Wage											
Effect:	Changes to Benefit Structures		Reduction in Staffing Levels		Reduction in Number of Working Hours		Increase in Prices		Reduction in Profits		
	Sig.	Slight	Sig.	Slight	Sig.	Slight	Sig.	Slight	Sig.	Slight	
Degree of effect (Sig. = significant)	% of Sample										
BHA	14	24	11	28	6	34	10	36	25	51	
RTA	17	26	22	39	16	44	18	44	50	40	
Other	5	32	9	27	18	36	18	50	48	29	
All	14	26	16	34	12	39	15	42	39	44	

Age-related Pay

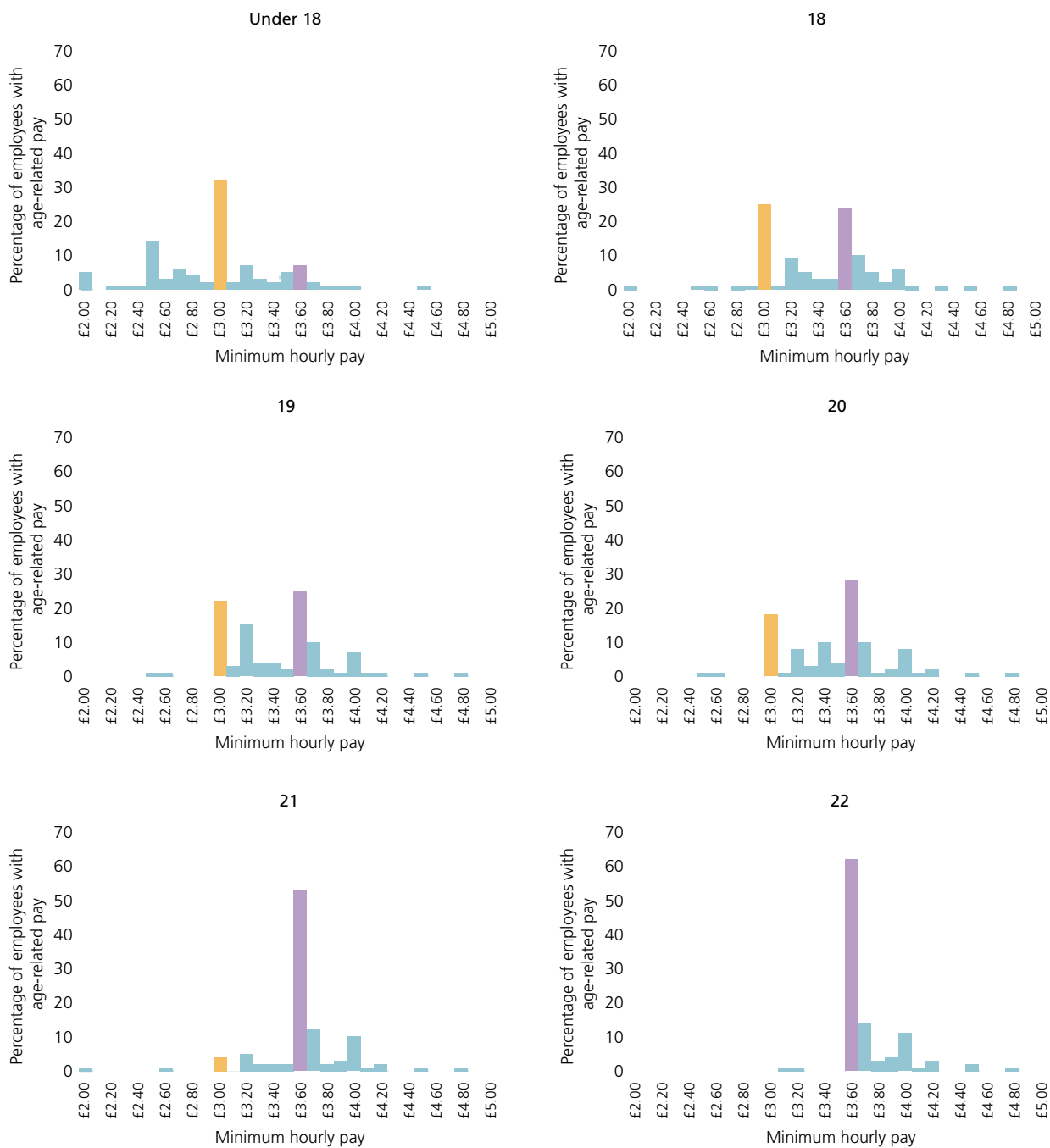
- 23 Just over two-fifths of respondents used age-related pay structures. The figure was higher for the RTA (Table A5.8). Some 16 per cent of businesses had age-related pay structures with adult rates starting at 18 and a similar proportion started at 21. The RTA tended to have adult rates at older ages than the BHA.
- 24 While the majority of firms paid 21 year olds at least £3.60 per hour, over half had minimum pay rates for 18–20 year olds below that figure. In addition, minimum pay rates for under 18 year olds were below £3.00 per hour in 40 per cent of firms. Figure A5.1 opposite shows the distribution of minimum pay rates by age for those firms in the sample.

Table A5.8

	Percentage of Firms With Age-related Pay Starting at Age:									Total with Age-related Pay (%)
	16	17	18	19	20	21	22	23		
BHA	0	1	19	1	1	8	7	0	37	
RTA	2	0	12	3	2	23	5	0	47	
Other	2	0	12	0	0	5	7	0	27	
Total	1	0	16	2	2	16	5	0	42	

Figure A5.1

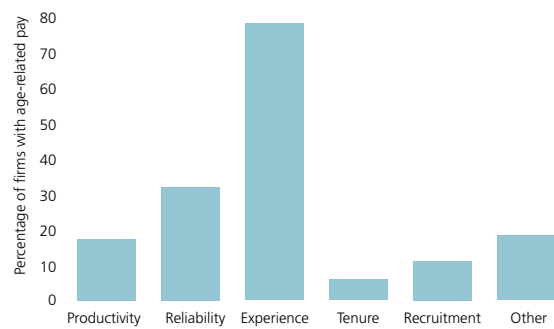
Distribution of Minimum Hourly Pay Rates by Age



25 The most common reason given for using age-related pay systems was experience. This reason was cited by almost three-quarters of the firms with such systems in operation. Reliability was given as a reason by just under a third. Reasons given in the 'other' category included the legal requirements concerning the sale of alcohol and previous Wages Council practice (Figure A5.2).

Figure A5.2

Reasons for Age-related Pay



26 Among those firms not using age-related pay, the most common reason for differentiating pay was again experience (42 per cent) with reliability (36 per cent) and productivity (34 per cent) also figuring strongly.

Conclusion

27 The surveys provide evidence that a significant range of adjustments have taken place where the National Minimum Wage has affected business. While most firms indicated a reduction in profits, many also indicated they had made organisational changes. There is clear evidence that pay restoration has been largely confined to the lower half of the pay distribution. The data on young people broadly confirm the evidence from the NES that only a tiny proportion of 21 year olds are paid less than £3.60 per hour. A significant proportion of firms, however, are paying 18–20 year old employees less than the adult minimum.

28 The surveys have proved extremely useful in establishing a baseline from which to measure the impact of the minimum wage in low-paying sectors. We now have detailed information for a large number of firms directly affected by the minimum wage. This information should be helpful in future evaluation. We hope to publish a fuller analysis of the data early in 2000.

National Minimum Wage Survey: One

PART A

1. **How many workers does your business currently employ (full-time, part-time, casual and all other workers)?**

Total (all ages)

2. **Will the National Minimum Wage affect your business?** *(Please tick box)*

Yes *Please go to Question 3*

No *Please go to Question 9 (and return questionnaire even if nothing further to add)*

PART B *(Applies only if answered yes to Question 2)*

3. **How many workers in your business are:** *(Please insert numbers)*

a) Aged under 18?

b) Aged 18 to 21? Aged 18 to 21 and earn less than £3.60 per hour (excluding overtime)?

c) Aged 22 or over? Aged 22 or over and earn less than £3.60 per hour (excluding overtime)?

4. **What is likely to happen to your TOTAL pay bill as a result of the National Minimum Wage? (Include changes already made in anticipation of the minimum wage.)**

a) No change d) Increase by 5% to 10%

b) Increase by less than 2.5% e) Increase by over 10%

c) Increase by 2.5% to 5% f) Don't know

5. **What is likely to happen to the pay of your workers earning above £3.60 per hour as a result of the National Minimum Wage?**

a) No change *Please go to Question 6*

Pay will rise *Please answer b), c), and d)*

	Yes	No	No one in Pay Band	Don't Know
b) Pay will rise for workers earning £3.60–£4.00 per hour	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c) Pay will rise for workers earning £4.01–£5.00 per hour	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
d) Pay will rise for workers earning £5.01 per hour and above	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

6. As a result of the National Minimum Wage, are you planning any of the following:

(If yes, please tick box)

- a) Changes in work organisation (e.g. working patterns, shift systems, overtime working, the mix of full-time and part-time labour)?
- b) Tighter controls on labour costs (e.g. treatment of absence, paid breaks, staff meals, overtime premia)?
- c) Increased investment in training and development of workers?
- d) Increased use of technology?
- e) Improved quality of service or product?

7. Will the National Minimum Wage mean you have to take ANY of the following action:

	<i>Definitely</i>	<i>Maybe</i>	<i>No</i>	<i>Don't Know</i>
a) Significantly change workers' pay and benefits structures (e.g. payment methods, overtime premia, pay supplements, commission or tips, workers benefits)?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
b) Significantly reduce staffing levels?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c) Significantly reduce working hours?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
d) Significantly increase prices?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
e) Significantly reduce profits?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

8. How important is the National Minimum Wage compared to other factors affecting your business (e.g. customer demand/regulation/interest rates/competition from other businesses)?

Very important Fairly important Minor importance Not important

PART C

9. Please specify any other significant effects of the National Minimum Wage on your business (e.g. in the cost to you of materials, goods or services) or provide more details on any of the above.

National Minimum Wage Survey: Two

1. How many workers in your business are: (Please insert numbers)

a) Aged under 18 b) Aged 18 to 21 c) Aged 22 or over

2. Has the National Minimum Wage directly affected your business? (Please tick box)

Yes go to Question 3 No go to Question 8 (overleaf)

3. What has happened to your TOTAL pay bill as a result of the National Minimum Wage?

a) No significant change b) Increased by less than 5%
c) Increased by 5 to 10% d) Increased by more than 10%

4. Have you increased the pay rates of higher grade staff (e.g. supervisors) to maintain pay differentials as a result of the National Minimum Wage?

a) Yes Please specify the highest hourly rate you had to increase £
(i.e. the rate before the introduction of the minimum wage)
b) No

5. Has the National Minimum Wage led to any of the following benefits for your business?

(Please state whether significant, slight or none.)

	Significant	Slight	None
a) Lower staff turnover	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
b) Higher staff motivation	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c) Faster filling of vacancies	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

6. As a result of the National Minimum Wage, have you taken any of the following actions?

(Please state whether significant, slight or none.)

	Significant	Slight	None
a) Changed work organisation (e.g. working patterns, shift systems, overtime working, mix of full- and part-time labour)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
b) Tightened controls on labour costs (e.g. treatment of absence, paid breaks, staff meals, overtime premia)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c) Increased investment in training and development of workers	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
d) Increased the use of technology	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
e) Improved the quality of service or product	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

7. Has the National Minimum Wage led to any of the following in your business?

(Please state whether significant, slight or none.)

	Significant	Slight	None
a) Changes to workers' pay and benefits structures: (e.g. payment methods, overtime premia, pay supplements, commission or tips, worker benefit)	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
b) Overall reduction in staffing levels	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
c) Reductions in the number of working hours of workers	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
d) Increases in prices	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
e) Reduction in profits	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

8. Do you have age-related pay structures?

Yes

(go to Q9)

No

(go to Q12)

9. At what age is a worker entitled to the adult rate?

10. Enter the current minimum hourly rates for workers in each of the following age groups in your business. If you have no workers in any age band please leave blank

Under 18	<input type="text" value="£"/>	18	<input type="text" value="£"/>	19	<input type="text" value="£"/>	20	<input type="text" value="£"/>
21	<input type="text" value="£"/>	22	<input type="text" value="£"/>	23 or over	<input type="text" value="£"/>		

11. There could be a number of reasons why employers have age-related pay structures. Some of these are listed below. Please tick which, if any, are applicable in your case

Productivity	<input type="checkbox"/>	Reliability	<input type="checkbox"/>	Experience	<input type="checkbox"/>
Tenure	<input type="checkbox"/>	Recruitment	<input type="checkbox"/>		

Other (please specify) _____

12. If there are no age-related pay structures, what other factors account for differences in workers' pay?

Experience	<input type="checkbox"/>	Qualifications/skills	<input type="checkbox"/>	Responsibilities	<input type="checkbox"/>
Length of service	<input type="checkbox"/>	Performance assessment/appraisal	<input type="checkbox"/>		

Other (please specify) _____

13 Use this space to make any other comments about the National Minimum Wage

Appendix 6

Vocational Qualifications and Training Initiatives

- 1 We believe that the minimum wage Development Rates can play a part in encouraging take-up of work-based training, helping not just workers but the overall performance of businesses. This appendix provides details of the Government initiatives designed to improve the employment opportunities for young people by ensuring that all those leaving full-time education and entering the workplace have the maximum opportunity to gain the necessary skills and qualifications. It also gives details of initiatives for older people. Many of these initiatives are new and it will be some time before their effects are measurable. There are some differences between England, Scotland, Wales and Northern Ireland. But, overall, what is being put in place represents a significant attempt to develop a coherent framework for the provision of work-based training.
- Government-funded Work-based Training for Young People**
- England**
- 2 **Modern Apprenticeships** were introduced in September 1995. They are open to young people aged 16–24, provided they can complete the training before their 25th birthday.
 - 3 By 1999 frameworks of training arrangements for Modern Apprenticeships had been developed and agreed with employers through National Training Organisations (NTOs) in eighty-one sectors of industry, business and commerce. Lasting on average for three to four years, a Modern Apprenticeship involves development of key skills and leads to a National Vocational Qualification (NVQ) at Level 3 or above. There is a training agreement which sets out what is expected of the young person and the employer, and each young person is given a Modern Apprenticeship plan which outlines the training content. The aim is that the trainee is employed and paid a wage; where this is not possible, the trainee is linked to an employer or group of employers, and paid a training allowance.
 - 4 At the end of September 1999, there were around 128,000 young people (98 per cent of whom had employed status) on Modern Apprenticeships in England. This compares with 101,000 at the end of September 1997.
 - 5 **National Traineeships**, aimed primarily at 16–18 year olds, were introduced in England and Wales in September 1997 as one of the measures to replace Youth Training. Complementing Modern Apprenticeships, National Traineeships have been designed by employers through NTOs. In 1999, frameworks were in place for fifty sectors of industry, business and commerce.
 - 6 As for Modern Apprenticeships, the young person achieves an NVQ through a structured programme of training, but at Level 2 rather than Level 3. Some people will move from a National Traineeship to a Modern Apprenticeship.
 - 7 At the end of September 1999, over 52,000 young people in England were engaged in National Traineeships compared with almost 16,000 at the end of September 1998. Of these 52,000, around three-quarters had employed status.

Scotland

- 8 Work-based training for young people in Scotland comes under the **'Skillseekers'** programme which replaced Youth Training. Skillseekers was introduced in 1992 and covered the whole of Scotland by 1996, when it was extended to include Modern Apprenticeships. The key elements of Skillseekers are training leading to a qualification up to Scottish Vocational Qualification (SVQ) Level 3, an individual training plan, and employer involvement. The target group is 16–17 year olds, the Youth Training Guarantee Group, although Local Enterprise Companies have discretion to fund training for young people aged 18 and over.
- 9 Modern Apprenticeship frameworks developed by NTOs must be approved by the Scottish Enterprise/Highlands and Islands Enterprise Modern Apprenticeship Implementation Group to ensure they meet the Scottish education and training requirements. In 1997 there were sixty-eight Modern Apprenticeship frameworks endorsed for use in Scotland.
- 10 Additional training opportunities are also available within Skillseekers. Many of these are comparable to National Traineeships; for example in the use of a training agreement and qualification at SVQ Level 2. At the end of September 1999 there were 38,300 Skillseekers (including 12,500 Modern Apprentices), with around three-quarters having employed status. This compares with 40,000 Skillseekers, including 6,000 Modern Apprentices, in September 1997. Proposals for the extension of the Skillseekers programme are being considered by the Scottish Parliament (*Opportunities and Choices*, 1999).

Wales

- 11 Work-based training for young people in Wales is delivered through the **'Skillseekers'** programme. Skillseekers has three distinct components: Modern Apprenticeships (NVQ Level 3) and Higher Modern Apprenticeships (NVQ Level 4); National Traineeships

including Welsh Traineeships (NVQ Level 2); and 'Skillbuild' (training below NVQ Level 2).

- 12 Welsh Traineeships are developed by Training and Enterprise Councils (TECs) and employers through NTOs for those sectors where there is little or no likelihood in the immediate future of a National Traineeship and where there is a demand from employers for such training. The standards will mirror those of a National Traineeship. Skillbuild aims to motivate young people and to give them the skills and competencies they require to progress to further education, skills training or a job. It has two components: Preparatory Training (basic skills) and Occupational Training (competence based training to NVQ Level 1 for those not yet ready for Level 2).
- 13 In 1999 there were 20,000 Skillseekers, including 9,000 Modern Apprentices. This compares with 19,500 in 1998. In 1999, four-fifths of Skillseekers had employed status compared with three-quarters in 1998.

Northern Ireland

- 14 In Northern Ireland, work-based training for young people comes under the **'Jobskills'** framework. Modern Apprenticeships are available to employed status trainees following a training framework which has been approved for delivery under the programme. 'Traineeship' provision focuses on NVQ Level 2. 'Access' offers NVQ Level 1 to young people (including those with learning difficulties or a disability) who are not ready to start Level 2 training. Those on Access training attract an enhanced weekly training fee particularly during their first 13 weeks of initial assessment. Modern Apprentices and those on Traineeships who are offered employment during training normally receive the going rate for the job.
- 15 At September 1999 there were just over 14,000 trainees on the Jobskills programme, of which 5,500 were on the new programme introduced on 1 April 1999 and 8,500 were on its predecessor. Of the 8,500, 1,600 were Modern Apprentices and 3,000

had employed status. Data are not yet available on Modern Apprenticeship levels and employed status for the 5,500 within the new programme.

Training and Development Initiatives

White Paper: Learning to Succeed (England)

- 16 The White Paper *Learning to Succeed* (June 1999), set out proposals for a national Learning and Skills Council to be set up from April 2000. The Council will be responsible for the delivery of all post-16 education and training with the exception of higher education. It aims to provide coherence and reduce bureaucracy. The Further Education Funding Council and TECs will cease to exist. Forty-seven local Learning and Skills Councils will be created to develop local plans.

ConneXions (England) (formerly Investing in Young People)

- 17 Announced as part of the White Paper proposals, ConneXions aims to provide a unified approach to the education and training of 14–19 year olds. A range of measures are being put in place to keep track of young people moving on from compulsory education at 16, and offering support and guidance, especially to the most disadvantaged. Measures include extending the New Start initiative to all parts of England, including funding over sixty pilot projects to identify innovative ways of tackling disaffection among 14–17 year olds; introducing a Learning Card to make young people aware of their entitlement to education and training, and improve the quality of the options available; and giving all 16 and 17 year olds without NVQ Level 2 qualifications the right to paid time off work for study or training. Also among the measures are refocusing the Careers Service towards those with the most need; introducing measures to combat truancy and exclusion from school; introducing a new Learning Gateway for those not ready to access NVQ Level 2

learning, including personal advisers for those who need them; and auditing the Youth Service.

Right to Time Off for Study or Training

- 18 From 1 September 1999 all 16 and 17 year old employees in Great Britain who are not in full-time education and who have not achieved NVQ Level 2 or equivalent are entitled to reasonable time off for study or training for a qualification at that level. The study or training can take place in the workplace, at college or elsewhere, and is during normal working hours. The regulations do not specify the amount or pattern of time off, which is agreed between the parties on the basis of what is reasonable in the circumstances. The time off is paid at the normal hourly rate. It is legally enforceable. The legislation is for Great Britain; Northern Ireland will follow in due course.

Learning Gateway (England)

- 19 The Learning Gateway was introduced in September 1999, providing a client-centred approach to support 16 and 17 year olds through the transition from school to subsequent education or work-based training. The priority groups are those who are disengaged from learning and those who are in danger of becoming disengaged because of a lack of the right skills, qualifications or attitudes, or who face personal or social obstacles. The 'front end' covering outreach, skills assessment, guidance, support and planning is the responsibility of the Careers Service. Every young person will be assigned a personal adviser. A new 'Life Skills' learning option is designed to help young people improve their self-esteem and motivation as well as helping them to develop their basic and key skills. Life Skills provision is the responsibility of TECs, and personal advisers will continue to give support as necessary. Young people will progress from the Learning Gateway into work based training for young people, further education or a job with study/training, where they will continue to receive support from their personal adviser if they need it.

New Start (England)

- 20 The aim of New Start is to motivate and re-engage in learning those 14–17 year olds who have dropped out of education and training or are at risk of doing so. It spans both compulsory schooling and post-16 learning. It is based on partnerships, involving all relevant parties in a local multi-agency approach. This initiative started in September 1997 with 17 partnership projects – all including the Careers Service, schools, further education colleges, TECs, local authorities, the Youth Service and voluntary organisations. It was launched across England on 2 March 1999.

New Deal for Young People

- 21 The New Deal for 18–24 year olds is aimed at young people who have been unemployed and claiming Jobseeker's Allowance for six months. It helps them find work and, more generally, improve their longer-term employability. If they do not find a job within four months of joining New Deal, there are four options: a period of subsidised employment lasting six months; a course of full-time education/training; a job placement with the Environment Task Force; or a job placement in the voluntary sector. By the end of September 1999, around 100,000 young people had moved into unsubsidised jobs lasting more than thirteen weeks. There are similar New Deal initiatives in place for other groups, such as lone parents, long-term unemployed people aged 25 and over, long-term unemployed people aged 50 and over (from April 2000 in Northern Ireland), and disabled people.

Social Exclusion Unit

- 22 The Social Exclusion Unit Report *Bridging the Gap* (July 1999) focuses on 16–18 year olds who are not in education, training or work and the problems they, and society more generally, will face. The report's recommendations are designed to ensure that young people stay in education, training, or work with a strong education/training component until they are at least 18. There are four main elements: a clear outcome to aim for by age

19 – referred to as 'graduation' – requiring as a minimum NVQ Level 2 and also the key skills of communication, numeracy and IT; a variety of pathways to 'graduation' which suit the needs of all young people; a new 'youth card' to assist with transport and other costs; and a new multi-skill support service giving priority to those most at risk of underachievement.

National Skills Task Force

- 23 The National Skills Task Force was set up in Spring 1998 to provide advice on the following: skills needs and shortages in the UK; practical measures to ease skills and recruitment difficulties; likely longer-term changes in skills needs; and how best to ensure that the education and training system responds effectively to the needs identified. The membership is drawn from employers, unions, councils and training agencies. Its first report, *Towards a National Skills Agenda* (July 1998), set out the evidence on skill shortages and skill gaps in the labour force, and listed the issues which need to be addressed in order to build a training and education system in which the supply of skills is more closely matched to the needs of the economy. The second report, *Delivering Skills for All* (May 1999), made substantive recommendations on three fundamental issues: how to build a system which provides a high level of skill for all young people, not just those who go on to degree level study; how to equip everyone with the key skills they need for employability, including those who may have missed out on educational opportunities earlier in life; and how to ensure that all students, potential students and education and training institutions have the information they need on the labour market to make informed choices and to plan ahead. The third report, *Bridging the Adult Skills Gap: Upskilling adults and the role of workplace learning*, is due to be published in January 2000 and will address the linked areas of adult workplace learning, including organisational change, management skills and informal (on-the-job) learning. The final report is due in Spring 2000 and will consider learning

at work for adults, management skills, funding and planning systems, and the role of the various agencies operating in the skills arena. It will take account of the *Learning to Succeed* White Paper and will include recommendations on the shape of a National Skills Agenda.

Lifelong Learning

University for Industry

- 24 The University for Industry (Ufi) was created as a limited company in March 1999. It will operate in England, Wales and Northern Ireland, and will work closely with the separate Scottish Ufi to promote lifelong learning. Its aim is to provide information and advice to 2.5 million people a year by 2002 and create demand for up to one million courses and learning packages a year by 2004. The aim is to overcome barriers to learning such as low expectations, lack of awareness, cost, time and distance. Products and services will be delivered through partners in such areas as the education and training sectors, employers, trade unions, and local, regional and national government bodies.

Individual Learning Accounts

- 25 Individual Learning Accounts (ILAs) support employees buying their own training. The Government has given a commitment to put in £150 to every account, provided the employees put in some money themselves. ILAs will be available through a wide range of financial institutions. The scheme will be run by the forty-seven new local Learning and Skills Councils in England and Wales and by the relevant government departments in Scotland and Northern Ireland.

Scotland

- 26 In September 1998, *Opportunity Scotland* set out the Government's agenda for lifelong learning, and was followed by the consultation paper, *Opportunities and Choices* (1999). There are two

goals: to raise the skills levels in the workforce, and to help young people achieve their full potential. The main policy objectives which should underpin the design and delivery of post-school education and training are seen as being: to help young people to acquire skills and qualifications; to assist young people in finding work, including jobsearch support and careers guidance; to encourage employers to support the training of young people; and to provide additional support to young people who face particular barriers or difficulties in finding employment.

Wales

- 27 *An Education and Training Action Plan for Wales* (March 1999) recommended that the National Assembly for Wales should: secure the basics in education and training from the earliest years; tackle skills needs and reduce social exclusion; and ensure that all training and education provision takes account of labour market information provided by the Future Skills Wales project. The Action Plan also recommended that the Assembly should establish a National Council for Education and Training for Wales accountable to the Assembly and having the lead responsibility, together with the Higher Education Funding Council for Wales, for the resourcing of all publicly-funded education and training post-16. It also recommended establishing a national credit-based qualification and quality assurance framework; introducing local Community Consortia for Education and Training to develop partnerships, promote the integration of provision and better respond to needs; and establishing Careers Wales, a national all-age information, advice and guidance service.

Northern Ireland

- 28 *Strategy 2010*, the report of the Economic Development Strategy Steering Group (March 1999), contains proposals for consideration by the new Northern Ireland Assembly aimed at achieving a vision for the Northern Ireland economy of 'a fast

growing, competitive, innovative, knowledge-based economy where there are plentiful opportunities and a population equipped to grasp them'. This demands 'an education and training system which is fully contributing to the development of a strong, dynamic, participative economy'. To achieve this, it recommends that the 1997 Report of the National Inquiry into Higher Education (the Dearing Report) should be speedily and comprehensively implemented; economic development strategy should inform education and training policy and its funding and delivery mechanisms; collaborative clusters of schools, businesses and colleges should be established; a valued sub-degree level vocational educational programme should be developed; a clearer focus should be given to the Further Education sector; the current system of careers guidance should be enhanced; and teacher training should include an industry placement module.

Appendix 7

Minimum Wage Systems in Other Countries

- 1 Since our first report, there have been few structural changes to minimum wage systems in other countries. This appendix updates information on international minimum wages for 1999. The First Report of the Low Pay Commission and our Review of the Accommodation Offset contain additional information.
- 2 We looked at minimum wage systems in the following countries: Australia, Belgium, Canada, France, Greece, Japan, the Netherlands, New Zealand, Portugal, Spain and the United States (US). These are the major countries with a National Minimum Wage within the European Union and the Organisation for Economic Co-operation and Development. We were assisted in our research by a number of British Embassies and the papers presented at the Low Pay Commission International Seminar, which will be published in Occasional Paper 4.
- 3 For the Republic of Ireland, we report the outcome of its inter-departmental group's report on the minimum wage proposals. We also summarise minimum wage proposals in Jersey and provide updates on recent changes in France, New Zealand, Spain and the US.
- 4 There continues to be significant variation in the rates of minimum wages across countries. Conversions to sterling using purchasing power parities show little variation since the time of our last report. The UK minimum wage remains in the centre of the distribution of minimum rates (see Table A7.1).

Rates

Table A7.1

Full Adult Rates of Minimum Wages Per Hour, November 1999					
Country	Local Currency		Normal Period	Rates	Rates
	Rate Per Hour		(Rate if Not Hourly)	Per Hour ^a (£)	(PPP) Per Hour ^b (£)
Australia ^c	Aus. dollar	9.64	week (385.40)*	3.79	4.83
Belgium	Belg. franc	255.00	month (44,208)	4.06	4.55
Canada ^d	Can. dollar	6.62		2.77	3.74
France	French franc	40.72		3.97	4.10
Greece	drachma	826.00	day (6,195)	1.61	2.34
Japan ^e	yen	638.00		3.74	2.57
Netherlands ^f	guilder	14.38	month (2,367.40)	4.19	4.56
New Zealand	NZ dollar	7.00		2.20	3.15
Portugal	escudo	368.00	month (63,800)	1.17	1.93
Spain	peseta	466.00	month (14: 69,270; 12: 80,815)	1.80	2.43
US	dollar	5.15		3.18	3.38

Sources: *Australian Industrial Relations Commission (1999); Martin (LPC, 2000); all other data from British Embassies.

Notes: a. Calculated using exchange rates at November 1999.

b. PPPs refer to Purchasing Power Parities for final private consumption expenditure for 1998. PPPs should be taken as indicative rather than precise.

c. Federal minimum wage.

d. Weighted average of provincial hourly minimum wages (weighted by the labour force).

e. Weighted average of prefectural hourly minimum wages (using employment weights).

f. Based on working week of 38 hours.

Uprating

- 5 Minimum wages in most countries are uprated through an annual review and evaluation process. A number of countries consult social partnership groups, including employer and employee representatives. These often consider wider economic and labour market factors.
- 6 In some countries, the international uprating of minimum wages is often the result of political as

- well as economic forces. This can lead to frequent increases in the rate, as in France, or large, infrequent increases after political debate, as in the US.
- 7 The use of indexation varies between countries. The Netherlands usually uprates its minimum wage by automatic indexation unless there is specific proof of negative employment effects. In Japan and Spain economic factors such as inflation and productivity levels are considered. Table A7.2 shows details of evaluation and uprating systems in other countries.

Table A7.2

Uprating of Minimum Wages	
Country	Method of Uprating
Australia	Independent body (Australian Industrial Relations Commission) responsible for setting minimum 'safety net' rates for awards and federal rate. Considers economic factors and needs of low paid.
Belgium	Indexation combined with collective bargaining every two years.
Canada	Based on recommendation from provincial Labour Board from time to time, taking into account cost of living and views of employers and employees.
France	Automatic, annual uprating in line with a legal minimum increase. This is calculated on the basis of the annual rate of price increases (excluding tobacco) in the year to May, added to half the value of the averaged increase in hourly purchasing power of manual workers in the first quarter. Before 1999, the Government often increased the level above this legal minimum increase.
Greece	Negotiation between unions and employers. Twice yearly (every January and July), usually in line with inflation.
Japan	Minimum wages reviewed every year in September. Ministry of Labour considers retail price index and Spring wage round.
Netherlands	Ministry of Social Affairs uprates twice yearly (1 January and 1 July) taking account of increase in average wages, unless wages and/or the social security bill have risen too fast. If the ratio between the number of people claiming social benefits and the number of people working exceeds the level of 82.6, the Government may decide not to link the wage to average contractual wage increase (as it did between 1993 and 1996). If the ratio is lower than 82.6 (as has happened since 1996), the minimum wage must be linked to wage growth.
New Zealand	Annual review carried out each year by Minister of Enterprise and Commerce (responsible for Department of Labour). Considers effectiveness of minimum wage in meeting its objectives, impact on employment and unemployment, training and macroeconomy. Invites submissions from New Zealand Council of Trade Unions and New Zealand Employers' Federation, as well as other organisations, before making recommendations.
Portugal	Inter-Ministerial annual review considers social and economic effects of the minimum wage. This includes the expected inflation rate and productivity levels. Following consultation with social partners, the wage is usually uprated annually and implemented from January of each year.
Spain	Uprated annually by a Government decree every December. This follows consultation with the social partners and is based on consideration of the following factors: cost of living index/inflation; productivity; participation levels; and general economic conditions.
US	Changes voted on by Congress intermittently.

Enforcement

- 8 Enforcement is usually through a labour inspectorate. Inspectorates often carry out both active and reactive investigations to ensure compliance with the legislation. Since our first report, we have obtained additional information about enforcement in other countries, in particular the US. For further details, see Table A7.3. Non-compliance is an issue of concern for all countries with minimum wage systems, but in those countries where the minimum wage is long-established, such as the US, there is generally wide compliance.

Table A7.3

Enforcement of Minimum Wages	
Country	Method of Enforcement
Australia	Department of Workplace Relations and Small Business inspectors. Employees can also refer to a Small Claims Court.
Belgium	Labour inspectorate.
Canada	Labour inspectorate. Employees can sue for breach of contract.
France	Labour inspectorate (which is also responsible for general conditions of work, health and safety). There are approximately 500 inspectors and 2,000 assistants. They carry out random checks and investigate complaints from trade unions and individual employees.
Greece	Labour inspectorate. Employers can be sued by employees or by inspectors.
Japan	Labour inspectorate.
Netherlands	Labour inspectorate. Employees can sue.
New Zealand	Labour inspectorate (in Department of Labour) can recover any wages owing or refer case to industrial tribunal, at no cost to the employee. Majority of investigations are resolved without tribunal. No pro-active investigation.
Portugal	Labour inspectorate.
Spain	Labour inspectorate (Dirección General de la Inspección de Trabajo). This inspectorate has the power to enforce a wide range of labour issues, including collectively-bargained rates. Can fine employers; or employee can take case to tribunal to obtain back-pay. Both reactive and pro-active. Around 600 inspectors and 800 assistants, stationed on a provincial basis.
US	Wage and Hour Division in Department of Labor. Both pursues complaints and investigates likely areas of non-compliance. Team of 1,050 inspectors, spread over 62 offices. Enforcement initiatives include 'Eradicating Sweatshops' scheme. These schemes led to the recovery of \$120 million in back wages last year. 70% of investigations follow complaints to regional offices.

Treatment of Young People and Training

- 9 At the time of our previous report, all eleven minimum wage systems (except most of those provincial systems in Canada) had some form of special treatment for workers below age 18. Since that time, there has been one change: Spain abolished differentiation by age in 1999. There continues to be a range in the age variations included in minimum wage systems of other countries (see Table A7.4).

Table A7.4

Age Variations Under Minimum Wage Systems	
Country	Treatment by Age
Australia	Full minimum wage at 21. Below 21 a sliding scale from age 16 (40–50% of the minimum wage) through age 18 (65–80%) to age 20 (85–100%).
Belgium	Minimum wage applies at age 21. If a worker has achieved six or twelve months of active service at this age, increased rates apply. There is a 6% deduction from the minimum wage for each year below 21.
Canada	Full minimum wage at all ages in most Provinces, except for Alberta, Ontario, and North West Territories.
France	Full minimum wage at 18. Workers aged 16 receive 80%; workers aged 17 receive 90% (both for first 6 months only, then the full rate).
Greece	Full minimum wage at 18 (but variation by marital status). Exempt below 18.
Japan	Full minimum wage at 18. Under 18s and over 65s usually receive the lower regional minimum wage rather than the industry rate. (18–65s receive the higher of the regional/industrial rates.)
Netherlands	Full minimum wage at 23. Youth rates are 30% at 15, 45.5% at 18, 72.5% at 21, and 85% at 22.
New Zealand	Full minimum wage at 20. 16–19 year olds get around 60% of the main rates. Youth rate only introduced in 1994; young workers previously exempt.
Portugal	Full minimum wage at 18. Workers below 18 receive 75%.
Spain	Full minimum wage at 16 (since 1999; for details, see paragraph 18).
US	Full minimum wage at all ages, except below 20 where lower rate can apply (approx. 80% of full minimum wage) for first 90 days in the job.

Specific Country Updates

France

- 10 The annual increase of the French minimum wage was announced by the Council of Ministers on 30 June 1999. From 1 July 1999, the Salaire Minimum Interprofessionnel de Croissance (SMIC) increased by 1.24 per cent, from FF40.22 to FF40.72 per hour. In previous years, the French Government had raised the level of the SMIC above the usual legal minimum increase (a formula based on inflation, as outlined above in Table A7.2). In 1999, however, following a report of the Employment and Finance Committee to the Prime Minister on the impact of the SMIC on employment, the annual revaluation did not exceed the formulaic increase. Concern at the prospect of higher labour costs under the proposed 35 hour working week may also have been a factor in the Government's decision. A recent bill for the 35 hour week has proposed that the wages of SMIC recipients should be maintained after the move to fewer hours by means of a complementary payment funded by the employer.

Jersey

- 11 Since publishing our first report, the Government of Jersey has voted to introduce a minimum wage. A Proposition and Report for a minimum wage was lodged for debate on 10 November 1998. The States debated the proposition in March 1999 and approved a recommendation that a minimum wage be introduced at a single hourly rate. But the proposal that the minimum wage be introduced in January 2000 was amended to state that it would be introduced when the necessary financial and manpower resources were available.
- 12 At the time of the minimum wage debate, the States voted to establish an advisory and conciliation service which would be supported by an employment tribunal. The latest employment proposals, if adopted, will introduce legislation on issues such as unfair dismissal and the issuing of a pay statement. These are all deemed necessary for

the smooth functioning of a minimum wage policy. The Report and Proposition on the broader employment proposals are likely to be lodged towards the end of the year with a view to a debate in the States early in 2000.

- 13 An Employment Forum has been established to assist with consultation on the employment proposals, including the minimum wage, and to review and monitor any new legislation that is introduced. Its framework is similar to that of the UK Low Pay Commission. The nine members include an independent chairman, two other independent representatives, three employee and three employer representatives.

New Zealand

- 14 Under the Minimum Wage Act 1983, the Government is obliged to review the minimum wage rate annually. In 1998, however, it decided that an increase in the minimum adult wage would be 'neither responsible nor prudent'. The reasons given included: increasing the minimum wage was not perceived to be a well-targeted method to meet income distribution objectives; the weight of international and domestic research highlighted small negative employment effects for young adults; poor economic and labour market outlook; and a negative forecast growth for the main Asian trading partners.

Republic of Ireland

- 15 The Irish National Minimum Wage Commission made recommendations in April 1998 for the introduction of a national minimum wage in Ireland.
- 16 The Final Report of the Inter-departmental Group on Implementation of a National Minimum Wage was submitted to the Deputy Prime Minister in June 1999. The report endorsed an adult rate of £1r4.40 per hour and a rate of £1r3.08 per hour for those under the age of 18. The social partners were consulted in the preparation of the Final Report, and further consultations took place prior to the drafting of the proposed legislation. The National Minimum

Wage Bill is expected to be published in the near future. The expected enactment date is 1 April 2000.

- 17 It is estimated that 13.5 per cent of employees in the Republic of Ireland will be entitled to higher pay. Over 40 per cent of Irish beneficiaries will be young people under the age of 25. Adjusting for the exchange rate, the Irish minimum wage of €14.40 is equivalent to around £3.55 sterling (November 1999).

Spain

- 18 The age differentiation of the Spanish minimum wage has been altered over the period since 1990. Prior to 1990, there were three rates of minimum wage: one for 16 year olds, one for 17 year olds and one for 18 year olds and above. In 1990 the lower rate for 16 year olds was abolished: hence 16 and 17 year olds were entitled to the same wage. In 1999 the full minimum wage was extended to cover all ages.
- 19 We were informed that the elimination of age differentiation was part of a general reform of the labour market agreed between unions and employers. There is some academic evidence, nevertheless, that the stages of abolition of age differentiation have led to substitution of older workers in the place of teenage workers (Dolado et al., 1996).

United States

- 20 Legislation was introduced in March 1998 to implement a Presidential proposal to increase the minimum wage by \$1.00, to \$6.15 an hour, in two equal instalments in the period up to 1 January 2000. The Senate rejected the legislation later in 1998. On 19 January 1999, Senator Kennedy and Representative Bonior introduced the Fair Minimum Wage Act of 1999. This proposed a fifty cent increase to the \$5.15 rate in September 1999, and a fifty cent increase in September 2000.
- 21 On 9 November 1999, the Senate voted to accept a Republican bill which proposed a \$1 increase in the minimum wage, but spread over the next three years. However, the wage increase has been linked to \$18.4 billion in tax relief for small businesses, which could threaten the survival of the bill since the President has promised to veto 'special interest tax breaks'. But the House version of the minimum wage bill did not reach the floor of the House of Representatives before Congress recessed for 1999. Republican members intend resurrecting the bill next year, but it is unlikely to be debated before February 2000. If passed, reconciliation of the Senate and House bills will begin in early Spring.

Abbreviations

ACAS	Advisory, Conciliation and Arbitration Service	NACAB	National Association of Citizens Advice Bureaux
AEI	Average Earnings Index	NCVO	National Council for Voluntary Organisations
BAHA	British Activity Holiday Association	NES	New Earnings Survey
BATC	British Apparel and Textile Confederation	NGH	National Group on Homeworking
BHA	British Hospitality Association	NHF	National Hairdressers' Federation
BLRA	Brewers and Licensed Retailers Association	NHS	National Health Service
BSA	Business Services Association	NIC	National Insurance Contribution
CAB	Citizens Advice Bureau	NMW	National Minimum Wage
CBI	Confederation of British Industry	NTO	National Training Organisation
CSSA	Cleaning and Support Services Association	NVQ	National Vocational Qualification
DfEE	Department for Education and Employment	NZ	New Zealand
DSS	Department of Social Security	ONS	Office for National Statistics
DTI	Department of Trade and Industry	PAYE	Pay As You Earn
EEA	European Economic Area	PBR	Payment By Results
ESRC	Economic and Social Research Council	ph	per hour
EU	European Union	pw	per week
GB	Great Britain	PLA	Pre-school Learning Alliance
HEA	Hairdressing Employers Association	PPP	Purchasing Power Parity
HMT	Her Majesty's Treasury	PWR	Pay and Workforce Research
IB	Incapacity Benefit	RTA	Retail Trade Alliance
IDS	Incomes Data Services Ltd.	SERPS	State Earnings-Related Pension Scheme
ILA	Individual Learning Accounts	SIC	Standard Industrial Classification
ILO	International Labour Organisation	SME	Small and Medium-sized Enterprises
IRS	Industrial Relations Services Ltd.	SMIC	Salaire Minimum Interprofessionnel de Croissance (French Minimum Wage)
IS	Income Support	SVQ	Scottish Vocational Qualification
IT	Information Technology	TEC	Training and Enterprise Council
JUVOS	Joint Unemployment Vacancy Operating Statistics	TGWU	Transport and General Workers' Union
KFAT	National Union of Knitwear, Footwear and Apparel Trades	TUC	Trades Union Congress
LFS	Labour Force Survey	Ufi	University for Industry
LPA	Leather Producers' Association	UK	United Kingdom
LPC	Low Pay Commission	US/USA	United States of America
LPU	Low Pay Unit	VAT	Value Added Tax
MA	Modern Apprentice	WFTC	Working Families' Tax Credit

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