National Minimum Wage

Low Pay Commission Report 2005

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February 2005

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Chairman's Foreword

The National Minimum Wage was introduced on 1 April 1999, with an adult rate of £3.60. Its introduction benefited about one million low-paid workers and had no measurable adverse effects on employment or inflation. This reflected the deliberately cautious policy of the Commission in setting the initial rate.

From 1999–2002 the minimum wage was increased roughly in line with average earnings, reaching £4.20 in October 2002. These increases also had no significant adverse effects and indeed employment continued to grow strongly in the sectors where low pay is most prevalent. By 2002, however, it had also become apparent that somewhat fewer people had benefited from the minimum wage than originally estimated, due to deficiencies in the labour market data originally available but subsequently improved.

It was against that background that the Commission, in its fourth report published in March 2003, concluded that it was appropriate to increase the effective level of the minimum wage, increasing it faster than average earnings for a number of years, and thus benefiting more workers. In line with our recommendations, the adult minimum wage rose to £4.85 in October 2004, an increase of 15.5 per cent over two years in which average earnings increased by nearly 8 per cent. We also indicated in our fourth report that we believed that some further increase above average earnings would likely be required in subsequent years to arrive at an appropriate long-term level.

This report analyses the impact of the significant upratings over the last two years and considers the appropriate path of the minimum wage over the next two. Our analysis suggests that the upratings have largely been absorbed without adverse effects. Employment continues to grow in most low-paying sectors and the impact on wage bills and profitability appears sustainable. We have therefore concluded that it is safe to propose a further two year period of increase above average earnings.

But we are aware that some businesses have found the significant increase of 2004 a challenge, particularly because of the consequences for pay differentials. And the full impact of the 2004 upratings may not yet be clear in the macroeconomic data. We have therefore erred on the side of caution, proposing an increase only slightly above average earnings, and with a smaller increase in the first year to allow business time to adjust. The implication of this caution, however, is that some further increase relative to average earnings is likely to remain appropriate in subsequent years.

In making our recommendations on the adult rate and the youth Development Rate (which currently applies to 18–21 year olds) we have also needed this year to consider the impact of two other pieces of proposed or prospective labour market regulation: the proposed requirement that bank holidays count as paid holidays in addition to the 20 days required by current legislation, and the forthcoming implementation of anti-age discrimination legislation (the Equal Treatment Directive). The bank holiday proposal would not be an impediment to the medium-term uprating of the minimum wage, and if implemented its full impact would be very unlikely to be felt within the next two years. In our next report, and once the details of its implementation are known, we will consider its impact in more detail. Our recommendations are, however, based on the assumption that the implementation of the Equal Treatment Directive will facilitate the continued use of the youth Development Rate, which plays a key role in protecting the employment prospects of some young people. We believe, however, that the youth Development Rate should most appropriately apply to 18–20 year olds, with 21 year olds paid the adult rate.

The National Minimum Wage has been a great success. It has brought higher wages to many low-paid workers. In combination with the tax and benefits system it has significantly improved the incomes of many low income families. As Chapter 4 describes, it has played a major role in reducing the gender pay gap. And it has achieved these benefits without any significant adverse effects on business or employment creation.

This result reflects the careful way in which the wage has been set and the detailed analysis on which the Commission's decisions are based. As will be clear to readers of this report, that analysis depends upon an enormous amount of hard work by the Commission's secretariat. It is therefore appropriate that I end with my thanks for their support over the last year.

Adair Turner

February 2005

The Commissioners

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Adair Turner
Paul Gates
William Brown

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Executive Summary

Chapter 1: Introduction

The Government set the terms of reference for this report in August 2004. We were asked to monitor the impact and review the levels of the minimum wage and to make any consequent recommendations for change. Subsequently, in October, the Government enlarged the remit, asking us to consider a number of other issues including the incidence of the youth Development Rate and the likely cost to employers of the intention to ensure that bank holidays were not treated as counting towards workers' statutory leave entitlement. We were asked to report by the end of February 2005.

As with previous reports, we have based our recommendations on evidence gathered from a number of sources and by a variety of means. We commissioned thirteen research projects and we carried out a survey of mainly small firms in low-paying sectors. We analysed relevant data provided by the Office for National Statistics. We consulted workers and their representatives and we consulted employers and their representative bodies. We visited different parts of the UK to listen face-to-face to some of the employers and workers most affected by the minimum wage. Finally, in the Autumn of 2004 we undertook a formal process of consultation taking written and oral evidence from a wide range of organisations.

Chapter 2: The Impact of the National Minimum Wage

The October 2003 and October 2004 upratings combined increased the minimum wage by 15.5 per cent compared with an increase in average earnings of just under 8 per cent between October 2002 and October 2004. Before that two year period, the minimum wage had increased since its introduction at a rate roughly equal to average earnings. We now estimate that workers in at least 1.1 million jobs benefited from the 2004 upratings. These are workers whose pay increased between April and October 2004 from below the October 2004 rate to equal or exceed it. We estimate the impact on the aggregate wage bill of pay increases for these beneficiaries to be 0.08 per cent. In addition, many other workers may have benefited from the October 2004 upratings prior to April 2004, when the earnings survey on which we base our estimates was conducted. Many formal pay settlements are implemented in January and early April and any wage increases made then in anticipation of the October increase would not show up in our estimates of beneficiaries.

Low pay continues to be concentrated among certain sectors and groups of workers. The main beneficiaries of the increase in the National Minimum Wage are women, part-time workers, some minority ethnic groups, young people and those who have a work-limiting health problem.

Since our fourth report the UK economy has grown faster than its long-run trend. The labour market continues to be remarkably robust. Employment is at record levels and unemployment is at its lowest for thirty years. Wage and price inflation pressures continue to be relatively subdued.

Overall, employment has increased among the groups of workers and in the sectors most affected by the National Minimum Wage. The main exceptions to this have been agriculture and the textiles, clothing and footwear sectors (the decline is a long-term trend attributable mainly to external factors) and young workers. The low-paying sectors are considered in Chapter 3; young workers are covered in Chapter 5. Among young workers, for those aged 18–21 the fall in employment has eased, remaining largely unchanged since the Autumn of 2003. Employment rates for 16–17 year olds continue to fall. But commissioned independent research found minimal negative impact of the minimum wage on employment.

In written and oral evidence, many employers told us that they were finding it a struggle to accommodate the two consecutive large increases in 2003 and 2004. Our data suggest that there has been only a small impact on the wage bill, but there is evidence suggesting that differentials have been squeezed.

There is little evidence that the minimum wage has had any impact on profits at the macroeconomic level. We did, however, find some evidence of small negative impacts on profits at the individual firm level, but not on a scale that led firms to close down or to lay off workers. We found no significant effects of the minimum wage on either prices or overall productivity, although we found some evidence of small positive effects on labour productivity in the service sector.

We again note the importance of accurate and reliable data on low pay to inform our assessment of the impact of the minimum wage. We therefore welcome the improvements made so far and we would encourage the Office for National Statistics to continue to review and improve the quality of these data.

Public sector workers are generally paid above the National Minimum Wage. The impact on public sector wage bills of the 2003 and 2004 minimum wage upratings has therefore been minimal. The 'Agenda for Change' in the National Health Service will further improve the wages of the public sector workforce.

Chapter 3: The Effects of the National Minimum Wage on Specific Sectors and on Small Firms

We have identified nine sectors of the economy where low pay is common and which are most affected by the minimum wage. These nine sectors provide around six million employee jobs, nearly a quarter of all the jobs in the UK economy. About three-quarters of these jobs are to be found in the retail and hospitality sectors.

We found evidence of continued employment growth in the two largest low-paying sectors and stable or growing employment in most of the others. In the two sectors where job numbers are falling, i.e. the agriculture sector and the textiles, clothing and footwear sector, the decline is part of a long-term trend attributable to external factors. As in previous reports, we found that the cleaning and security industries experience some problems in renegotiating long-term contracts to take account of minimum wage upratings.

The evidence presented to us has suggested that the minimum wage is becoming less of an issue for some small firms, but, conversely, a more significant issue for some large firms. There is, for example, evidence that some larger firms – particularly in the retail sector – are, for the first time, having to make adjustments to their pay structures as a result of recent increases in the National Minimum Wage. Overall we have found no evidence of any insuperable difficulty in coping with the October 2003 upratings, nor have we discovered any negative impact on employment. But our analysis concentrates on the impact of the October 2003 upratings, with only limited data available relating to the October 2004 upratings. We are aware that many employers in the low-paying sectors have expressed concern about the impact of the increase in the adult rate to £4.85 per hour.

We also discuss in this Chapter the complex issue of salary sacrifice, an arrangement whereby a worker agrees to a reduction in pay in return for a non-cash benefit, and note that the National Minimum Wage Regulations do not permit those earning the minimum wage to participate in these schemes. We conclude by recommending that the Government invite us to consider the issue in depth and to report back by February 2006.

We recommend that the maximum daily accommodation offset should increase to £3.90 in October 2005 and £4.15 in October 2006, in line with our recommendations for the adult rate of the minimum wage.

We continue to receive evidence that some local authorities are not taking full account of minimum wage upratings, including the costs of travelling time, when calculating fees for private care provision. We note that progress has been made in this area and recommend that the Government continue to make clear to local authorities that policies on commissioning care should reflect the costs of provision. We also recommend that the Government should monitor the approach of local authorities to the funding of social care. Two further issues which affect the social care sector are 'sleepovers' and on-call arrangements. We believe that greater publicity of the guidance is needed to ensure that the rules are understood.

Chapter 4: Groups of Workers and Specific Enforcement Issues

Women, ethnic minority and disabled workers are disproportionately represented among the beneficiaries of the minimum wage. Two-thirds of the beneficiaries of the 2004 upratings are estimated to be women workers.

We found clear evidence suggesting that the minimum wage has had a major impact in narrowing the gap between the pay of women workers and that of men at the lower end of the earnings distribution. Although still significant, the gender pay gap has also been narrowing slowly for some time in the middle range of the pay distribution independently of any influence of the minimum wage. The minimum wage has now had such a marked effect at the bottom of the distribution that only a very large uprating in relation to average earnings would have much further effect.

Upratings of the minimum wage have also helped to raise the wages of disadvantaged workers, particularly those with work-limiting disabilities, without harming their employment opportunities. In common with the rest of the labour market, the employment situtation of disadvantaged groups has improved in recent years. Indeed, in many respects, those groups whose position in the labour market was weakest have demonstrated the greatest gains in employment.

The pattern of pay by ethnic group is complex. Although some minority ethnic groups suffer a pay penalty compared with the white majority, others do not. Indeed, some men from minority ethnic groups tend to earn more than their white counterparts and black women earn more on average than white women. However, some minority ethnic groups (such as those originating from Bangladesh and Pakistan) continue to earn considerably less than the average. The minimum wage has improved the position of these disadvantaged ethnic groups without adverse employment effects. Indeed employment rates of disadvantaged ethnic groups, though lower than those of white workers, are increasing.

The analysis in this Chapter also reveals the poor position of part-time workers relative to full-time workers. Part-time work is more commonly available in low-paying occupations. While female full-time workers have made significant progress in closing the earnings gap with male full-time workers, the same is not as true of female part-time workers. However, there is no gap between the earnings of female part-time workers and male part-time workers over most of the distribution. This suggests that while the labour market for full-time workers has strengthened, the pay and conditions of both male and female part-time workers has trailed behind.

Homeworkers are a largely hidden workforce. It is estimated that there may be up to one million of them, of whom 90 per cent are probably women, many of them from minority ethnic groups. These workers face particular difficulties in enforcing their rights to the minimum wage. We believe that the new system of fair piece rates, which replaced the fair estimate agreement system, will help improve the situation of homeworkers. However, we continue to believe that this is an important area for enforcement activity. We would welcome any steps taken by the Government to heighten awareness of the minimum wage among these vulnerable workers.

We continue to believe that people with disabilities should be entitled to the minimum wage and recognise that the Government's revised guidance since the publication of our fourth report (2003) has helped resolve many of the uncertainties about entitlement to the minimum wage. But we wish to highlight the fact that minimum wage upratings can result in some disabled people reducing the number of hours they spend in paid employment to avoid breaching the £20.00 per week earnings disregard. We would encourage the Government to take this into account as part of its efforts to increase work incentives for those with disabilities.

Some voluntary sector organisations have pointed to a lack of clarity about the position of volunteers. We recommend that the Government should review and draw together existing guidance into a single source to provide clear and accessible advice to the voluntary sector.

Chapter 5: Young People and Trainees

The number of jobs held by 18–21 year olds that benefited from the October 2004 uprating of the youth Development Rate is estimated at 120,000; this compares with 70,000 benefiting from the October 2003 uprating. In addition, many young people received pay rises as a result of increases in the adult rate. All the available evidence indicates that the minimum wage has not harmed the employment prospects of young people. Employment rates for 18–21 year olds have remained largely unchanged following the October 2003 increases in the minimum wage, though they are below the peaks reached in 2000/01. Total employment levels of young people are increasing, including in low-paying sectors.

The introduction of the 16–17 year old rate in October 2004 benefited up to 45,000 jobs. We will consider the impact of the minimum wage for 16–17 year olds in future reports.

In line with previous experience following a large uprating, the number of young people's jobs being paid below the adult rate of the minimum wage has increased, with a number of firms introducing age-related pay to offset the cost of minimum wage upratings. But other firms are moving in the opposite direction and there is no clear long-term trend. Age-related pay is not widespread and, even in the minority of firms that employ it, its use is often restricted to certain positions or new recruits in the first few months of employment. Where firms have introduced age-related pay, there is evidence that the minimum wage has resulted in age 22 being established as the threshold for payment of full adult rates of pay, whereas previously lower ages tended to be used.

The forthcoming implementation of the Equal Treatment Directive outlawing age discrimination at work increases the need to ensure an appropriate youth Development Rate. We are strongly convinced that there is a need for a youth Development Rate which is lower than the adult rate and that adverse consequences for some young people would result if employers were not able to pay some younger workers below the adult minimum wage level. But we believe that the most appropriate cut-off point between the youth Development Rate and the adult rate is at the 21st birthday. We therefore again recommend that 21 year olds should receive the adult rate of the National Minimum Wage.

The exemptions from the minimum wage for apprentices continue to work well, while the older workers' Development Rate remains little used. We believe that implementation of the Equal Treatment Directive will necessitate a change to the present requirement that apprentices must be under the age of

26 for the 12 months exemption from the minimum wage to apply. Our provisional conclusion is that the older workers' Development Rate should be abolished from October 2006, and that, simultaneously, the 12 months exemption from the minimum wage should be extended to cover all apprentices aged 19 and over. We recommend that the Government invite the Commission to review these provisional conclusions and make firm recommendations on these matters by February 2006.

Chapter 6: Compliance and Enforcement

Effective enforcement of the National Minimum Wage is crucial to its success. As recognised in our previous reports, the vast majority of employers support and comply with the minimum wage. But we continue to be concerned that a minority of workers are still being underpaid. The Inland Revenue has continued to develop and focus its minimum wage enforcement activities in the light of its experience since the introduction of the minimum wage in 1999. Since our fourth report (2003) the Department of Trade and Industry has taken action to address some legislative anomalies that have arisen and which impeded effective enforcement. We welcome the work that has been done by both Departments, but we believe that more could be done to tackle persistent non-compliant employers and to encourage more workers to report underpayment so that they can receive the pay due to them.

Reviewing the evidence, we are concerned that awareness of the minimum wage remains low in some groups of vulnerable workers. To tackle this, we recommend that the Government review its minimum wage publicity strategy to consider how best to target low-paid workers, with particular emphasis on vulnerable groups of workers.

We also now believe that a more significant deterrent to non-compliance by employers is needed. We therefore recommend that the Government should introduce interest charges payable on arrears arising from minimum wage underpayment and financial penalties for seriously non-compliant employers.

Chapter 7: Setting the Rates

The evidence shows that the minimum wage has been a success. The economy has continued to generate new jobs, including in the main low-paying sectors, without any signs of an emergence of wage inflation. Many low-paid workers have benefited. While some firms continue to report difficulties in adjusting to the successive upratings of the minimum wage, the impact on aggregate and sectoral wage bills has been minimal.

Our formal and informal consultations with employers, however, revealed high levels of concern about the effect of the last two upratings and about the potential impact of further significant increases. And the available macroeconomic data do not yet allow an appraisal of the full effects of the uprating of the minimum wage to £4.85 in October 2004. Our assessment therefore needs to balance the available macro data with the input from consultations.

Most of the interested parties accepted the case for an uprating, but there was no consensus. The range of opinions varied from below to substantially above the predicted growth in average earnings.

Balancing these considerations, we believe that there is a strong case for continuing along the path of uprating the minimum wage outlined in the fourth report (2003), with a further increase relative to average earnings over the next two years. But, in the light of the level of employer concern, we judge it appropriate to proceed with caution. For that reason we are recommending that the increase over two years should be above predicted average earnings, but not substantially so. We also consider that the upratings should be phased so that the increase in the first year is modest, allowing employers further time to adjust to the October 2004 uprating. We recommend that the adult rate of the minimum wage should be increased to £5.05 in October 2005 and further increased to £5.35 in October 2006. We recommend that the 2006 uprating be subject to review, both to check that the macroeconomic conditions continue to make it appropriate, and in the light of the implementation of age discrimination legislation as outlined below.

The Government has set out its intention of legislating, during the course of the next Parliament, to ensure that the eight bank holidays count as paid leave in addition to the 20 days of paid leave (for a typical full-time worker) which the law currently requires. In the vast majority of cases this change will make no difference, since about 92 per cent of full-time workers already enjoy at least 20 days paid annual holiday excluding the eight bank holidays. And the overall hourly wage bill impact of the change seems unlikely to exceed 0.4 per cent. But those specific companies which currently do not allow paid bank holidays in addition to the 20 days could face hourly wage bill increases of 3.2 per cent and such companies are likely to be concentrated in low-paying sectors.

We do not believe therefore that the proposed change will have an impact sufficiently large or sufficiently widespread as to make further upratings of the minimum wage inappropriate, but we note that the pace of introduction will determine the severity of adjustment difficulties in specific firms. The timing of the implementation is presently uncertain and dependent both upon Government intentions and the Parliamentary schedule. We have based our recommendations on the assumption that the full impact will not occur within the two years covered by this report. We will take the additional costs into account in future years.

While workers in other age groups have seen their position in the labour market improve, the position of young people has remained more or less static. Our ability to increase the adult rate by slightly more than average earnings depends on the continued existence of the youth Development Rate and the 16–17 year old rate. We believe that the application of the adult rate to younger people would damage their employment prospects. And the existence of separate rates for young people is fully consistent with the Equal Treatment Directive.

Our recommendation of a figure of £5.35 for the adult rate in October 2006 therefore depends on the assumption that the forthcoming UK implementation of the Equal Treatment Directive will continue to allow the straightforward use by employers of the lower rates for younger people. The Commission therefore recommends that it should review its recommendation for October 2006 in February 2006 and confirm it if the implementation of the legislation has been designed to achieve this.

The Commission believes, however, that this reinforcement of the principle of lower rates for younger people should be combined with a change in the upper age limit for the youth Development Rate from the 22nd to the 21st birthday.

We recommend that the youth Development Rate be increased to £4.25 in October 2005 and to £4.45 in October 2006. We recommend an increase slightly lower than the adult rate (and lower than the forecast increase in average earnings) recognising that young people have done less well in the labour market and in the expectation that the Government will recognise the case for extending the adult rate to 21 year olds.

In our fourth report we said that we believed that there was a case for increasing the effective level of the minimum wage. The increase we have recommended over the next two years will again exceed the predicted growth of average earnings. We have, however, kept the adjustment above average earnings small, and concentrated it in the second year to allow business time fully to absorb the impact of the increases.

However, it remains our view that some further increases relative to average earnings will be required in subsequent years to bring the minimum wage to an appropriate long-term level.

We make no recommendations with regard to the 16–17 year old rate. We propose instead that the Government invite us to review the operation of the 16–17 year old rate in 2005 and report in February 2006 with recommendations for any subsequent increase suitably adjusted to take account of the absence of any uprating in 2005.

Recommendations

National Minimum Wage Rates

The adult rate of the minimum wage should be increased to £5.05 in October 2005. The rate should be further increased to £5.35 in October 2006, subject to confirmation by the Commission in February 2006 following a review to check that the macroeconomic conditions continue to make it appropriate, and in the light of the implementation of age discrimination legislation. (Paragraph 7.36)

The youth Development Rate should be increased to £4.25 in October 2005 and £4.45 in October 2006. (Paragraph 7.38)

The Government should invite the Commission to review the operation of the 16–17 year old rate (above compulsory school age) and to report in February 2006, with recommendations suitably adjusted to take account of the absence of any uprating in 2005. (Paragraph 7.41)

Young People

Twenty-one year olds should receive the adult rate of the National Minimum Wage. (Paragraph 5.48)

Training

We have provisionally concluded that the older workers' Development Rate should be abolished from October 2006 and that, simultaneously, the 12 months exemption from the minimum wage should be extended to cover all apprentices aged 19 and over. The Government should invite the Commission to review these provisional conclusions and make firm recommendations on these matters by February 2006. (Paragraph 5.60)

Awareness

The Government should undertake a review of its minimum wage publicity strategy to consider how best to target low-paid workers more pro-actively, with particular emphasis on vulnerable groups of workers. (Paragraph 6.9)

Enforcement

The Government should introduce interest charges payable on arrears arising from minimum wage underpayment and financial penalties for seriously non-compliant employers. (Paragraph 6.48)

Salary Sacrifice

The Government should invite the Commission to review the issue of salary sacrifice in depth and to report by February 2006. (Paragraph 3.27)

Accommodation Offset

The accommodation offset should increase in line with the adult rate of the minimum wage, rising to £3.90 per day from October 2005 and £4.15 per day from October 2006. (Paragraph 3.40)

Social Care Sector

The Government should continue to make clear to local authorities that policies on commissioning care should reflect the costs of provision, including payment of travelling time. The Government should monitor the approach of local authorities, examine the reasons for any uneven provision and, if appropriate, provide further guidance. (Paragraph 3.71)

Volunteers

The Government should review and draw together existing guidance into a single source to provide clear and accessible advice to the voluntary sector. (Paragraph 4.54)

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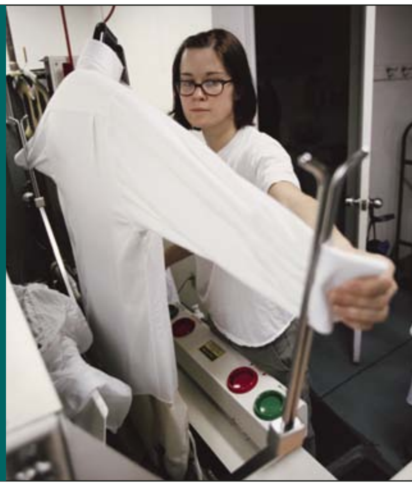
Introduction



The Government set the terms of reference for this report in August 2004. We were asked to monitor the impact and review the levels of the minimum wage and to make any consequent recommendations for change. Subsequently, in October, the Government enlarged the remit, asking us to consider a number of other issues including the incidence of the youth Development Rate and the likely cost to employers of the intention to ensure that bank holidays were not treated as counting towards workers' statutory leave entitlement. We were asked to report by the end of February 2005.

As with previous reports, we have based our recommendations on evidence gathered from a number of sources and by a variety of means. We commissioned thirteen research projects and we carried out a survey of mainly small firms in low-paying sectors. We analysed relevant data provided by the Office for National Statistics. We consulted workers and their representatives and we consulted employers and their representative bodies. We visited different parts of the UK to listen face-to-face to some of the employers and workers most affected by the minimum wage. Finally, in the Autumn of 2004 we undertook a formal process of consultation taking written and oral evidence from a wide range of organisations.

Background

1.1 Four years ago we recommended that the minimum wage should be reviewed every two years and that a report should be issued in February so that recommendations could be implemented the following October. This report follows that cycle. It builds on previous reports, reflects on the impact of the minimum wage since its introduction, but particularly over the past two years, and looks forward over the next two.

1.2 The National Minimum Wage was introduced nearly six years ago on 1 April 1999. Since its introduction amid controversy, it has become an accepted part of the UK labour market scene. For many, it has proved an unadulterated success story. However, as our consultation and our visits reminded us, aspects of the minimum wage still cause some people concern. Some of the employers we met were concerned at the pace of recent increases to the minimum wage and many raised concerns about the difficulty of maintaining differentials. And there was no shortage of union voices calling for a more substantial rate of increase and for the adult rate to apply to all workers regardless of age.

1.3 This introductory Chapter explains how we have gone about our task. It sets out how we collected the information which has informed our debates and discussions, and the evidence which underpins our conclusions and recommendations. We have aimed to combine an understanding of high level economic issues with an appreciation of specific implementation problems. We have relied on academic research and analysis of statistical data, but not exclusively. We have also taken account of discussion, debate and personal testimony.

Terms of Reference

1.4 In August 2004, the Government set out the terms of reference for our 2005 report. We were asked to:

- continue to monitor and evaluate the impact of the National Minimum Wage, with particular reference to the effect on pay, employment and competitiveness in low-paying sectors and small firms; and the effect on pay structures; and
- review the levels of each of the different minimum wage rates and make recommendations, if appropriate, for change.

1.5 In making any recommendations for future rate changes, we were asked to have regard to the wider social and economic implications; the likely effect on employment levels; the impact on the costs and competitiveness of business; and the potential costs to industry and the Exchequer. We were also asked to report on the effect that the minimum wage has had on the gender pay gap and the pay of ethnic minority and disabled workers since its introduction.

1.6 In October 2004, the Government wrote to us again enlarging our remit. The Commission was asked to:

- consider whether there was evidence of any significant increase in the number of employers paying 18–21 year old workers lower rates than adults and to advise on the reasons for any such increase;

- factor into our deliberations the increased cost to employers of the Government's intention to make bank holidays additional to the existing annual leave entitlement of twenty days;
- continue to cooperate with the new Women and Work Commission;
- consider whether salary sacrifice schemes involving childcare vouchers should be allowed to count towards minimum wage pay.

1.7 The Commission considered the last point carefully and came to the conclusion that the issue of childcare vouchers could not be properly considered in isolation from the wider issue of non-pay benefits as a whole. This meant that we were not in a position to produce the advice required within the timescale requested. We explained this to the Government in late October. We return to the subject of salary sacrifice in Chapter 3 when we consider the retail sector in more detail and suggest that the Government invite us to give the matter detailed consideration for inclusion in our next report.

Research

1.8 Academic research into the effects of the minimum wage provides us with an important source of insight. After a tendering exercise, we commissioned twelve research projects designed to help us arrive at our recommendations for this report. We were looking for answers to questions such as: what has been the impact of the minimum wage over time on the hours people work and the number of second jobs? What is the extent of non-compliance? What are the effects of the minimum wage at the level of the individual business in those sectors most affected? Has it harmed employment prospects in any of the most affected sectors for any of the groups most likely to be at risk? Who benefits most from the minimum wage? What has been the impact on productivity?

1.9 In September 2004 we organised a one day workshop to enable researchers to share their emerging findings with each other and the Commission. A fuller list of the research projects and a summary of findings is set out in Appendix 2. We will publish the research reports on our website (www.lowpay.gov.uk) and make them available for study in certain libraries.

1.10 In addition to the research projects mentioned above, in October 2004 we commissioned additional research from Incomes Data Services (IDS) to help us address the part of the remit relating to the extent of the use of the youth Development Rate by employers. We draw on that research when we address this subject in Chapter 5.

Low Pay Statistics

1.11 In previous reports we have drawn attention to problems with the official data on low pay and acknowledged the work that the Office for National Statistics (ONS) has done to improve the accuracy of data relating to low-paid workers.

1.12 There have been noticeable improvements in the quality of low pay statistics. We note that the ONS has responded positively to many of our earlier comments and we have been able to place greater confidence in official data this time round. We are confident that the improvements in train – for example the introduction of the Annual Survey of Hours and Earnings (ASHE) in place of the New Earnings Survey (NES) – will provide even more reliable data in the longer term. Appendix 7 sets out the changes made so far and those planned. We would like to record our thanks to the ONS for the significant work it has done to improve the data on low pay.

Visits

1.13 We regard visits as an essential part of our programme. During 2004 Low Pay Commissioners undertook eight visits to different urban and rural areas of the UK: the West Midlands, Edinburgh, Belfast, the North East of England, Kent, Cardiff, Leeds and Cambridgeshire. In the course of these visits we spoke to a wide variety of people affected by the minimum wage. We met homeworkers, representatives of major supermarket chains, cleaners, owners of hairdressing salons, staff from Citizens Advice Bureaux and employment agencies, farmers and shelf stackers – among others. As in previous years, we found that talking to people directly often added a dimension of understanding that could not be arrived at by any other means.

1.14 In addition to the visits we undertook as Commissioners, the LPC secretariat arranged many more meetings and visits with interested parties. During 2004 members of the secretariat met a wide range of officials from different Government Departments, dozens of businesses and firms, and unions and employer representatives from all sectors of the economy most affected by the minimum wage.

1.15 A list of the organisations we visited is provided in Appendix 1. We are grateful to everyone we saw and also to the many people who helped us to arrange the visits.

Postal Survey

1.16 In the Summer of 2004 we conducted a survey of employers in low-paying sectors to find out what they thought about the minimum wage in general and about the impact of the October 2003 upratings in particular. In designing the survey, we followed the broad outline of previous LPC surveys so as to facilitate comparison. We employed NOP World to administer the survey.

1.17 Questionnaires were sent to over 32,000 employers in low-paying sectors with a deliberate bias toward smaller firms. We received 3,130 completed questionnaires – a response rate of about 10 per cent. As expected, those who completed the survey tended to be companies with concerns about the National Minimum Wage. Many of the concerns expressed, for example about the rate of increase and difficulty of maintaining differentials, were consistent with much of our other evidence.

1.18 We are grateful to those businesses that took the time to complete the questionnaires. Further information about the survey and details of the results are set out in Appendix 3.

Consultation

1.19 In addition to our programme of visits, we launched a formal consultation process in August 2004. We wrote to hundreds of bodies inviting them to submit written evidence on the impact of the minimum wage and related issues.

1.20 More than eighty organisations sent in written evidence. Some submissions took the form of detailed reports with attached survey findings, others responded in letters of various length and detail. The Government delivered cross-Departmental evidence co-ordinated by the Department of Trade and Industry (DTI). As with previous Low Pay Commission consultation exercises, much of the material we received was impressive. Appendix 1 lists the written submissions. All of the written evidence received will be made available in selected university libraries, except in cases where the respondent has requested that it be treated in confidence.

1.21 In our attempt to understand as fully as possible the practical impact of the minimum wage on firms, we also approached trade associations to invite firms in low-paying sectors to produce case studies detailing the actions they took to respond to the minimum wage. Twelve firms sent us such studies. As might be expected, we said that we would treat this information as confidential, but we would like to place on record our thanks and appreciation of those companies that took the trouble to prepare and send in case studies.

1.22 In addition to the formal written consultation process, the Commission spent three days taking oral evidence. During that time we heard from the TUC, the CBI and many other key organisations representing employers and workers in low-paying sectors. These discussions were valuable in that they often provided an opportunity to seek clarification, exchange views or debate an issue in a way not possible in written consultation.

1.23 A list of the organisations which gave oral evidence is provided at Appendix 1.

Conclusion

1.24 In February 2003 we recommended two consecutive increases above predicted average earnings, bringing the adult rate of the minimum wage to £4.85 by October 2004. We said at the time that we thought there was a case for increasing the effective level of the minimum wage, implying a series of increases for a number of years above average earnings.

1.25 Our task this time was to review, in the light of available evidence, the impact of our last decision to recommend two significant upratings. We also needed to revisit the commitment to increase the effective level of the wage and consider if it still held good. We had to do both before we could make a decision as to our recommendations for 2005 and 2006. The Chapters that follow provide the evidence for our conclusions and lead to our recommendations concerning future rates in Chapter 7.

1.26 This report also looks at ways of improving the operation of the National Minimum Wage including compliance and enforcement. We have discussed operational aspects of the policy with officials in the Inland Revenue, HM Treasury and the DTI and we have had similar discussion with other interested groups. Our recommendations have been shaped by such discussions.

1.27 The next Chapter assesses the overall impact of the minimum wage so far, looking in particular at the effect of the October 2003 upratings. The impact of the October 2004 upratings is more difficult to assess since earnings data for October 2004 are not yet available, but some of its impact is likely to be reflected in an analysis of earnings and employment earlier than October 2004, given that some employers appeared to anticipate the October increases at least six months in advance. In Chapters 3–5 we look in more detail at the impact on particular sectors and groups of workers. Chapter 6 addresses awareness and the important issue of compliance and enforcement of the minimum wage. Chapter 7 sets out our recommendations.

The Impact of the National Minimum Wage

The October 2003 and October 2004 upratings combined increased the minimum wage by 15.5 per cent compared with an increase in average earnings of just under 8 per cent between October 2002 and October 2004. Before that two year period, the minimum wage had increased since its introduction at a rate roughly equal to average earnings. We now estimate that workers in at least 1.1 million jobs benefited from the 2004 upratings. These are workers whose pay increased between April and October 2004 from below the October 2004 rate to equal or exceed it. We estimate the impact on the aggregate wage bill of pay increases for these beneficiaries to be 0.08 per cent. In addition, many other workers may have benefited from the October 2004 upratings prior to April 2004, when the earnings survey on which we base our estimates was conducted. Many formal pay settlements are implemented in January and early April and any wage increases made then in anticipation of the October increase would not show up in our estimates of beneficiaries.

Low pay continues to be concentrated among certain sectors and groups of workers. The main beneficiaries of the increase in the National Minimum Wage are women, part-time workers, some minority ethnic groups, young people and those who have a work-limiting health problem.

Since our fourth report the UK economy has grown faster than its long-run trend. The labour market continues to be remarkably robust. Employment is at record levels and unemployment is at its lowest for thirty years. Wage and price inflation pressures continue to be relatively subdued.

Overall, employment has increased among the groups of workers and in the sectors most affected by the National Minimum Wage. The main exceptions to this have been agriculture and the textiles, clothing and footwear sectors (the decline is a long-term trend attributable mainly to external factors) and young workers. The low-paying sectors are considered in Chapter 3; young workers are covered in Chapter 5.

Among young workers, for those aged 18–21 the fall in employment has eased, remaining largely unchanged since the Autumn of 2003. Employment rates for 16–17 year olds continue to fall. But commissioned independent research found minimal negative impact of the minimum wage on employment.

In written and oral evidence, many employers told us that they were finding it a struggle to accommodate the two consecutive large increases in 2003 and 2004. Our data suggest that there has been only a small impact on the wage bill, but there is evidence suggesting that differentials have been squeezed.

There is little evidence that the minimum wage has had any impact on profits at the macroeconomic level. We did, however, find some evidence of small negative impacts on profits at the individual firm level, but not on a scale that led firms to close down or to decrease employment. We found no significant effects of the minimum wage on either prices or overall productivity, although we found some evidence of small positive effects on labour productivity in the service sector.

We again note the importance of accurate and reliable data on low pay to inform our assessment of the impact of the minimum wage. We therefore welcome the improvements made so far and we would encourage the Office for National Statistics to continue to review and improve the quality of these data.

Public sector workers are generally paid above the National Minimum Wage. The impact on public sector wage bills of the 2003 and 2004 minimum wage upratings has therefore been minimal. The 'Agenda for Change' in the National Health Service will further improve the wages of the public sector workforce.

Introduction

2.1 The National Minimum Wage was introduced in April 1999 and we now have over five years of data and experience with which to assess its impact. The initial level was set at £3.60 an hour (the adult rate) for those aged 22 and over, and £3.00 an hour (the youth Development Rate) for those aged 18–21. Those under 18 years of age were not covered at the outset. By October 2004, the adult minimum wage had risen to £4.85, the youth Development Rate was £4.10 and a new rate had been introduced at £3.00 for 16 and 17 year olds (above compulsory school age). Details of the different minimum wage rate levels since the introduction of the National Minimum Wage are set out in Table 2.1.

Table 2.1 National Minimum Wage Hourly Rates, April 1999–October 2004

	Age 16–17	Age 18–21	Age 22 and over
April 1999–May 2000		£3.00	£3.60
June 2000–September 2000		£3.20	£3.60
October 2000–September 2001		£3.20	£3.70
October 2001–September 2002		£3.50	£4.10
October 2002–September 2003		£3.60	£4.20
October 2003–September 2004		£3.80	£4.50
October 2004–	£3.00	£4.10	£4.85

2.2 In this Chapter, we assess the impact of the minimum wage since its introduction, focusing in particular on the last two upratings in October 2003 and October 2004. We consider in turn, the number of jobs affected, and thus the number of beneficiaries, the impact on earnings and differentials, the impact on the labour maket (including employment, unemployment, inactivity, hours, vacancies and pay settlements), and the impact on firms (including wage bills, profits, productivity and prices, as well as the impact on business start-ups and failures). We conclude with an overall assessment and the identification of areas for future research.

Beneficiaries

2.3 In this section we estimate the number of jobs which have benefited from the October 2003 and October 2004 upratings. First, we explain our reasoning for looking at coverage and consider some methodological difficulties in making these calculations. Then we look at how many jobs in April each year are paid below the forthcoming October's minimum wage and see how this has varied since the introduction of the minimum wage. Third, we use this data as an input to our estimates of the number of jobs that have benefited from the 2003 and 2004 upratings. Finally, we investigate the characteristics of the expected beneficiaries of the 2004 October upratings in terms of gender, hours worked, age, ethnicity, disability, region, sector and size of firm.

Methodological Difficulties

2.4 It is important to be able to calculate the coverage of the minimum wage – the number of people who benefit from the National Minimum Wage – but it is not straightforward. The number of beneficiaries is important not because the Low Pay Commission has a target figure in mind; we do not. But it makes little sense to have a minimum wage that does not benefit a reasonable number of people. And a minimum wage that affected too many would almost certainly be counter-productive. However, knowing the scale of coverage is important chiefly as an indicator of stability. If there are no discernible adverse effects at a given level of coverage, we can be reasonably sure that maintaining that level, or increasing it slightly, would not present major future risks.

2.5 Looking back over previous reports, we note that our forecasts of prospective beneficiaries ('forward-looking estimates') have tended to predict a higher number of beneficiaries than calculations made after an uprating has been introduced ('post-uprating estimates')[1]. In our fourth report (2003), we said we would investigate the reasons for this, reviewing our estimation methodology. We came to three main conclusions.

2.6 First, we considered whether the tendency results from the fact that estimating beneficiaries in advance requires an assumption about the forecast growth of average earnings. We concluded it does not. In fact, actual average earnings growth has tended to turn out slightly lower than the forecasts we have used looking forward. If anything, our use of forecast average earnings growth would have tended to underestimate the number of beneficiaries.

2.7 Second, we investigated the reliability of the earnings data on which our estimates are based. It is clear that earnings data deficiencies did cause an overestimate of the number of beneficiaries at the introduction of the minimum wage. Since then, however, the data have improved and we do not believe that data deficiencies have been a significant determinant of the undershooting effect in recent years. Further details of the changes to the Office for National Statistics (ONS) data and methodology are given in Appendix 7.

2.8 Finally, we found one key reason why forward-looking estimates of beneficiaries have tended to exceed post-uprating estimates: the early anticipation of minimum wage upratings. Many large employers, whose main pay settlement dates continue to be in January and April, implement future minimum wage increases before mid-April, the period when the ONS earnings survey is conducted. This will have the effect of reducing our post-uprating estimates of beneficiaries which are based on the number of workers who are calculated to have received a pay increase to bring them up to or above the minimum wage level between mid-April and October of any year.

2.9 We are unable at present to quantify this effect, but it will clearly tend to reduce post-uprating estimates of beneficiaries, and may fully explain the difference between forward-looking estimates and post-uprating estimates. If it does, then it should be noted that the forward-looking estimates are the more accurate measure of the number of

1 It should be noted that, although we carry out these estimates after the upratings, we use data from the mid-April that precedes the upratings.

direct beneficiaries of the minimum wage i.e. it is our post-uprating estimates which are undercounting beneficiaries rather than our forward-looking overestimating them.

Jobs Paid Below the Minimum Wage in April 2004

2.10 ONS data show that some workers are being paid below the minimum wage. The Annual Survey of Hours and Earnings (ASHE) estimates for April 2004 show that 272,000 jobs were held by people aged 18 or over with hourly pay below the appropriate National Minimum Wage. This represents 1.1 per cent of the total number of UK jobs. 227,000 jobs were held by people aged 22 and over (1.0 per cent of jobs held by those in this age group) with pay less than £4.50 per hour (the then adult rate). A further 45,000 jobs were held by 18 to 21 year olds (2.4 per cent of jobs held by those in this age group) with pay below £3.80 per hour (the then youth Development Rate). As can be seen in Table 2.2, most of these jobs were part-time and held by women.

Table 2.2 Jobs Paid Below the October 2003 National Minimum Wage by Gender and Hours of Work for Those Aged 18 and Over, UK, April 2004

	Men		Women		All jobs	
	000s	Per cent	000s	Per cent	000s	Per cent
Full-time	72	0.6	59	0.8	131	0.7
Part-time	31	2.7	110	2.2	141	2.3
All	103	0.8	169	1.4	272	1.1

Source: ONS low pay methodology estimates using ASHE 2004, with supplementary information.

2.11 The figures should not be used to calculate the number of workers being denied their legal right to the minimum wage. Some workers may legitimately be paid below the minimum wage and it is not possible to tell from the data whether an individual is entitled to the minimum wage. For example, it is not possible to identify those who are exempt from the minimum wage or are entitled to lower rates because of certain types of training (covered by the exemption for apprentices and the older workers' Development Rate). If workers receive free accommodation, employers are entitled to offset hourly rates by up to £3.75 per day. Further, some homeworkers may not receive the full minimum wage rate. We go on to discuss issues of compliance and enforcement in Chapter 6.

2.12 Revised estimates of those paid below the applicable minimum wage for 1998–2003 using the new ONS methodology and revised data are given in Table A7.1 in Appendix 7. Estimates using the old and new methodologies are compared in Table A7.2.

Jobs in April Paid Below the Forthcoming October Minimum Wage

2.13 Table 2.3 shows that the percentage of adult jobs paid below the minimum wage in April each year, which as noted above was 1.0 per cent in 2004, has tended to fluctuate around that level. But on average, in April each year, a further five per cent are paid below the hourly rate at which the minimum wage is due to be fixed in six months time (the ASHE survey is conducted in mid-April each year). As we would expect, this percentage is higher when a large increase in the minimum wage is planned, such as in 2003 and 2004, than when a smaller rise is expected, such as in 2000 and 2002. The percentage for 2004 is similar in magnitude to that for 2001, when the minimum wage increased by over ten per cent. A similar analysis is conducted for young workers in Chapter 5.

Table 2.3 Adults (Aged 22 and Over) Earning Below the Existing National Minimum Wage and the Forthcoming National Minimum Wage Rate, 1999–2004

Data year (April)	Adult minimum wage rate (in April) (£)	Proposed October adult minimum wage rate (£)	Number of adults earning less than the adult rate in April (thousands)	Number of adults earning less in April than the proposed October rate (thousands)	Percentage of employee jobs with wages less than the adult rate in April	Percentage of employee jobs with wages in April less than the proposed October rate
1999	3.60	£3.60	458	458	2.1	2.1
2000	3.60	£3.70	195	746	0.9	3.3
2001	3.70	£4.10	207	1,326	0.9	5.9
2002	4.10	£4.20	290	920	1.3	4.1
2003	4.20	£4.50	211	1,022	0.9	4.5
2004	4.50	£4.85	232	1,399	1.0	6.2
2004a	4.50	£4.85	227	1,237	1.0	5.5

Source: ONS central estimates using ASHE and LFS for 1999–2004. ONS estimates using ASHE with supplementary information for 2004a.

Jobs Benefiting From the 2003 and 2004 Upratings

2.14 While noting the danger of underestimating beneficiaries as a result of the ‘anticipation’ effect discussed above, for consistency we use the same method as in previous reports to estimate the number of beneficiaries of the 2004 upratings. This method entails calculating how many workers are expected to have received a wage increase between April and October to bring them from below to at least the October minimum wage level. Calculating this estimate, however, requires an assumption of what wage increases would have occurred in the absence of the National Minimum Wage. We make our estimates using two alternative assumptions: that the earnings of the low-paid would have risen in line with average earnings during this period; or that they would have risen in line with prices.

2.15 To estimate the number of beneficiaries using either of these assumptions, we calculate a 'downrated' equivalent value in April of the October minimum wage rate[2]. Using the earnings assumption (and with earnings growing at 4.2 per cent per annum in October 2004) an adult earning £4.75 or more in April 2004 was likely to have received a wage increase that would take them above the £4.85 October 2004 minimum wage rate and is therefore not counted as a beneficiary. The equivalent 'downrated' figure using the earnings assumption for youths (aged 18–21) was £4.00 (versus the October rate of £4.10) and for 16–17 year olds £2.95 (versus the October rate of £3.00). Downrating by prices (which were growing at 2.2 per cent per annum in 2004) would give us £4.80, £4.05, and £3.00 respectively. Employees have to be earning below these levels in mid-April 2004 to count as beneficiaries.

2.16 As Table 2.4 indicates, in our fourth report (2003) using data from Spring 2002, we estimated that around 1.7 million jobs would benefit from the October 2004 upratings using the earnings assumption. In the subsequent 2004 report, using data from Spring 2003, we revised our estimates downwards to 1.6 million. The latest estimate is that since April 2004, 1.1 million jobs have directly benefited from the 2004 upratings but crucially many more may have received the benefit of an anticipatory wage increase before April.

2 Rounded to the nearest 5p.

Table 2.4 Estimated Beneficiaries from the 2003 and 2004 Upratings Using the Earnings Assumption[3]

		October 2003		October 2004	
		Thousands	Per cent	Thousands	Per cent
Fourth report[1] (March 2003)	Adults	1,200	5.2	1,600	6.9
(Spring 2002 data)	Youths	80	6.3	100	7.6
	All	1,300	5.2	1,700	6.9
2004 Report[2] (March 2004)	Adults	1,000	4.3	1,500	6.2
(Spring 2003 data)	Youths	70	4.3	110	6.2
	All	1,100	4.3	1,600	6.2
2005 Report[2] (February 2005)	Adults	900	3.8	1,000	4.4
(Spring 2003 data for 2003)	Youths	70	4.3	120	6.3
(April 2004 data for 2004)	All	900	3.8	1,100	4.6

Sources: Fourth report (2003), 2004 Report (2004). LPC calculations for this report based on ASHE/LFS central estimates for 2003, and ASHE with supplementary information for 2004.

Notes:

1. Youths are aged 18–20 and adults 21 and over in the fourth report estimates.
2 .Youths are aged 18–21 and adults 22 and over in these estimates.
3. The numbers for youths are rounded to the nearest 10,000. The numbers for adults are rounded to the nearest 100,000.
4. Estimates of the percentages of gainers are rounded to the nearest 0.1 per cent.

2.17 The above estimates follow the now familiar pattern in that, at each iteration, the estimate of the total number of beneficiaries has been revised downwards. As already stated, it is likely that this is significantly explained by wage anticipation, i.e. the October increase is awarded prior to the April of the same year.

Characteristics of Beneficiaries

2.18 Having estimated the number of jobs which benefited after April 2004 from the October 2004 upratings, we now investigate the characteristics of these beneficiaries by gender, hours of work, age, ethnicity, disability, region and sectors. We begin by looking at a picture of the beneficiaries of the 2004 upratings at a single point in time, using the earnings assumption, before concluding with a summary of commissioned research that investigated beneficiaries over time from earlier upratings.

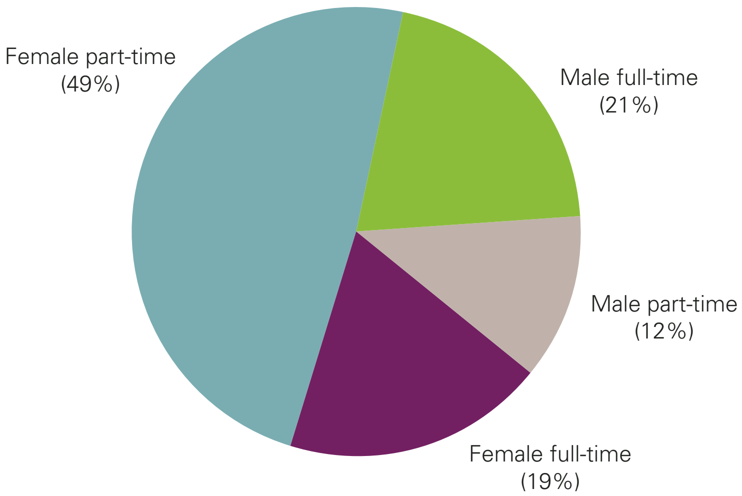
[3] Using the prices downrating assumption, in the fourth report we estimated the number of direct beneficiaries to be 1.5 million adults (aged 21 and over) and 100,000 youths (aged 18–20) in October 2003 and 2.3 million adults and 150,000 youths in October 2004. This was 6.5 per cent in 2003 and 9.8 per cent in 2004 of all employee jobs. In the 2004 report, we revised this estimate to 1.1 million adults (aged 22 and over) and 90,000 youths (aged 18–21) in October 2003 and 1.8 million adults and 130,000 youths in October 2004. This was 4.7 per cent in 2003 and 7.6 per cent in 2004 of all employee jobs. We now estimate that 1.1 million adults and 140,000 youths (about 5.2 per cent of all employee jobs for those aged 18 and over) will have directly benefited from the October 2004 upratings. This estimate will not include those who received their 2004 uprating prior to April 2004.

Gender and Hours Worked

2.19 As Figure 2.1 below reveals, two-thirds of the beneficiaries of the October 2004 upratings were women. Nearly half were women working part-time. A fifth were full-time male workers and men working part-time make up the remaining 12 per cent.

Figure 2.1

Percentage of Jobs Paying Less Than £4.75 (22 and Over), £4.00 (18–21) and £2.95 (16–17) by Gender and Hours Worked, April 2004



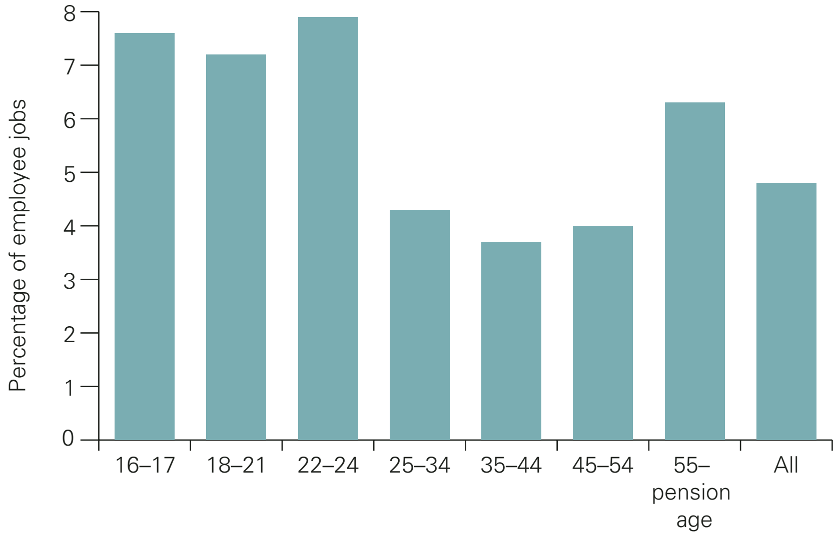
Source: LPC calculations using ASHE 2004, with supplementary information.
Note: We have used the earnings downrating assumption to derive estimates of the value in April 2004 of the October 2004 upratings. That is we have assumed that, in the absence of any labour market intervention, all wages would have grown by the average earnings index between April and October. In other words, wages would have risen by 2.1 per cent in this six-month period.

Age

2.20 We can see that the distribution of the beneficiaries by age is U-shaped. That is to say that between 7 and 8 per cent of workers aged 16 to 25 years old were beneficiaries compared with around 4 per cent of those aged 25 to 54. This proportion then increases to about 6 per cent of those nearing pension age.

Figure 2.2

Percentage of Jobs Paying Less Than £4.75 (22 and Over), £4.00 (18–21) and £2.95 (16–17) by Age, April 2004



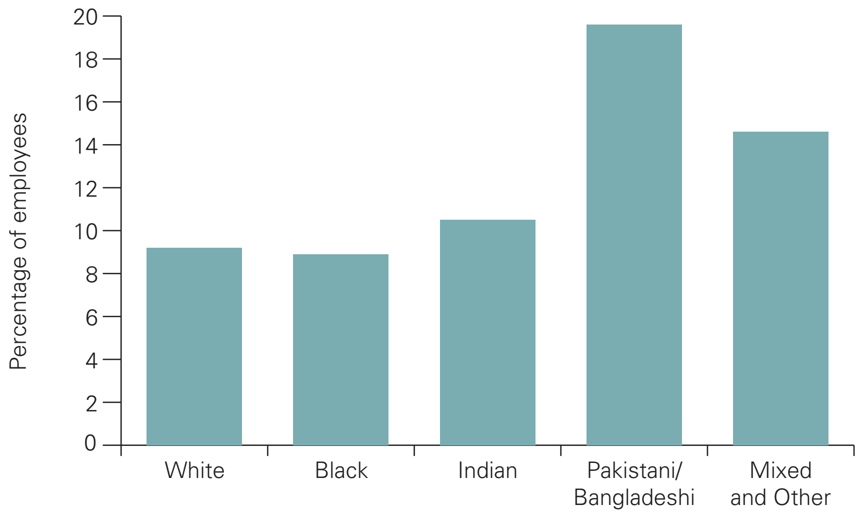
Source: LPC calculations using ASHE 2004, with supplementary information.
Note: See note to Figure 2.1.

Ethnicity

2.21 For our analysis of ethnicity we use the Labour Force Survey (LFS), as the ASHE contains no information on ethnicity. It should be noted that the earnings data in the LFS are not as reliable as that in the ASHE. Using the ASHE, we estimate coverage of the 2004 upratings to be less than 5 per cent. In contrast, about 9.5 per cent of employees are estimated to be beneficiaries in the LFS, using the derived hourly pay variable. Although over 90 per cent of the beneficiaries of the 2004 upratings were white, this proportion was less than the proportion of whites in the workforce. Figure 2.3 shows the percentage of each ethnic group who benefited from the 2004 minimum wage upratings. Using LFS data, nearly a fifth of all jobs held by Pakistanis and Bangladeshis were expected to benefit from the 2004 upratings. This compares with about nine per cent of whites. Blacks were least likely to benefit.

Figure 2.3

Percentage of Employees Earning Less Than £4.75 (22 and Over), £4.00 (18–21) and £2.95 (16–17) by Ethnicity, Spring 2004



Source: LPC calculations using LFS, Spring 2004.

Notes:

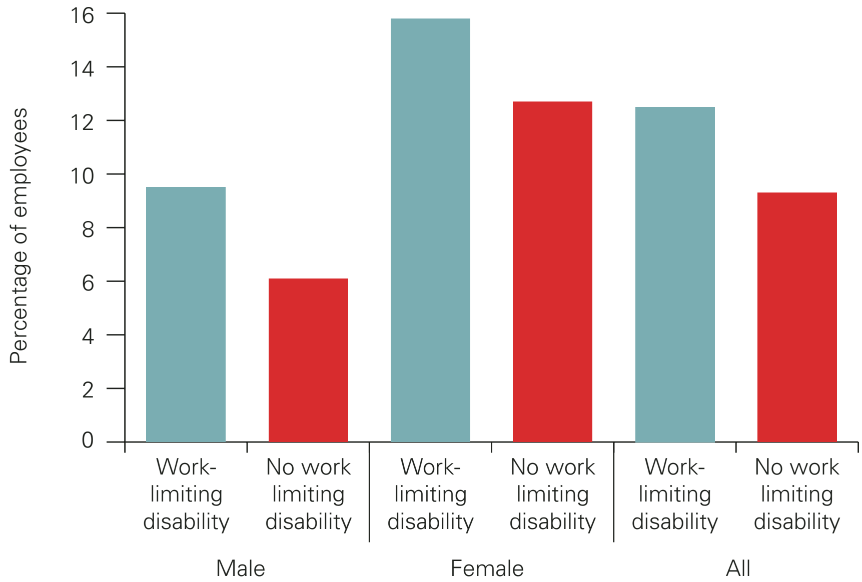
1. See note to Figure 2.1.
2. The derived hourly pay variable in the LFS overestimates the number of beneficiaries compared to the ASHE, hence the coverage in Figures 2.3 and 2.4 is greater than for the other Figures in this section that use ASHE.

Disability

2.22 This analysis also uses the LFS as there is no disability information in the ASHE. The same qualifications as set out in paragraph 2.21 concerning LFS data also apply to those with disabilities. Figure 2.4 shows the percentage of those with and without work-limiting disabilities, who were set to benefit from the 2004 minimum wage upratings. Those with work-limiting disabilities were more likely to have benefited from the 2004 minimum wage uprating. This result holds for both men and women.

Figure 2.4

Percentage of Employees Earning Less Than £4.75 (22 and Over), £4.00 (18–21) and £2.95 (16–17) by Disability, Spring 2004



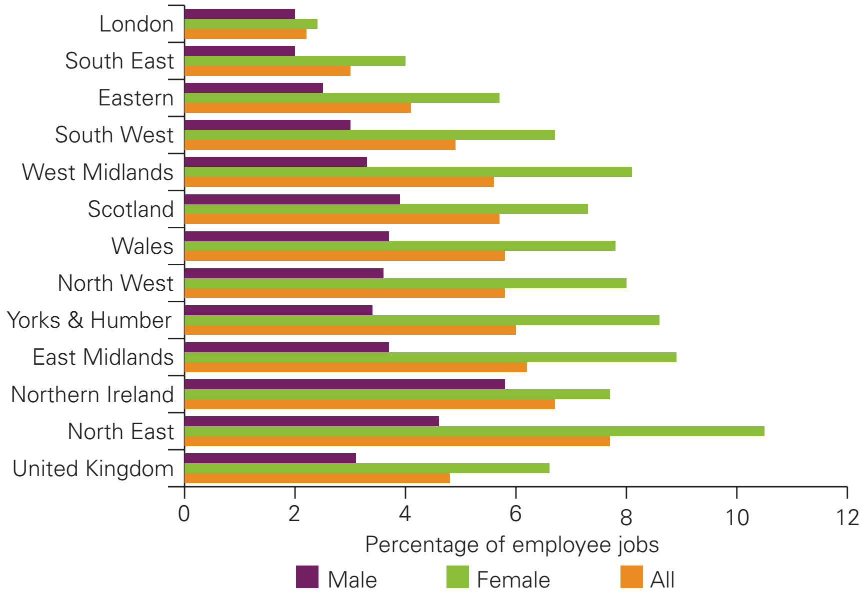
Source: LPC calculations using LFS, Spring 2004.
Notes:
1. See note to Figure 2.1.
2. See note 2 to Figure 2.3.

Region and Country

2.23 Figure 2.5 shows the percentage of jobs benefiting from the October 2004 upratings by region, country and gender. The preponderance of women is again apparent. Unsurprisingly, London has the lowest percentage of possible beneficiaries, with the South East of England close behind. The highest percentages are in the North of England, the East Midlands and Northern Ireland.

Figure 2.5

Percentage of Jobs Paying Less Than £4.75 (22 and Over), £4.00 (18–21) and £2.95 (16–17) by Region and Country, April 2004



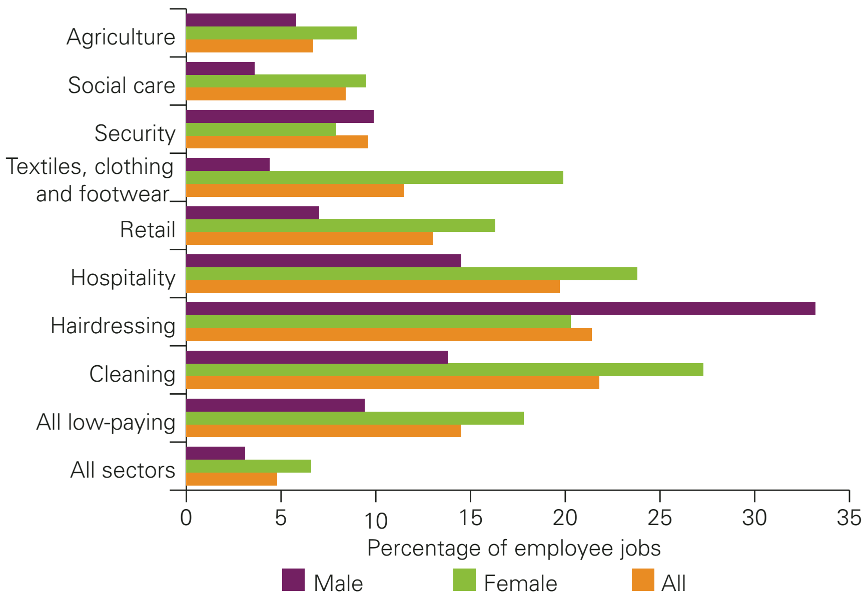
Source: LPC calculations using ASHE 2004, with supplementary information.
Note: See note to Figure 2.1.

Low-paying Sectors

2.24 For the purposes of our analysis, the low-paying sectors consist of agriculture, retail, hospitality, security, childcare, social care, cleaning, the manufacture of textiles, clothing and footwear and hairdressing. Figure 2.6 shows the percentage of jobs (and Figure 2.7 the number of jobs) in these traditional low-paying sectors (excluding childcare) set to benefit from the October 2004 upratings.

Figure 2.6

Percentage of Jobs Paying Less Than £4.75 (22 and Over), £4.00 (18–21) and £2.95 (16–17) by Low-paying Sector, April 2004



Source: LPC calculations using ASHE 2004, with supplementary information.

"Overall, over 40% of respondents have increased their minimum rates of pay in order to comply with the NMW. In the Midlands this percentage increases to 50% of the respondents. However, the areas worse affected are Scotland and Wales with nearly 60% and over 80% of respondents respectively stating that they have increased their minimum rates of pay in order to comply with the NMW."

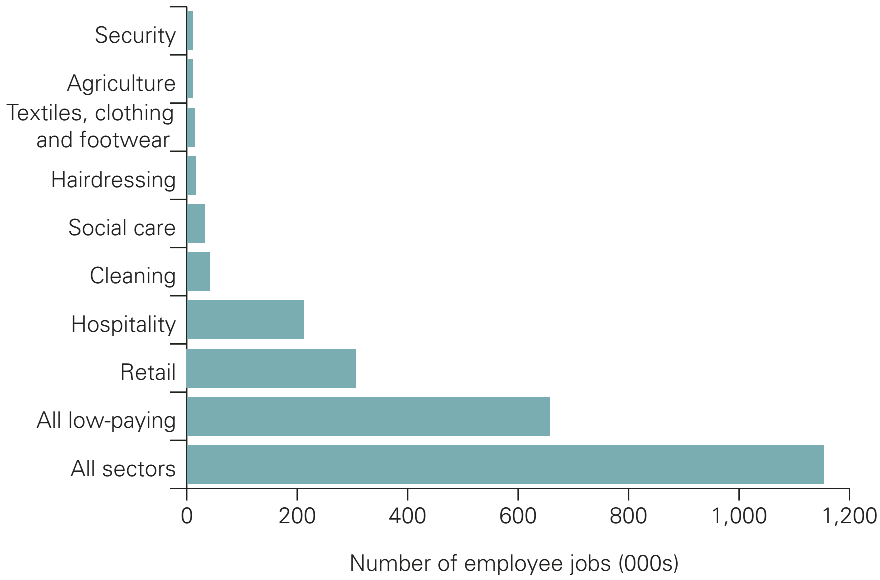
British Shops and Stores Association evidence

2.25 Figures 2.6 and 2.7 together help us see where the 2004 upratings of the minimum wage have had most impact. They reveal that more beneficiaries of the 2004 upratings were to be found in the retail sector than any other sector. Just over 300,000 retail jobs, representing about 13 per cent of jobs in the sector, were estimated to have had their hourly rate increased from 1 October 2004 as a result of the minimum wage upratings.

2.26 While the retail sector had the most beneficiaries in number, the sectors with the largest proportion of staff affected were hospitality and hairdressing. In both sectors about 20 per cent of employees stood to benefit. Compared with retail, the absolute numbers in hairdressing were very small. Hospitality, on the other hand, had over 200,000 workers who have benefited.

Figure 2.7

Number of Jobs Paying Less Than £4.75 (22 and Over), £4.00 (18–21) and £2.95 (16–17) by Low-paying Sector, Thousands, April 2004



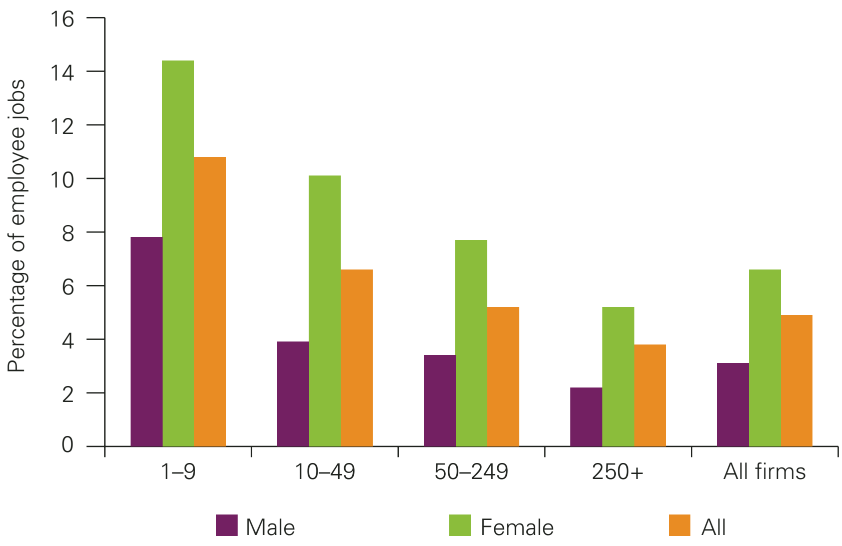
Source: LPC calculations using ASHE 2004, with supplementary information.
Note: See note to Figure 2.1.

Size of Firm

2.27 Figure 2.8 sets out beneficiaries by size of firm. It shows that, in general, the smaller the firm the more likely there will be workers who stand to benefit from the National Minimum Wage. Even so, most jobs in small firms were already paid above the October 2004 minimum wage rates by April 2004. Just over 10 per cent of jobs in micro firms (with 1 to 9 employees), but fewer than seven per cent in other small firms (with 10 to 49 employees) were estimated to gain from the October 2004 upratings.

Figure 2.8

Percentage of Jobs Paying Less Than £4.75 (22 and Over), £4.00 (18–21) and £2.95 (16–17) by Size of Firm, April 2004



Source: LPC calculations using ASHE 2004, with supplementary information.
Note: See note to Figure 2.1.

Flows

2.28 We commissioned research from Sloane, Murphy, Jones and Jones (2004) to examine whether minimum wage workers tended to get trapped in low-paying jobs, or whether such positions acted as a stepping-stone to more remunerative positions. They found high levels of flows into and out of minimum wage employment (churning), with 40 per cent moving into higher-paid employment a year later, 4 per cent exiting into unemployment and 12 per cent becoming economically inactive. They concluded that employment in minimum wage jobs lasted less than a year for about half of those paid at or below the minimum wage.

2.29 This dynamic picture of the characteristics of beneficiaries is similar to the static picture discussed above. The researchers found that men were more likely to exit minimum wage employment than women. Having a disability, being employed in a small firm, working part-time or being employed in the private sector increased the probability of remaining in minimum wage employment.

Conclusion

2.30 We calculate that there were 1.1 million jobs where the hourly rate of pay in mid-April 2004 was below the new October 2004 minimum wage rate (suitably downrated) and which benefited directly from the 2004 upratings. This latest estimate represents about 4.6 per cent of all employee jobs. In our fourth report we calculated that the 2004 upratings would cover 6.9 per cent of the workforce.

2.31 There will, however, have been other workers who benefited from the October 2004 increases. These fall into two categories:

- Workers whose pay had already been increased prior to April 2004 because employers were anticipating the October increases;
- Workers who did not need a pay increase to take them above the October 2004 minimum wage rates, but who received an increase in order to maintain differentials.

2.32 The latter category of indirect beneficiaries is not intended to be covered by our estimates of beneficiaries, which instead seek to measure 'direct beneficiaries'. The former category – direct beneficiaries who receive pay increases before April – will be captured by our forward-looking estimates of beneficiaries but not by our post-uprating estimates.

2.33 It may therefore be that our forward-looking estimates of beneficiaries are a better indication of total direct beneficiaries than our post-uprating estimates. The fact that our post-uprating estimates are lower than our forward-looking estimates does not, therefore, in itself establish any presumption that the increases in October 2003 and October 2004 produced less of an impact than we intended.

2.34 However, this is an area that we will wish to consider further and where we may want to commission future research.

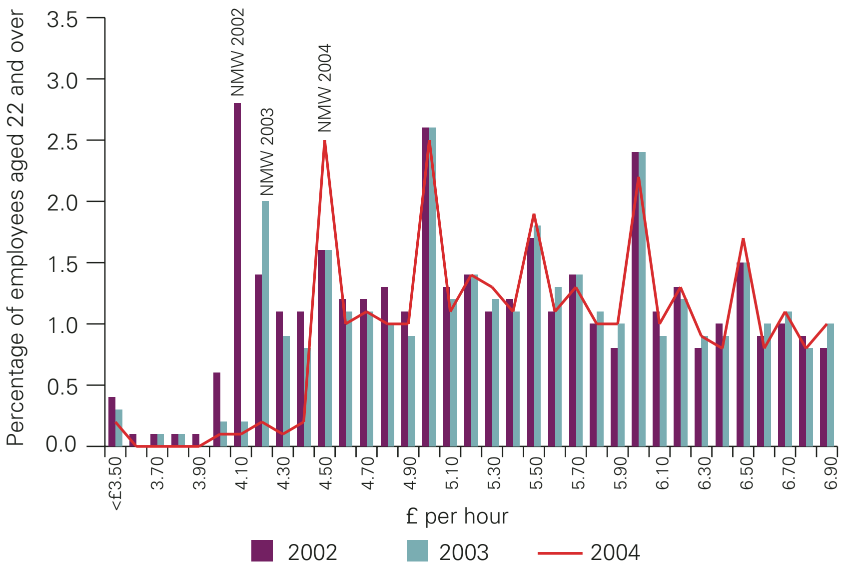
Earnings

2.35 In this section, we consider the hourly earnings distribution for adult workers (aged 22 and over). The hourly earnings distributions for younger workers are considered in Chapter 5.

2.36 The impact of the adult minimum wage can clearly be seen in Figure 2.9. There is a concentration of the workforce at the National Minimum Wage in all three years considered. This concentration is greatest in Spring 2002 and Spring 2004, periods that followed the large minimum wage upratings of October 2001 and October 2003. After the smaller uprating in October 2002, the proportion of jobs paid at the minimum wage rate was lower.

Figure 2.9

Hourly Earnings Distribution for Employees Aged 22 and Over, 2002–2004



Source: ONS central estimate methodology, Spring 2002–2004.

Notes:

1. Gross hourly earnings excluding overtime.
2. NMW label shows the adult NMW rate in April of the given year.

2.37 In Spring 2004, there were peaks in the adult earnings distribution at around £4.50 (the then National Minimum Wage), £5.00, £5.50, £6.00 and £6.50. Similar peaks are observed for 2002 and 2003. These peaks lend support to the idea that firms, particularly those in the low-paying sectors, had a 'mezzanine' level that was between 50p and £1.00 greater than the minimum wage. Our discussions with various employers and employer organisations bear this out. Many told us that they did not wish to be seen as 'minimum wage employers'. Further, many firms observed that they could not get the quality of workers they wanted at the minimum wage so had to pay higher rates.

'Nearly 60 per cent [of survey respondents] aimed at setting the lowest rate of pay above the NMW – the so-called "mezzanine" approach.'

British Hospitality Association evidence

'Retailers do not want to be regarded as minimum wage employers ... Many retailers choose to pay a rate above the NMW to recruit and retain the best staff.'

British Retail Consortium evidence

2.38 Excluding overtime, median gross hourly earnings of full-time adults, whose pay was not affected by absence, was £10.41 per hour in April 2004, up 5.1 per cent on April 2003. Excluding overtime, the median hourly earnings of full-time women (£9.46) increased by 5.3 per cent, compared with 4.9 per cent for men (£11.04). In comparison, the National Minimum Wage for adults rose from £4.20 in October 2002 to £4.50 in October 2003, an increase of 7.1 per cent.

2.39 The value of the adult minimum wage compared with other earnings measures is shown in Table 2.5. It can be seen that after the large upratings, such as in the 2002 and 2004 data, the minimum wage increases as a proportion of mean, median, lowest decile and lowest quartile hourly earnings. However, the converse occurs in years of small upratings, such as in the data for 2000, 2001 and 2003.

Table 2.5 Adult Minimum Wage as a Percentage of Various Gross Hourly Earnings (Excluding Overtime) Measures, All Employee Jobs, 1999–2004

Adult minimum wage as a percentage of	1999	2000	2001	2002	2003	2004
Lowest decile	87.0	83.3	82.2	86.7	84.0	87.2
Lowest quartile	68.3	65.7	64.8	69.0	67.5	69.4
Median	47.6	46.2	45.2	48.1	47.5	48.5
Mean	36.7	35.3	34.2	36.0	35.7	36.7
Upper quartile	31.3	30.2	29.5	31.3	30.9	31.6
Upper decile	21.6	20.9	20.3	21.4	21.1	21.7

Source: ASHE, April 1999–2004, without supplementary information.
Note: Employees on adult rates whose pay for the survey period was unaffected by absence.

‘The significant differences in the UK labour market have ultimately resulted in wage disparities.... Therefore, ACS recommends that the Low Pay Commission take into consideration the fact that retailers in some regions of the country are less able to sustain wage levels at the minimum wage than others.’

Association of Convenience Stores evidence

2.40 Overall, since its introduction the value of the adult minimum wage as a percentage of median hourly earnings has increased from 47.6 per cent to 48.5 per cent in April 2004. It is expected to increase further following the October 2004 uprating. It should be noted, however, that at its introduction in April 1999 the adult rate of the minimum wage as a proportion of mean hourly earnings was 36.7 per cent. It did not reach this level again until Spring 2004, although it is now expected to increase following the 7.8 per cent uprating in October 2004.

Region and Country

2.41 By looking at wages at a regional level, we can see which areas of the UK are likely to be most affected by the National Minimum Wage. In April 2004, median gross hourly earnings (excluding overtime) were highest in London at £12.89 (40 per cent higher than the national median) and lowest in the North East at £8.20, Northern Ireland at £8.26 (both about 11 per cent lower than the national median) and the East Midlands (£8.36). It can be seen from Table 2.6 that England

(£9.34) has higher median average hourly pay than Scotland (£8.66), Wales (£8.46) and Northern Ireland (£8.26).

Table 2.6 Gross Hourly Pay Excluding Overtime by Region, All Employee Jobs, April 2004

Region or Country	Median (£)	Adult minimum wage as a percentage of the median
United Kingdom	9.21	48.9
England	9.34	48.2
Scotland	8.66	52.0
Wales	8.46	53.2
Northern Ireland	8.26	54.5
North East	8.20	54.9
East Midlands	8.36	53.8
Yorkshire and the Humber	8.47	53.1
South West	8.57	52.5
West Midlands	8.67	51.9
North West	8.70	51.7
East	9.05	49.7
South East	9.95	45.2
London	12.89	34.9

Source: ASHE 2004, with supplementary information.
Note: Employees on adult rates whose pay for the survey period was not affected by absence.

2.42 We might expect the minimum wage to have more impact in the North East, the East Midlands and Northern Ireland, where the lowest decile hourly earnings were £5.00 or below, and much less impact in London, the South East and the East of England. Figure 2.5 showed that the highest percentage of jobs paying less than £4.75 were located in the North East, the East Midlands and Northern Ireland.

2.43 It is likely therefore that the minimum wage has had a noticeable impact in these regions. Indeed, in the year to April 2004 the largest increases in mean gross hourly earnings (excluding overtime) were in the North East (6.1 per cent), Wales (6.0 per cent) and Yorkshire and the Humber (5.1 per cent). This compares with 3.8 per cent in the East Midlands, another low-paying region, and 4.2 per cent in the UK. The largest increases in median gross hourly earnings (excluding overtime) were in Wales (7.7 per cent) and Northern Ireland (5.6 per cent).

2.44 Although there are regional disparities in gross hourly earnings, there are also significant differences within regions. Indeed, these within-region differences are often greater than those between regions. For example, median gross hourly earnings in Manchester are £10.45 but in Bolton, in the same region, they are £7.70. Further, median gross hourly earnings are £10.37 in Solihull but only £7.75 in nearby Dudley.

‘As a national employer, we are also aware of the varying degree of impact felt as a result of NMW increases across the country. Up to now the South East has seen relatively little impact from NMW increases – average pay rates being higher than the level of NMW. The situation in the North and in Scotland and Wales is very different. The majority of care home staff in the North and Scotland are now paid at NMW.’

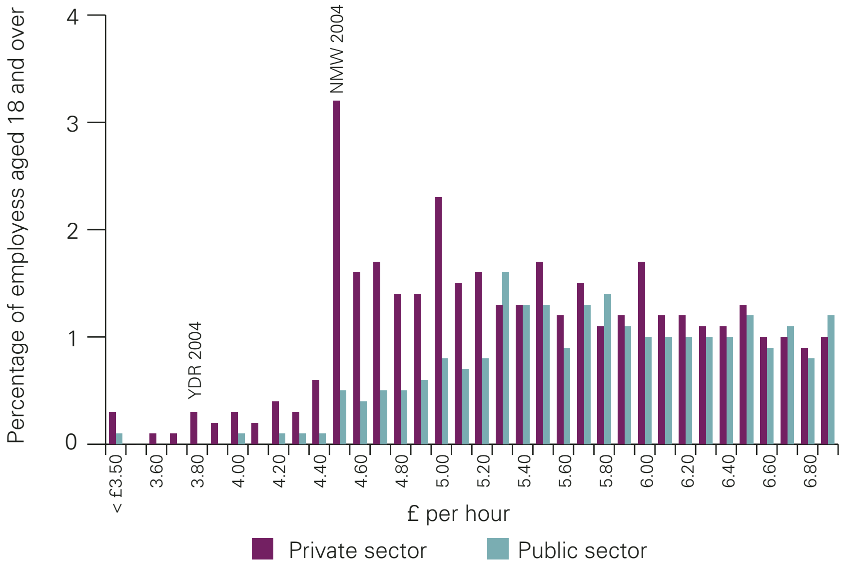
BUPA Care Homes evidence

Public and Private Sector

2.45 In April 2004, median hourly pay was about 21.4 per cent higher in the public sector (£10.49) than in the private sector (£8.64), although the mean hourly pay was only 4.9 per cent higher in the public sector. The lowest decile hourly earnings in the private sector was under £5.00 compared with £5.78 in the public sector.

Figure 2.10

Gross Hourly Earnings (Excluding Overtime) Distribution for Employees Aged 18 and Over by Public and Private Sector, April 2004



Source: ASHE, April 2004, with supplementary information.
Note: The NMW 2004 label refers to the adult minimum wage rate in April 2004 (£4.50). The YDR 2004 refers to the youth Development Rate in April 2004 (£3.80).

2.46 Figure 2.10 depicts the gross hourly earnings distribution in the public and private sectors and highlights the difference at the bottom end of the earnings distribution. We can clearly see that the private sector is more affected by the minimum wage than the public sector. When deciding upon our recommendations, we take full account of the relative impacts on the public and private sectors.

‘Employers who adopt a ‘mezzanine floor’ minimum rate set just above the minimum wage as part of their labour market strategy may fear that they will lose competitive advantage if the minimum wage is raised to a point where they cannot maintain this addition. This may well be seen as a problem for these employers, but it is not a problem for the UK economy as a whole.’

TUC evidence

Differentials

2.47 An important factor when assessing the impact of the National Minimum Wage is the degree to which differentials are restored following an uprating. This not only affects the number of workers who might indirectly gain from above-average increases in the minimum wage but also affects firms’ total wage bills. This has consequences not only for a firm’s ability to pay higher minimum wages but could also lead to economy-wide inflationary pressures.

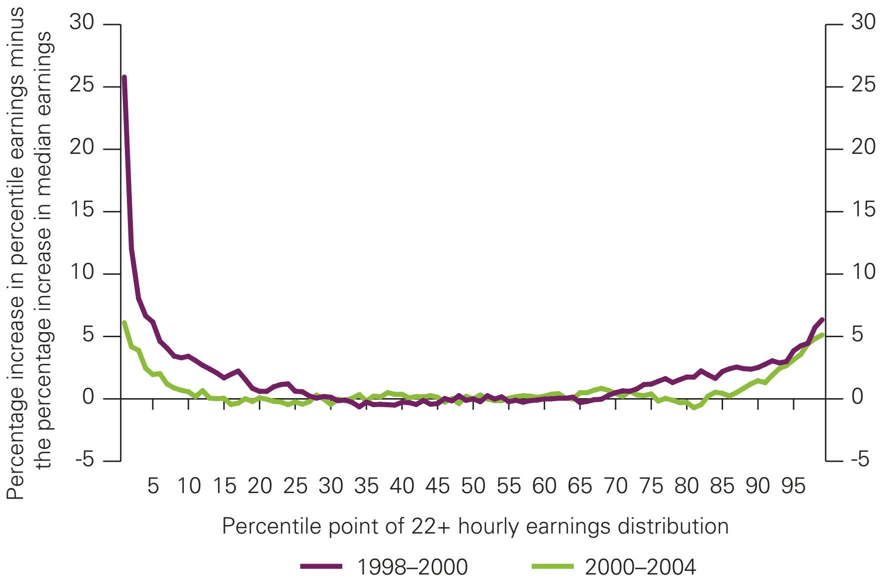
2.48 The further up the earnings distribution that the differential impacts, the greater the number of people that gain from higher wages, but the higher the cost to firms and the greater the potential impact on inflation.

2.49 In our fourth report (2003), we analysed the extent of the differential impact and concluded that following the minimum wage increases in October 2000 and 2001, earnings increases up to the 16th percentile were higher, on average, than the median increase but lower than the direct minimum wage impact. From the 16th to the 41st percentile earnings increases fluctuated around the median, with average rises being just above the median. Taking a longer view, from 2000 to 2004, similar conclusions can be reached, as seen in Figure 2.11.

2.50 Figure 2.11 also clearly shows that the minimum wage has increased the hourly wages of those at the bottom of the earnings distribution. The largest increases occurred between 1998 and 2000 following the introduction of the minimum wage. Significant gains, largely attributable to the minimum wage upratings, have also been made by those at the bottom of the distribution between 2000 and 2004.

Figure 2.11

Increase in Hourly Earnings Minus the Increase in Median Earnings by Percentile for Employees Aged 22 and Over, 1998–2004



Source: ASHE, 1998–2004, without supplementary information.

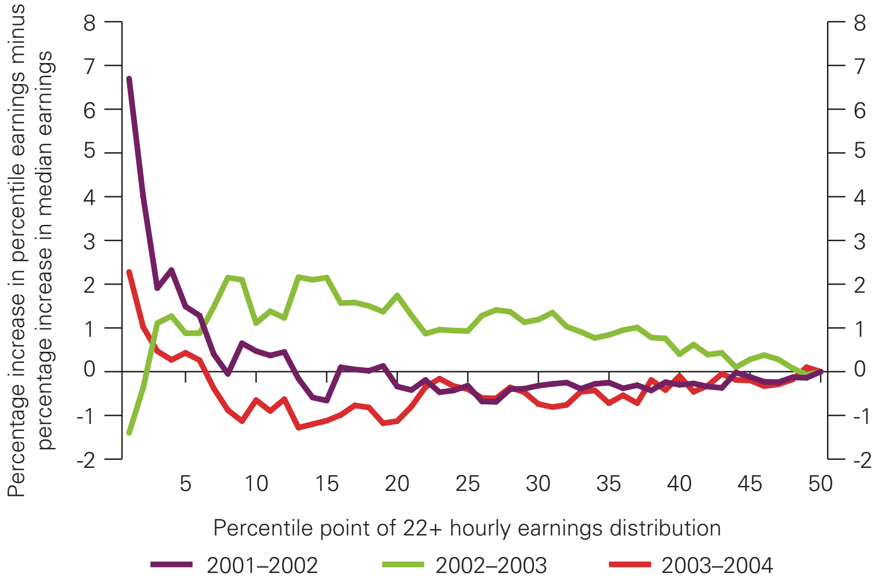
2.51 Looking in more detail at the most recent increases, as shown in Figure 2.12, we can clearly see a 'concertina' effect. When the minimum wage increase has been large, as in 2001/02 and 2003/04, differentials were eroded (especially after the October 2003 uprating) but were restored when the increase in the minimum wage was small, as in 2002/03 (the 2002 uprating).

'Differentials within companies have been squeezed to such an extent that firms now face considerable costs if they are to restore them in order to recruit staff, maintain employee motivation and reward progression. The erosion of differentials impacts on employers' ability to provide employees with a performance incentive and to recruit staff with some level of experience.'

CBI evidence

Figure 2.12

Increase in Hourly Earnings Minus the Increase in Median Earnings by Percentile up to the Median for Employees Aged 22 and Over, 2001–2004



Source: ASHE, 2001–2004, without supplementary information.

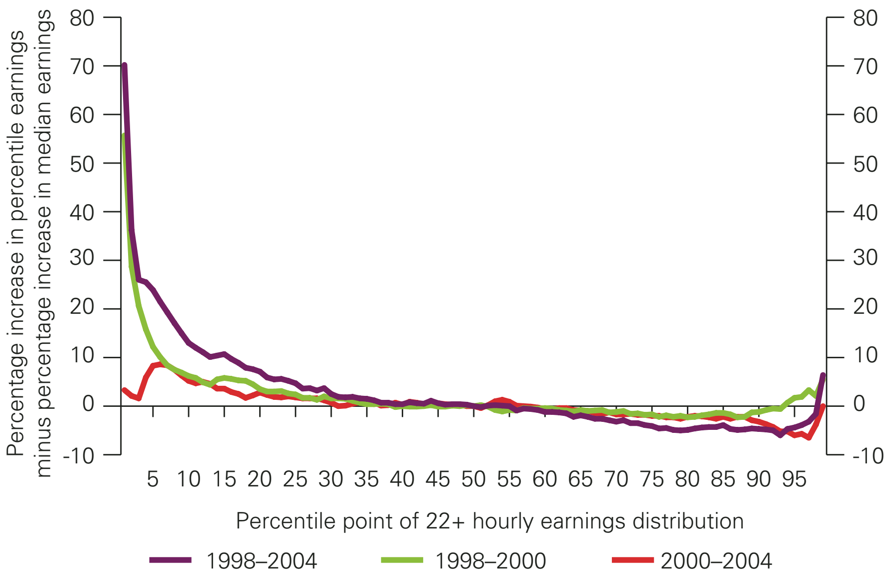
‘As a matter of good business practice, differentials are important incentives to good performance and need to be maintained, particularly at lower wage levels. It is unreasonable not to raise the wages of staff paid at rates above the NMW in line with those paid at NMW level.’

BRC evidence

2.52 Turning to the low-paying sectors (excluding childcare), we can see from Figure 2.13 that the lower paid in these sectors have benefited significantly from the introduction and subsequent upratings of the minimum wage. In contrast to the economy as a whole, low-paid workers in these low-paying sectors have generally had wage increases greater than for those at the upper end of the earnings distribution.

Figure 2.13

Increase in Hourly Earnings Minus the Increase in Median Earnings by Percentile for Employees Aged 22 and Over in the Low-paying Sectors (Excluding Childcare), 1998–2004

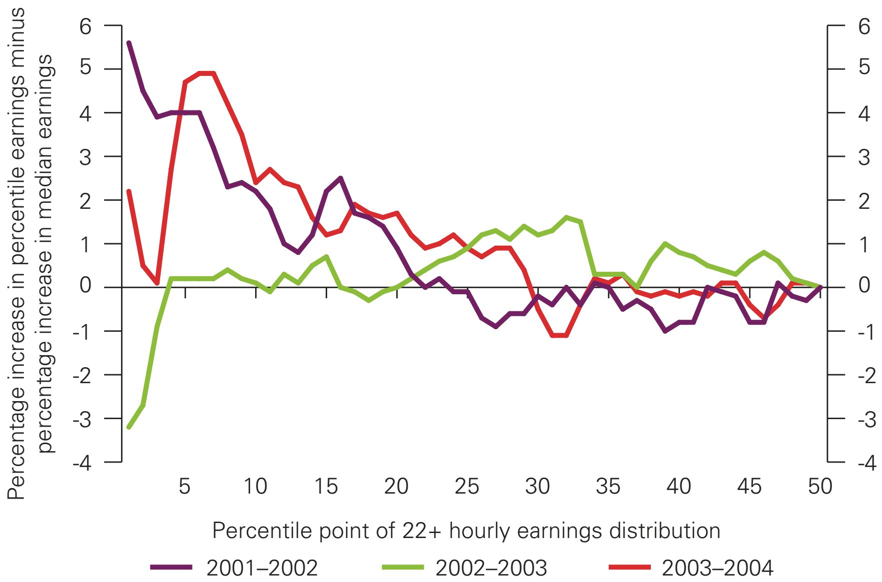


Source: ASHE, 1998–2004, without supplementary information.

2.53 Looking at the most recent increases, we can see in Figure 2.14 that there were significant increases at the bottom end of the hourly earnings distribution following the large minimum wage upratings in 2001/02 and 2003/04. In 2002/03, when the upratings were small, the low-paid received only small increases. There is also evidence to suggest some restoration of differentials in this 'pause year'.

Figure 2.14

Increase in Hourly Earnings Minus the Increase in Median Earnings by Percentile up to the Median for Employees Aged 22 and Over in the Low-paying Sectors (Excluding Childcare), 2001–2004



Source: ASHE, 1998–2004, without supplementary information.

2.54 Evidence received in our formal and informal consultation process is consistent with this 'concertina' pattern. Indeed, the CBI along with other employers organisations, argued forcibly for a 'pause' year in 2005 in order that differentials could be restored.

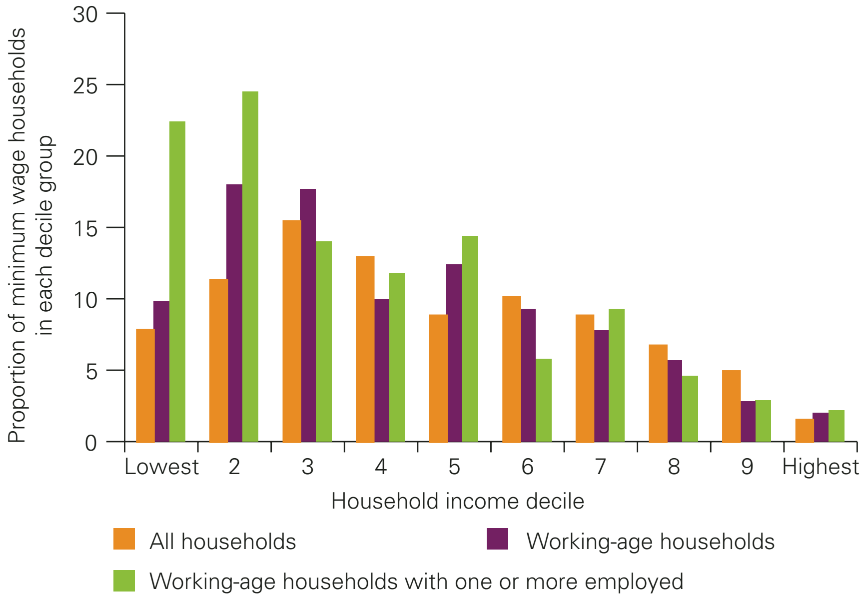
2.55 There were increasing concerns from employers and employer organisations that squeezed differentials had become a greater problem as a result of the two large minimum wage upratings in October 2003 and October 2004. Many employers argued that differentials had become so compressed that this had forced them to flatten their pay structures by removing some grades. This was a particular problem in the textiles industry where incentive pay was used widely.

Household Income Distribution

2.56 In the analysis on beneficiaries earlier in the Chapter, we focused our attention on individuals. In this section, we look at the impact of the National Minimum Wage on households. We commissioned research from Bryan and Taylor (2004) to investigate this issue using the British Household Panel Survey (BHPS). Defining minimum wage households as all those households containing at least one minimum wage worker, they found that these typically were couple households, usually with older dependent children, and contained multiple wage earners.

Figure 2.15

Position of Minimum Wage Households Within the Household Income Distribution, Autumn 2002



Source: Bryan and Taylor (2004) using data from the BHPS.

2.57 The proportion of minimum wage households in each decile group of the household income distribution is shown in Figure 2.15. Looking at the income distribution of all households, the National Minimum Wage does not look particularly well-targeted at the bottom of the income distribution. This is because households at the bottom of the income distribution typically contain no wage earners, consisting largely of pensioner households and benefit recipients. Confining the analysis to working-age households, however, and in particular to working-age households in which at least one individual is in work, suggests that the National Minimum Wage is well-targeted at the bottom of the income distribution. These findings are similar to those reported in Volume Two of our third report (2001).

The Labour Market

2.58 In this section we analyse overall trends in the UK labour market including employment, unemployment, inactivity, employee jobs, hours, vacancies and pay settlements. Although we look at trends since the introduction of the minimum wage, we focus our attention on the impact of the October 2003 upratings, looking in particular at employment, unemployment and participation among the working age population. Where data permits, we also comment on the emerging impact of the October 2004 upratings.

2.59 We analyse the labour market by looking first at the number of people in employment (employees and self-employed) using household survey data. We follow this by looking at the number of jobs in the economy using employer-based survey data.

Employment, Unemployment and Inactivity

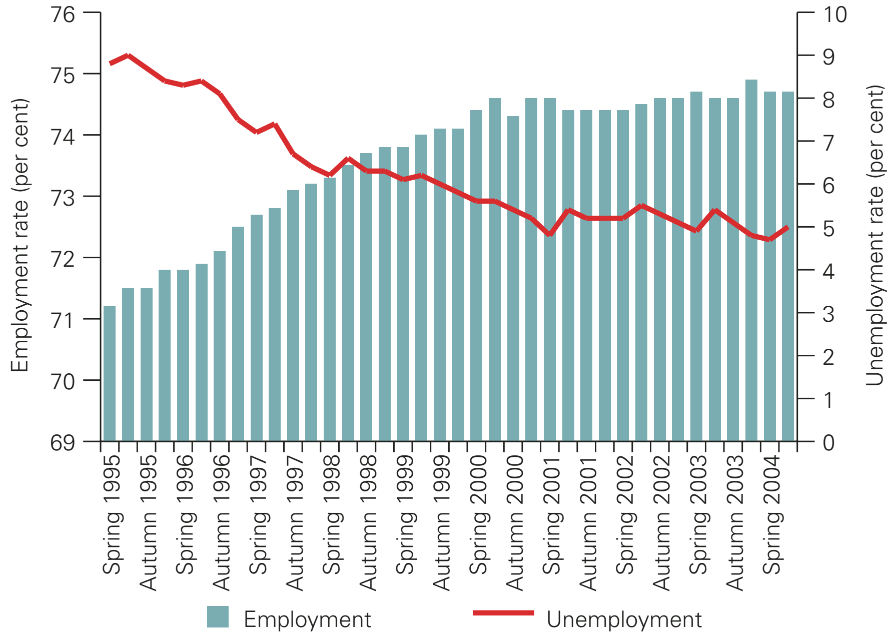
2.60 The UK labour market continues to be strong, with employment at record levels and unemployment low. There does not appear to have been any detrimental effect on total employment from the October 2003 upratings. Indeed, total employment in the economy rose by 271,000 in the year to Autumn 2004 and was 478,000 up since Autumn 2002. Initial indications of the impact of the 2004 upratings also suggest that there has been no negative effect. There was an increase in total employment of 99,000 in the three months to Autumn 2004.

2.61 Against this backdrop unemployment has also continued to be low. The unemployment level was 1.4 million in Autumn 2004, up 13,000 on the quarter but down 64,000 from a year earlier. Since Autumn 2002, it has fallen by 129,000. The claimant unemployment count shows similar trends. In December 2004 it was down 12,400 on October 2004 and stood at 824,200. This compares with 924,600 in October 2003 and 940,400 in October 2002.

2.62 Figure 2.16 shows how the working age employment and unemployment rates have changed since Spring 1995. The employment rate in Autumn 2004 stood at 74.8 per cent, an increase of 0.2 percentage points since the minimum wage upratings in Autumn 2003. It was also 74.6 per cent in Autumn 2002.

Figure 2.16

Working Age Employment and Unemployment Rates, UK, 1995–2004



Source: LFS, seasonally adjusted, 1995–2004.

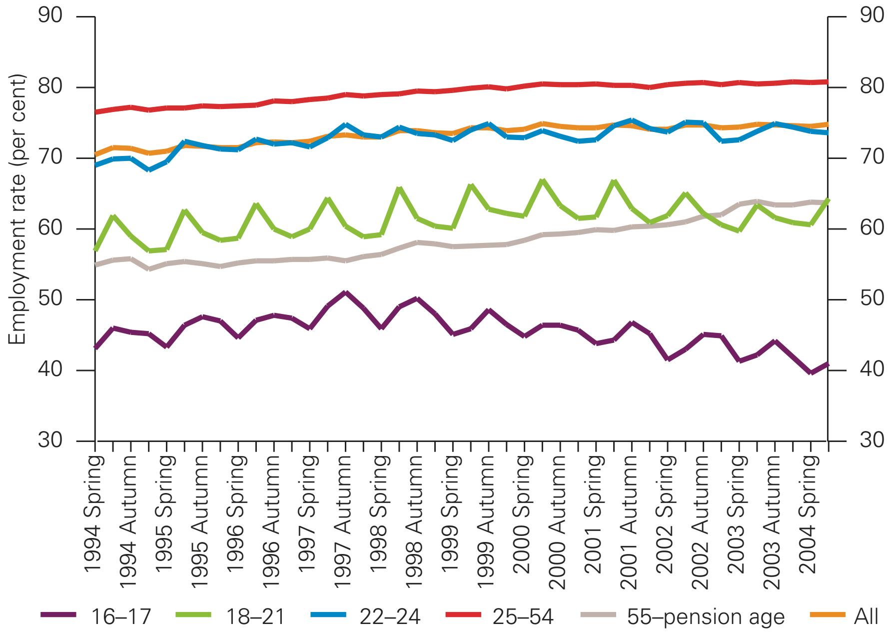
2.63 Figure 2.16 also shows that the unemployment rate has fallen from 5.3 per cent in Autumn 2002 to 5.0 per cent in Autumn 2003 and in Autumn 2004 was at a historically low rate of 4.8 per cent.

2.64 The claimant count unemployment rate in December 2004 was at its lowest since May 1975. The inactivity rate has fallen from 21.5 per cent in October 2003 to 21.4 per cent in October 2004, although it was 21.2 per cent in October 2002.

2.65 It is also worth taking a closer look at unemployment, inactivity and employment rates for different age groups. Figure 2.17 clearly shows that most age groups have benefited from the general increase in employment. There has been a particularly steep rise in the employment rate of those aged 55 and over. In contrast the employment rates of 16–17 year olds have been falling since the Summer of 1997. The employment rates of 18–21 year olds had been declining from mid-2000 to mid-2003 but appear to have levelled off since then. Young workers are analysed in more detail in Chapter 5.

Figure 2.17

Working Age Employment Rates by Age, 1994–2004



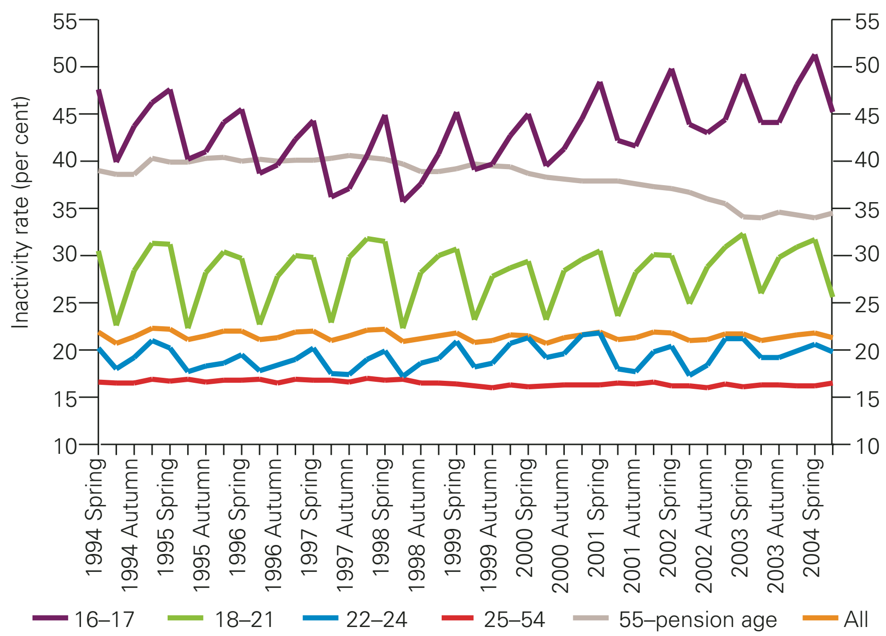
Source: LFS, not seasonally adjusted, 1994–2004.

2.66 All age groups, with the exception of 16–17 year-olds, have experienced a declining trend in unemployment rates since the introduction of the minimum wage in April 1999.

2.67 As shown in Figure 2.18, despite their recent improvement in employment rates, inactivity rates among those aged 55 and over, although declining, are the highest of any group other than 16–17 year olds. Since the Autumn of 2001, there appears to have been an increase in inactivity among the younger age groups.

Figure 2.18

Working Age Inactivity Rates by Age, 1994–2004



Source: LFS, not seasonally adjusted, 1994–2004.

2.68 Employment at an aggregate level appears strong. Two of our commissioned research projects, however, found small negative employment effects in those sectors and among those workers most affected by the minimum wage. Galindo-Rueda and Pereira (2004) found that employment grew at a slower rate in those areas of the country most affected by the minimum wage. Dickens and Draca (2005) examined the employment effects arising from upratings to the minimum wage. They found no statistically significant effects.

Jobs

2.69 The above analysis has concentrated on data from the LFS, a household survey which looks at the number of people in jobs. In this section we explore the number of jobs by looking at data from the ONS employee jobs series, an employer-based survey.

2.70 The number of employee jobs in Great Britain was around 25.6 million in September 2004. This consisted of about 17.6 million full-time and eight million part-time employee jobs. Since September 2003, the number of employee jobs has increased by about 138,000, with most of the increase being in full-time rather than part-time positions.

2.71 The low-paying sectors we referred to earlier in the Chapter (excluding childcare) accounted for some 6.1 million jobs – around 24 per cent of all employee jobs – in September 2004. Table 2.7 shows how the number of employee jobs in the economy and in the low-paying sectors has changed since the October 2003 upratings, the October 2002 upratings and the introduction of the National Minimum Wage. In the year since the October 2003 upratings, the number of employee jobs across the low-paying sectors has remained fairly constant, increasing by 34,000. During this period, the total number of employee jobs in the economy increased at a similar rate. There was little change between September 2002 and September 2003. Since March 1999, just before the introduction of the minimum wage in April 1999, there has been an increase of around a quarter of a million in the number of employee jobs in the low-paying sectors compared with over 1.2 million extra employee jobs in the economy.

Table 2.7 Number of Employee Jobs by Sector, Great Britain, 1999–2004

Employee job	Sector	Number of employee jobs (thousands)			
		September 2004	Change since September 2003	Change since September 2002	Change since March 1999
All employee jobs	Whole economy	25,585	138	98	1,228
	Low-paying sectors	6,065	34	37	249
Full-time	Whole economy	17,579	118	118	503
	Low-paying sectors	2,774	58	-21	-3
Part-time	Whole economy	8,005	19	-20	725
	Low-paying sectors	3,292	-23	58	251

Source: ONS employee jobs series, GB, 1999–2004.

2.72 In the economy as a whole, about 69 per cent of all employee jobs are full-time. In contrast, only 46 per cent of employee jobs in the low-paying sectors are full-time. Between September 2003 and September 2004, there has been an increase in both full-time (up 118,000) and part-time (up 19,000) employee jobs in the economy as a whole. In the low-paying sectors the number of full-time employee jobs increased by 58,000, although the number of part-time ones fell by 23,000.

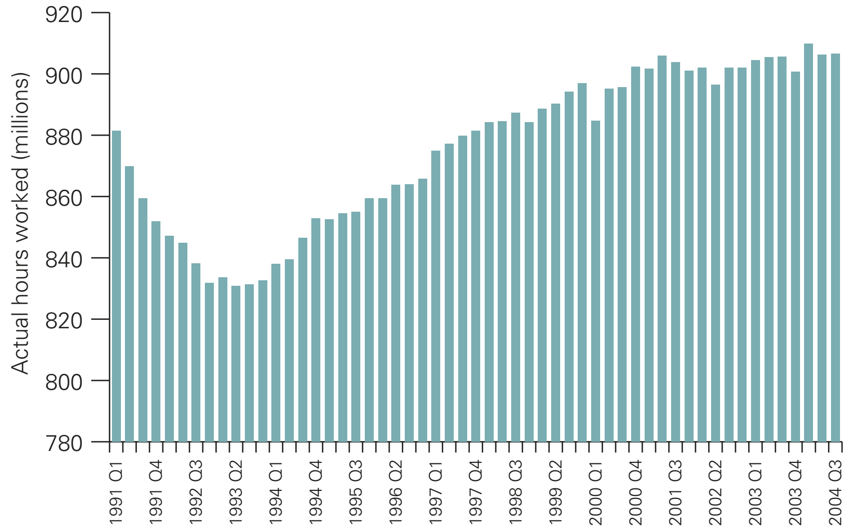
2.73 Since the introduction of the National Minimum Wage, the number of full-time employee jobs in the economy has risen by 503,000 and part-time employee jobs increased by 725,000. In contrast, the number of full-time employee jobs in the low-paying sectors has remained largely unchanged, while the number of part-time employee jobs has increased by 251,000.

Hours

2.74 As can be seen in Figure 2.19, the total number of actual weekly hours worked in the UK has increased significantly since the 1990s recession, reflecting the increase in employment. The actual number of weekly hours worked has increased from about 830 million in the last quarter of 1993 to about 907 million in the third quarter of 2004. The introduction of the minimum wage in Spring 1999, and the subsequent upratings, have not had any adverse effect on the total number of hours worked. Indeed, total weekly hours increased by nearly 18 million between the first quarter of 1999 and the third quarter of 2004. In the year after the 2003 upratings, the total number of actual weekly hours increased by nearly 13 million.

Figure 2.19

Total Actual Weekly Hours Worked (Millions) in the UK, 1991–2004



Source: LFS, seasonally adjusted, 1991–2004.

'At the time this survey was conducted [July 2004], 21% of retailers had reduced staff hours as a direct result of the NMW increasing to £4.50.'

BRC evidence

2.75 Average weekly hours have been declining since 1994, reflecting the increase in part-time work. This decline has been further accentuated by Government policies, such as the Working Time Directive, enhanced employment rights for part-timers and targeting the 'long hours' culture by promoting work-life balance. Average weekly hours have fallen from 33.2 in the first quarter of 1997 to 31.9 in the third quarter of 2004.

2.76 According to ASHE, full-time employees worked a median of 37.5 hours per week in April 2004, up 0.2 hours on 2003. Part-time employees worked a median of 20 hours a week in April 2004, the same as in April 2003.

2.77 Table 2.8 shows that the proportion of full-time employees working overtime in April 2004 was 23.2 per cent. Using comparable data, there has been a slight increase in overtime hours since April 2003.

Table 2.8 Paid Overtime Hours: Percentage Who Worked Overtime and Their Median Hours, All Employee Jobs, UK, April 2004

Hours per week		Full-time		Part-time	
		Per cent	Hours	Per cent	Hours
April 2004[1]	Men	28.0	5.5	20.3	5.0
	Women	15.4	2.9	19.4	3.0
	All	23.2	4.6	19.6	3.4
April 2004[2]	Men	28.3	5.5	20.8	5.0
	Women	15.6	2.9	19.7	3.0
	All	23.5	4.6	19.9	3.4
April 2003[2]	Men	28.3	5.3	18.0	4.4
	Women	15.5	2.5	19.0	2.6
	All	23.4	4.4	18.8	3.0

Source: ASHE, 2003–2004.
Notes:
1. ASHE with supplementary information.
2. ASHE without supplementary information.
3. Employees on adult rates whose pay for the survey period was not affected by absence.

2.78 Stewart and Swaffield (2004) were commissioned to research the impact of the minimum wage on hours worked. They found evidence to suggest that, although the initial impact of the minimum wage was small and insignificant, there were some significant 'lagged' effects. Although the results were not completely robust across data sets and model specifications, they conclude that 'the introduction of the minimum wage led to a reduction in the paid working hours of about 1 to 2 hours per week for both male and female low-wage workers'. They were unable, however, to determine whether this reduction was a result of employee choice or imposed by employers.

2.79 If the minimum wage boosts take home pay then individuals may no longer need to work in two jobs in order to maintain income levels. Conversely, if hours worked decline in response to upratings of the minimum wage, then individuals may take second jobs in order to earn enough money. Robinson and Wadsworth (2004) considered these issues and found that the introduction of the minimum wage had little overall effect on the incidence of second job holding or the hours worked in second jobs.

2.80 In conclusion, the minimum wage does not seem to have had much impact on aggregate hours. Stewart and Swaffield (2004) found that some individuals worked fewer hours after the introduction of the minimum wage; this may have been their choice or may have been imposed by the employer.

'Bearing in mind that many charities running shops are relatively small businesses with limited budgets, the result of these higher costs has been, in some cases, a limit on the number of hours offered to those employed. Therefore although the NMW has risen ... earnings of individuals employed in our sector at the lowest levels have not necessarily increased ....'

Association of Charity Shops evidence

Vacancies

2.81 The number of vacancies in the economy is another indicator of the health of the labour market. The number of vacancies tends to be pro-cyclical, going up in a boom but falling in a recession. The ONS monthly job vacancy series, based on a survey of employers, was introduced in April 2001. We do not, therefore, have a consistent vacancy series that covers the introduction of the National Minimum Wage. The available Jobcentre vacancies show, however, that the introduction of the minimum wage coincided with an increase in the number of Jobcentre vacancies from just under 300,000 in March 1999, to about 345,000 in March 2000 and almost 395,000 by March 2001. The number of new vacancies (inflows) and the number of filled vacancies (outflows) also increased over that period.

2.82 Table 2.9 shows the average level of vacancies in the UK, and for selected industries covering the main low-paying sectors, from September 2001 to September 2004. In general, vacancies fell from mid-2001 to mid-2003 before picking up again. Since the 2003 minimum wage upratings, vacancies have generally increased. The number of vacancies appears to be robust in the distribution, hotels and restaurants sector, which is characterised by many low-paying jobs.

Table 2.9 Job Vacancies in Selected Industries, UK, 2001–2004

Thousands	UK job vacancies	Distribution, hotels and restaurants	Manufacturing	Construction	Other services	Total services
2001 Sep	650.5	186.5	67.3	26.5	39.2	552.2
2002 Sep	601.3	179.7	60.3	20	35.4	518.2
2003 Sep	588.4	174.5	53.6	23.7	30.7	508.4
2004 Sep	644.4	191.7	61.6	23.7	34.6	556.3
Change since 2003 Sep	56.0	17.2	8.0	0.0	3.9	47.9

Source: ONS Vacancy Survey, not seasonally adjusted, average for three months ending in month shown.

2.83 An alternative interpretation is that the level of vacancies might also be indicative of the level of mismatch in the economy. An increasing number of vacancies might be a sign that employers cannot find workers with the skills they need for the job, or that the wages on offer are not attractive to those seeking work.

Pay Settlements and Average Earnings Growth

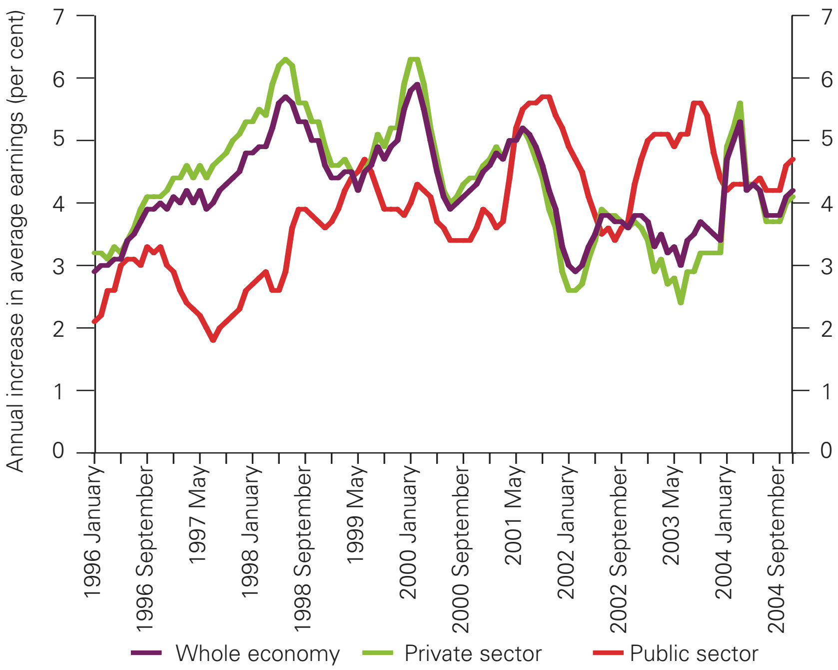
2.84 Wage growth has been remarkably subdued in a period of tight labour markets and low unemployment. Pay settlement data from both Incomes Data Services (2005b) and Industrial Relations Services (2005) show that the median pay settlement in the economy has been running at about 3 per cent for every month since early 2003.

2.85 In the year to April 2004, growth in gross weekly pay excluding bonus payments grew by 3.9 per cent according to ASHE, compared with a figure of 4.3 per cent from the Average Earnings Index (AEI). We use the AEI as our measure of average wage growth. The AEI is also the index used for forecasts by City and independent economic institutions. Average earnings growth captures a host of influences such as hours worked, overtime, bonuses and merit awards, which partly explain why it differs from the pay settlement data.

2.86 As shown in Figure 2.20, the pace of average earnings growth has quickened slightly in 2004 but remains at a moderate level. The year-on-year growth in average earnings for the whole economy (including bonuses) leapt from 3.4 per cent in December 2003 to 5.3 per cent in March 2004, driven by large private sector bonuses in January, but moderated to 4.2 per cent in April 2004. This was still the rate of growth of average earnings in November 2004, remaining just below the pace of 4.5 per cent the Bank of England believes is consistent with its inflation target.

Figure 2.20

Growth in Average Earnings Including Bonuses: Total, Public and Private Sectors, 1996–2004



Source: ONS, AEI including bonuses, year on year three-monthly averages, 1996–2004.

2.87 In November 2004 there was a gap between the public and private sectors, with the former running slightly ahead of the private sector at 4.7 per cent per annum compared with 4.1 per cent. The increase in public sector average wage growth is likely to continue into 2005 as 'Agenda for Change' is implemented in the NHS. Public sector average wage growth is therefore likely to remain above that for the private sector.

Conclusion

2.88 The UK labour market remains healthy with employment rates high and unemployment low. Total actual weekly hours worked in the UK has continued to increase, even though average hours worked by each individual has fallen. With inflation and interest rates still low, pay settlements remain relatively subdued.

2.89 Overall, employment has increased among the groups of workers and sectors most affected by the National Minimum Wage. Employment has also been increasing in the low-paying sectors as a whole. The low-paying sectors are considered in more detail in Chapter 3. Since the introduction of the minimum wage, unemployment has fallen for all age groups except for 16 and 17 year olds. The most affected groups of workers, including young workers, are considered in more detail in Chapters 4 and 5.

2.90 In conclusion, the minimum wage does not seem to have had any significant negative impact on the labour market. We now turn our attention to the impact of the minimum wage on the firm.

Impact on Firms

2.91 When recommending an appropriate rate for the National Minimum Wage, the Commission aims to benefit those on low pay, but also to ensure that businesses will be able to accommodate the recommended increases. This section examines the impact of the minimum wage on some key indicators of company performance: the wage bill, profits, productivity and prices, and business start-ups and failures.

The Wage Bill

2.92 In the 2004 report the Commission committed itself to a review of the methodologies used to estimate both the number of minimum wage beneficiaries and the impact of the minimum wage on the total wage bill. The methodological issues involved in estimating beneficiaries have been discussed earlier in this Chapter. Our review of the methodology for estimating wage bills suggests that the technique used in past reports is reasonably robust.

2.93 The direct effect of the minimum wage on firms is through higher labour costs which increase the wage bill. In order to estimate the effect of the October 2004 upratings, we need to establish a counterfactual and ask what would have happened to wages in the absence of the increase. To do this, we need to make two assumptions: what would have happened to the earnings of those paid below the new rate had there been no minimum wage increase; and would the shape of the earnings distribution above the minimum have been any different – that is, has the uprating affected differentials in a way which changes the distribution?

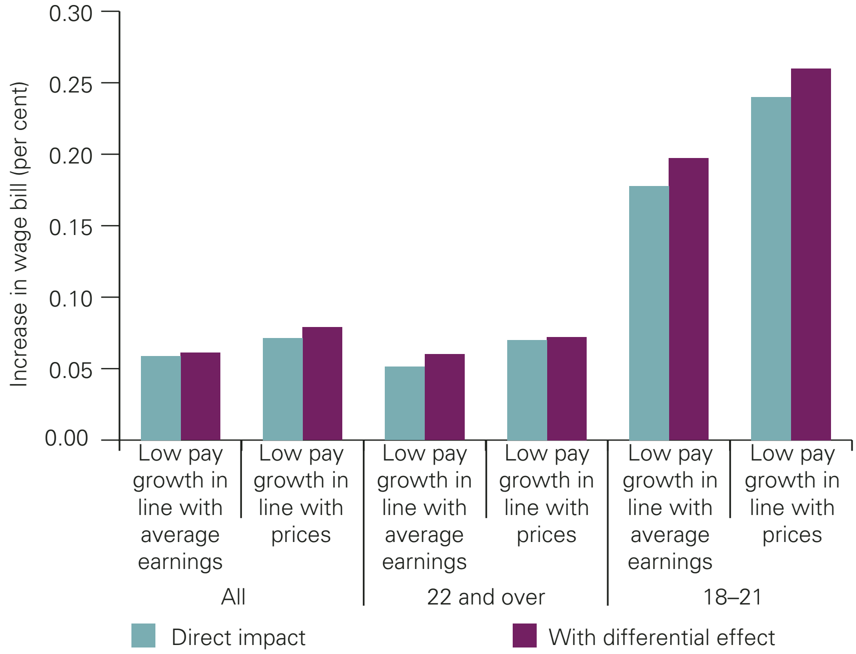
2.94 In our fourth report (2003), we adopted two alternative assumptions about the growth in earnings of the low paid in the absence of a new rate. The assumptions were first, either that earnings would grow at roughly the same rate as the growth in average earnings or that these earnings would grow at roughly the same rate as the growth in prices.

2.95 The second assumption we need to make is about the effect of differentials on the earnings distribution. In our fourth report we assumed that the impact on differentials would be limited to around the sixteenth percentile. These assumptions were based on data for 2000–2002. As can be seen in Figure 2.11, which depicts hourly earnings by percentile, this assumption is still reasonable given the latest data.

2.96 Figure 2.21 shows the latest estimates of the wage bill impact of the October 2004 upratings. We estimate that the direct impact of the October 2004 upratings increased the total adult wage bill by between 0.05 and 0.07 per cent and the 18–21 year old wage bill by between 0.18 and 0.24 per cent. Taking account of differentials this rises to 0.06 to 0.08 per cent for adults and 0.2 to 0.26 per cent for youths.

Figure 2.21

Estimated Impact on Wage Bills of the 2004 Minimum Wage Upratings, April 2004



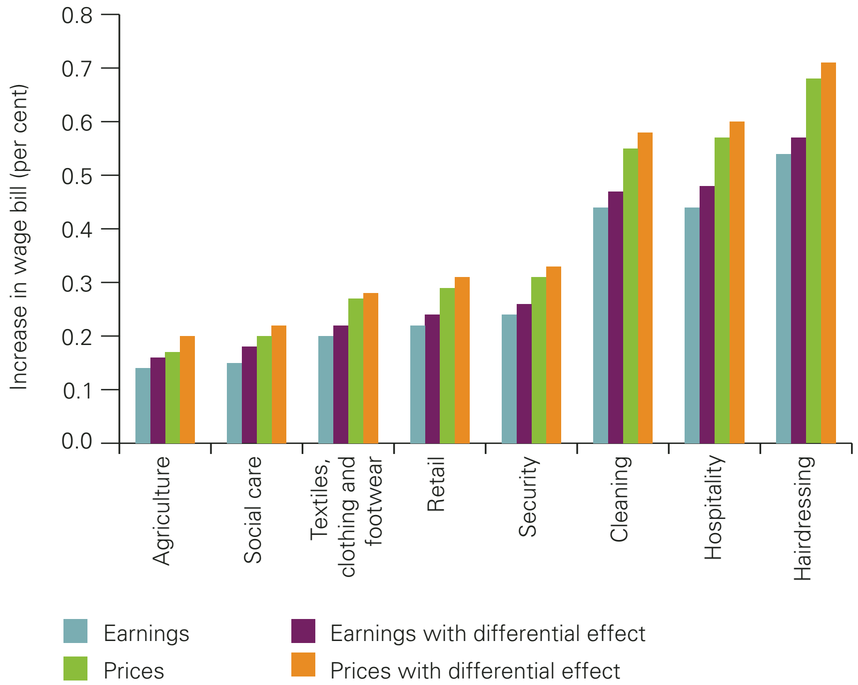
Source: LPC calculations based on ASHE 2004, with supplementary information.

2.97 Comparing our estimates with those in the fourth report (2003), we now estimate that the direct effect of the October 2004 upratings was to increase the aggregate wage bill by between 0.06 and 0.07 per cent, compared with 0.05 to 0.09 per cent estimated in our fourth report (2003). Taking account of the impact on differentials raises the aggregate wage bill estimate to 0.06 to 0.08 per cent compared with the estimate of 0.09 to 0.13 per cent presented in the fourth report (2003).

2.98 Figure 2.22 looks at the impact of the 2004 minimum wage upratings on the wage bills in low-paying sectors. We can see that there are larger impacts on these sectors than on the economy as a whole. The largest impacts, in terms of percentage increase in the wage bill, are in hairdressing, hospitality and cleaning. The largest monetary impacts, however, are in the retail and hospitality sectors.

Figure 2.22

Estimated Impact on Wage Bills of the 2004 Minimum Wage Upratings on the Low-paying Sectors, April 2004



Source: LPC calculations based on ASHE 2004, with supplementary information.

Profits, Productivity and Prices

2.99 In our analysis above, we found that the minimum wage has had little effect, at the macroeconomic level, on employment or hours of work. This section considers whether the effect of the minimum wage might be felt instead through a fall in profits or an increase in prices.

2.100 First, we analyse the impact of the minimum wage on profits at a macroeconomic level. Second, we analyse whether there is any tendency for profit margins in the low-paying sectors to be more affected than those not exposed to changes in the minimum wage. Third, we look at the impact of the minimum wage on productivity and, finally, in this section we consider whether any price effects arise from upratings to the minimum wage.

Profits in the Macroeconomy

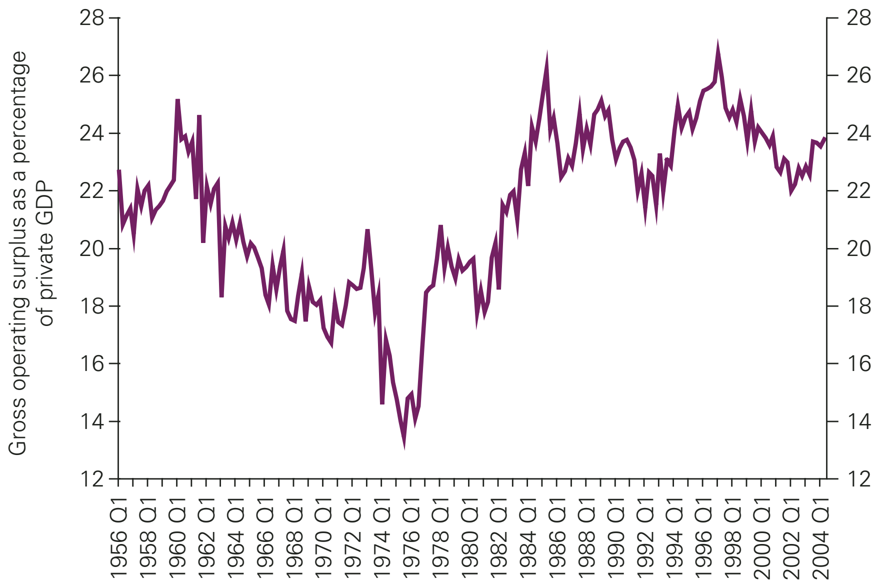
2.101 Fluctuations in the share of profits in gross domestic product (GDP), and in profit margins, are an important aspect of overall macroeconomic performance. Profits are the source of retained earnings by companies, which make up a major source of finance for investment spending. A higher rate of profit tends to be closely related to higher levels of investment spending on the modernisation and expansion of the capital stock. In turn, this enables higher levels of productivity, rising living standards and growth in the level of employment.

2.102 Overall, it appears that the profitability of the whole economy is currently at a healthy level. According to the Bank of England (2004) '...higher profits and ample corporate liquidity point to continued healthy growth in capital spending by business'. Further, the Bank of England goes on to note that, having been negative for extended periods since 1987, the financial balance of private non-financial corporations has remained in positive territory for the past two years.

2.103 This largely positive conclusion is borne out by Figure 2.23, which shows the long-term trend in the measure used by the Bank of England – the gross operating surplus of non-financial corporations as a percentage of private sector GDP.

Figure 2.23

Gross Operating Surplus of Non-financial Corporations as a Percentage of Private Sector GDP, 1956–2004



Source: ONS, current prices, not seasonally adjusted, 1956–2004.

Note: Private sector GDP is approximated by subtracting General Government Final Expenditure from Gross Domestic Product.

2.104 On this measure, the share of profits fell from the mid-1960s to the mid-1970s, but then staged a recovery up until the mid-1980s. Since the mid-1980s, the ratio has essentially gone sideways, fluctuating with the ebbs and flows of the business cycle. More recently, the data indicate that profits as a share of GDP reached a peak of 26.7 per cent in the first quarter of 1997, then fell to a low of 22 per cent in the first quarter of 2002 before recovering from the second quarter of 2003 onwards.

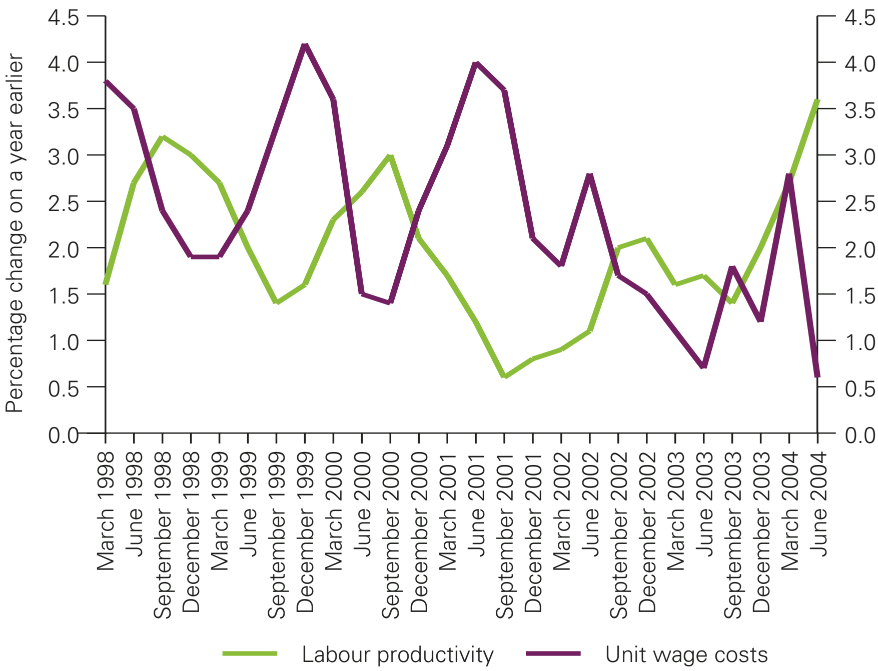
2.105 These movements in the profits share depicted above appear consistent with cyclical fluctuations such as those encountered in normal business cycles, and do not suggest any sustained deviation from the range that has been established over the last 20 years.

2.106 Some have suggested that, should the economy continue to grow at an above trend rate, a downturn in profits might result from renewed wage inflation as the labour market tightens. So far however, as noted above, there is no sign of increasing wage inflation. And such an effect could be offset if tight labour markets were accompanied by productivity growth.

2.107 The interaction between productivity growth and unit labour costs is depicted in Figure 2.24 below. According to the Bank of England (2004), productivity growth 'together with relatively subdued earnings growth means that annual growth in private sector unit wage costs slowed to less than 1 per cent in the second quarter of 2004. So currently, there is little near-term pressure from wage costs on CPI inflation.' Equally, there will be no macroeconomic tendency for profits to be squeezed by rising wage costs.

Figure 2.24

Private Sector Labour Productivity and Unit Wage Costs, 1998–2004



Source: ONS, Bank of England calculations, 1998–2004.

Notes:

1. Private sector labour productivity is private sector output divided by private sector workforce jobs. Private sector is defined as the whole economy less the public administration, education, health and social work sectors. The workforce jobs series has been adjusted so that it corresponds to calendar-year quarters. This measure of productivity is based on output per job rather than output per hour.
2. Private sector unit wage costs are private sector AEI (including bonuses) divided by private sector labour productivity.

'The overall UK economy performed very creditably during the second half of 2003 and the first half of 2004. However, the profits-to-GDP ratio remains well below the peak seen in the late 1990s cycle and the CBI is sceptical about the ability of this ratio to recover much in the short term. This relative squeeze on profits means that any increase in the NMW will be much less affordable than might be implied by simply looking at the state of the macro-economy.'

CBI evidence

2.108 Although the share of profits in private GDP is illuminating, it is not the measure that business people would use in gauging the success of an enterprise. Instead, they would typically focus on the rate of return on capital employed. ONS publishes rate of return data, both gross and net, for private non-financial corporations excluding UK Continental Shelf companies and it is these data to which we turn next.

Figure 2.25

Gross and Net Rates of Return on Capital Employed, All Private Non-financial Corporations Excluding UK Continental Shelf Companies, 1989–2004

Source: ONS, seasonally adjusted, 1989–2004.

For service sector firms in general rates of return have remained very high. In 2004 the average net return on capital for public corporations classified to the service sector was 15.5 per cent. There has been no significant difference in average profitability comparing the five years 1999–2004 with the previous five years. By international standards these returns are very high.

TUC evidence

2.109 Drawing on ONS quarterly data on rates of return since 1989, Figure 2.25 shows that the 1990/91 business cycle recession gave rise to a much more severe downturn in the rate of return than has occurred during the recent period, when the minimum wage was in operation.

2.110 Overall, we conclude that there is no evidence to suggest that the introduction and the upratings of the minimum wage have so far had any measurable effect on the profitability of UK companies in aggregate.

Profits at a Sector Level

2.111 Even if profits at the level of the whole economy have not been influenced by the minimum wage, there could be sectoral effects. For instance, there could be low-paying sectors in which it was difficult to achieve productivity increases or to increase prices.

2.112 Unfortunately, it is extremely difficult to analyse profitability trends in specific sub-sectors. In general, the service sectors of the economy (which include the specific sectors which employ the vast majority of low-paid workers) enjoy higher rates of return than manufacturing, but this is solely because they are less capital intensive (on conventional accounting measures of capital). And while the service sectors in total are, in the third quarter of 2004 according to ONS data, earning returns of 15 per cent, a little below the 2003 average of 15.7 per cent, these data are still too aggregated to allow any conclusions about minimum wages in specific sectors.

2.113 Overall, therefore, an analysis of aggregate data, both at the whole economy and at sectoral level, does not allow a firm conclusion. We have no reason to believe that profits have been reduced by the minimum wage, at sectoral level let alone national level, but it is impossible to conclude definitely that no profit squeeze has occurred. We have therefore supplemented our analysis of the available aggregate data with attempts to investigate individual company effects.

Commissioned Research on Profits and Margins

2.114 There is by now a large body of work examining the impact of the minimum wage on employment, focusing particularly on the question as to whether or not minimum wages price workers out of jobs. Since substantial employment effects have not been found, the question arises as to how firms are able to sustain the higher wage costs induced by minimum wages. If employment effects are small, then something else has to give. It may be that the minimum wage eats into profit margins, or prompts firms into raising prices. This is a significantly under-researched area. We therefore commissioned Draca, Machin, and Van Reenen (2005) to carry out empirical work in this area.

2.115 The researchers compared profitability and prices in low wage firms and industries before and after the introduction of the minimum wage compared with higher wage firms and industries. They found that wage growth in the low wage firms in low pay industries after the introduction of the minimum wage was 9.2 per cent higher than in the comparison group. In turn, the introduction of the minimum wage was associated with a fall in profit margins in the low wage firms and an increase in profit margins at the higher wage firms. Overall, profit margins for the most affected firms fell by a statistically significant 4.9 per cent compared with higher wage firms. Draca, Machin and Van Reenen therefore concluded that profitability fell in firms that were more affected by the introduction of the minimum wage.

2.116 This margin squeeze in low-wage firms does not, however, seem to have been sufficiently large as to force firms out of business. While there was a slight increase in the exit rate of firms from the

‘Unlike infant or growth industries, where there is a great deal of scope for increased efficiency and competitiveness, retail is a mature industry, and it is a constant challenge for retailers to increase their levels of competitiveness.’

BRC evidence

‘Employers have often argued they are unable to increase prices to offset high labour costs. However, prices charged by “hairdressing and personal grooming establishments” went up by 4.5 per cent in the twelve months to August 2004 while prices charged by hotels and restaurants increased on average by 2.9 per cent compared with the overall increase in the index of 1.3 per cent (all figures Consumer Price Index).’

TUC evidence

experimental group versus the control group over the period, the difference was not statistically significant. Draca, Machin and Van Reenen concluded therefore that ‘it is hard to detect any evidence that the minimum wage raised wage costs so much as to force low wage firms out of business’. This is consistent with the findings of other research that the minimum wage has had no significant adverse employment effects.

Productivity

2.117 As discussed above, and highlighted in Figure 2.24, labour productivity at the macroeconomic level has been growing since 2001. It has primarily been driven by factors other than the minimum wage. We commissioned some research to look at the impact of the minimum wage on productivity. Galindo-Rueda and Pereira (2004) found that in the service sector there was evidence of a positive one-off effect on labour productivity following the introduction of the minimum wage, however, they found no significant impact on labour productivity in the manufacturing sector.

Prices

2.118 As for price effects, the Draca, Machin and Van Reenen (2005) research could find only minimal price effects, concentrated in particular in the canteen and catering sector. But they also noted the severe methodological difficulties involved in researching this area, and it is possible that there are price effects which it is impossible to discern from this analysis.

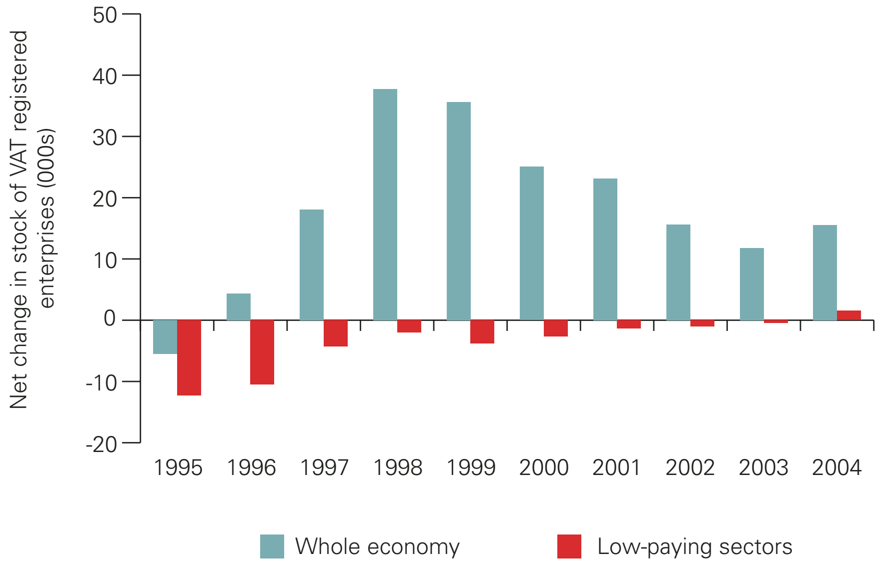
Business Start-Ups and Failures

2.119 Another way of looking for the impact of the minimum wage would be to look at the levels and changes in both business start-ups and business failures. Arguably, an increase in the minimum wage might make it less attractive to start a business (for example by forcing wages higher). Alternatively, increases in the minimum wage could squeeze profits of existing firms leading to an increased number of business failures.

2.120 Figure 2.26 shows that there has been an increase in the number of VAT registered businesses in every year since 1995. During 2003 there were almost 190,000 registrations, but fewer than 175,000 de-registrations, leading to an increase of 15,500 in the stock of UK businesses. The Figure also shows that the introduction of the minimum wage has had little adverse impact on the number of businesses registered in the low-paying sectors. Indeed, despite the large upratings in the minimum wage in October 2003, the number of businesses in the low-paying sectors increased during 2003.

Figure 2.26

Net Change in the Stock of VAT Registered Enterprises in the UK, Thousands, 1995–2004



Source: Small Business Service (2004).
Note: Stock is at 1 January of the given year.

2.121 Figure 2.26 also shows that there was a fall in the stock of low-paying sector businesses in 1999. It was not surprising, therefore, that Galindo-Rueda and Pereira (2004) found that employment and business creation became slower in areas of the country where the minimum wage had greater effect, although this was partly explained by a trend preceding the introduction of the minimum wage. In their study on profits and margins, Draca, Machin and Van Reenen (2005) were unable to find any evidence that the minimum wage had caused low-paying firms to go out of business.

‘Market conditions in the sectors most affected by the NMW have meant there has been little, if any, scope to raise prices in response to higher labour costs.’

CBI evidence

Conclusion

2.122 In this Chapter we have assessed the overall impact of the minimum wage, focusing on the most recent upratings which by our calculations will have increased the earnings of over one million workers. Despite its widening impact, we continue to find strong support for the minimum wage from employers as well as workers. Evidence from econometric studies we commissioned suggests any negative effects of the minimum wage have been minimal. Most firms have been able to accommodate the increases without too much difficulty.

2.123 It is important that we continue to monitor the impact of the minimum wage, improving our understanding of the way it affects the labour market in particular and the economy in general. Among the key issues for future consideration by the Commission are a more detailed analysis of our estimates of the number of beneficiaries; consideration of the role of migrant workers; and an assessment of the ability of firms to pass on the costs of the minimum wage in prices.

2.124 We now go on to consider in Chapters 3, 4 and 5, those sectors and groups of workers where the impact of the minimum wage has been most acute, examining in detail the issues affecting them.

The Effects of the National Minimum Wage on Specific Sectors and on Small Firms

We have identified nine sectors of the economy where low pay is common and which are most affected by the minimum wage. These nine sectors provide around six million employee jobs, nearly a quarter of all the jobs in the UK economy. About three-quarters of these jobs are to be found in the retail and hospitality sectors.

We found evidence of continued employment growth in the two largest low-paying sectors and stable or growing employment in most of the others. In the two sectors where job numbers are falling, i.e. the agriculture sector and the textiles, clothing and footwear sector, the decline is part of a long-term trend attributable to external factors. As in previous reports, we found that the cleaning and security industries experience some problems in renegotiating long-term contracts to take account of minimum wage upratings.

The evidence presented to us has suggested that the minimum wage is becoming less of an issue for some small firms, but, conversely, a more significant issue for some large firms. There is, for example, evidence that some larger firms – particularly in the retail sector – are, for the first time, having to make adjustments to their pay structures as a result of recent increases in the National Minimum Wage. Overall we have found no evidence of any insuperable difficulty in coping with the October 2003 upratings, nor have we discovered any negative impact on employment. But our analysis concentrates on the impact of the October 2003 upratings, with only limited data available relating to the October 2004 upratings. We are aware that many employers in the low-paying sectors have expressed concern about the impact of the increase in the adult rate to £4.85 per hour.

We also discuss in this Chapter the complex issue of salary sacrifice, an arrangement whereby a worker agrees to a reduction in pay in return for a non-cash benefit, and note that the National Minimum Wage Regulations do not permit those earning the minimum wage to participate in these schemes. We conclude by recommending that the

Government invite us to consider the issue in depth and to report back by February 2006.

We recommend that the maximum daily accommodation offset should increase to £3.90 in October 2005 and £4.15 in October 2006, in line with our recommendations for the adult rate of the minimum wage.

We continue to receive evidence that some local authorities are not taking full account of minimum wage upratings, including the costs of travelling time, when calculating fees for private care provision. We note that progress has been made in this area and recommend that the Government continue to make clear to local authorities that policies on commissioning care should reflect the costs of provision. We also recommend that the Government should monitor the approach of local authorities to the funding of social care. Two further issues which affect the social care sector are 'sleepovers' and on-call arrangements. We believe that greater publicity of the guidance is needed to ensure that the rules are understood.

Introduction

3.1 In this Chapter we look at the impact of the minimum wage on the sectors where low pay is common, which we have identified from the New Earnings Survey data. We consider the economic circumstances in which these sectors are operating and their responses to the October 2003 upratings. We also assess any sector specific issues stemming from the National Minimum Wage Regulations 1999.

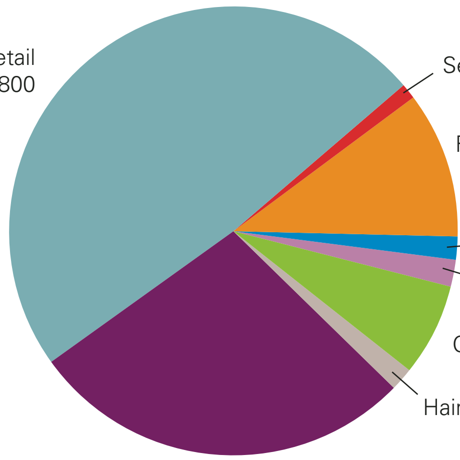
3.2 We have obtained information from a wide range of sources, including statistical data provided by the Office for National Statistics (ONS), our programme of research, our employer survey, responses to our consultation and a wide-ranging series of meetings and visits. The full results of our employer survey are in Appendix 3. As we explain there, it is important to bear in mind that the responses to our questionnaire are likely to overstate the impact of the National Minimum Wage on firms for two main reasons. First, the survey specifically targeted those low-paying sectors that are most likely to have been affected. Second, even within these sectors, respondents are more likely to have been affected than non-respondents. Nevertheless our survey does provide useful information to make comparisons between sectors on the impact of the minimum wage.

3.3 We begin the Chapter by providing an overview of the impact of the minimum wage on sectors where low pay is common. We then consider the impact on small firms, since previous reports found that they have been disproportionately affected by the minimum wage. We go on to consider the impact of the minimum wage on the nine sectors we have identified as being those where low pay is common: retail, hospitality, cleaning, security, childcare, social care, agriculture, the manufacture of textiles, clothing and footwear, and hairdressing. The role of the accommodation offset is considered within the analysis of the hospitality sector. The issue of salary sacrifice is addressed under the retail sector and issues relating to sleepovers and on-call arrangements are covered in the analysis of the social care sector.

Overview

3.4 The sectors we consider in this Chapter (excluding childcare) account for around 6 million jobs, nearly 24 per cent of all UK employee jobs. Figure 3.1 shows the relative proportion of jobs in each of the sectors. As can be seen, nearly half are in retail and over a quarter in hospitality.

Figure 3.1
Breakdown of Jobs in Low-paying Sectors, Thousands, September 2004

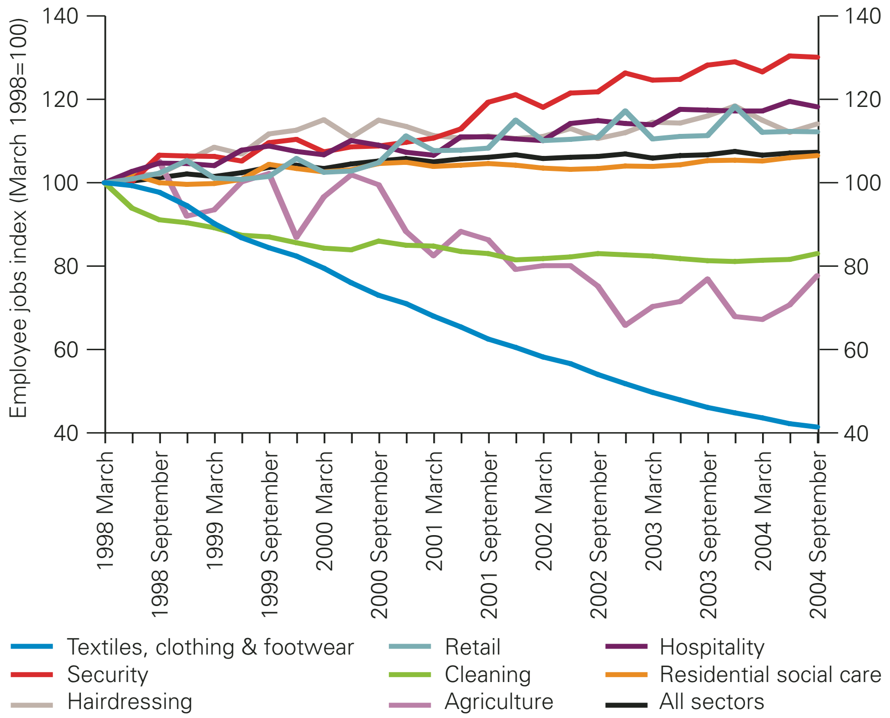


Source: ONS employee jobs series, September 2004, GB.

3.5 Recent employee job trends by sector are shown in Figure 3.2. This shows that since the introduction of the minimum wage there has been strong growth in the number of employee jobs in both hospitality and security, and noticeable falls in textiles, clothing and footwear, cleaning and agriculture, hunting and forestry (referred to as agriculture in the remainder of this Chapter). In the year to September 2004 the number of employee jobs increased in most low-paying sectors, particularly security and cleaning, but fell in textiles, clothing and footwear and hairdressing. During this period the total number of jobs in the economy rose by 0.5 per cent (140,000 jobs), and the number of jobs in low-paying sectors rose by the same percentage (over 30,000 jobs). Looking at the micro level, in response to our employer survey the retail, hospitality, textiles and hairdressing and beauty (referred to as hairdressing in the remainder of this Chapter) sectors were the most likely to report reductions in staffing levels as a result of the October 2003 upratings, but the childcare and social care sectors were the least likely to report reductions. Further information on trends in employee jobs in the low-paying sectors can be found in Appendix 5.

Figure 3.2

Change in Employee Jobs in Low-paying Sectors, 1998–2004

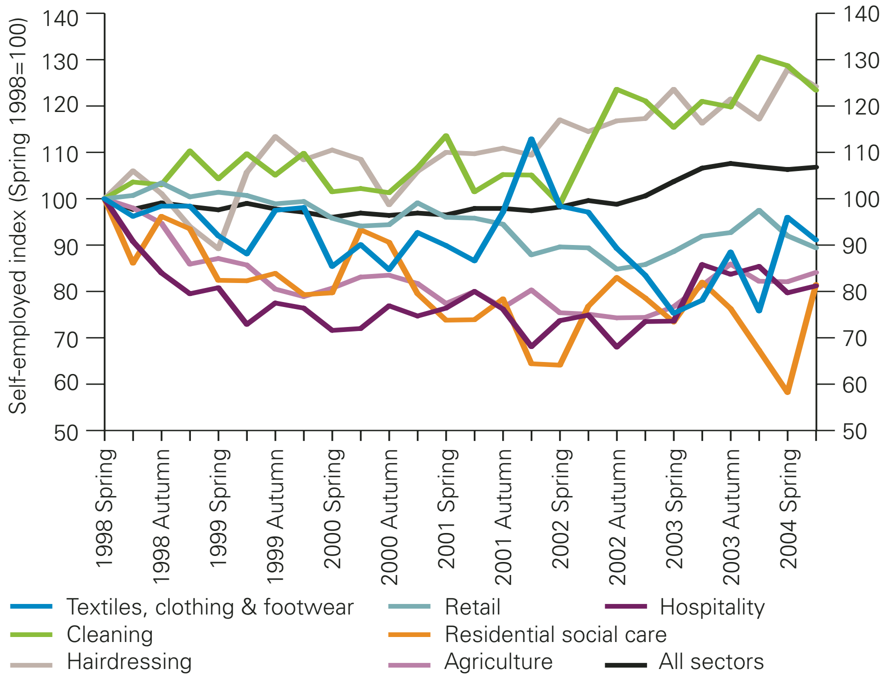


Source: ONS employee jobs series, 1998–2004, GB.

3.6 Trends in self-employment by sector are given in Figures 3.3 and 3.4. They show that self-employment has increased by around 25 per cent in both the hairdressing and cleaning sectors since the introduction of the minimum wage. This represents an increase in the level of self-employment by 20,000 in hairdressing and 10,000 in cleaning. Self-employment fell by nearly 20 per cent in both hospitality and residential social care, with the levels falling by 30,000 and 3,000 respectively. However, the largest reductions in the level of self-employment were in the retail and agriculture sectors (both fell by around 35,000).

Figure 3.3

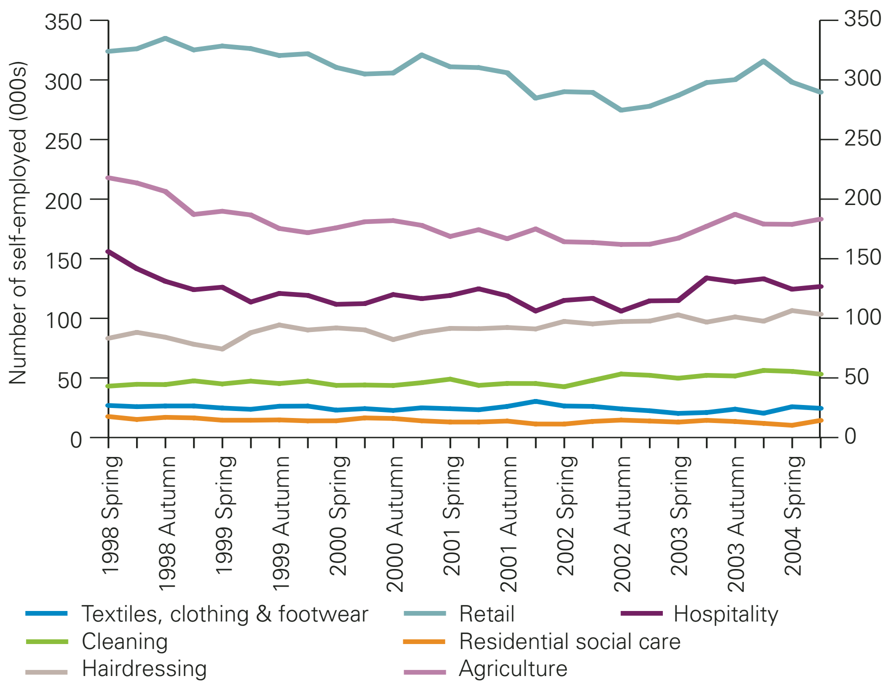
Change in Self-employment in Low-paying Sectors, 1998–2004



Source: Labour Force Survey (LFS), 1998–2004.

Figure 3.4

Number of Self-employed by Sector, Thousands, 1998–2004



Source: LFS, 1998–2004.

3.7 Table 3.1 shows that the cleaning, hospitality and hairdressing sectors have the highest percentage of employees aged 18 and over paid below or only just above the adult rate of the minimum wage. It also shows, comparing the position which applied after the upratings of 2001 with that following the October 2003 upratings, that there has been no significant change in the proportion of employees aged 18 and over being paid below or only just above the level of the adult minimum wage. The Table also illustrates the fact that a relatively high percentage of nursery nurses and employees in the hairdressing and hospitality sectors are paid below the adult rate of the minimum wage, reflecting more significant use of the youth Development Rate and exemptions from the minimum wage for apprentices in these sectors. Further information on hourly earnings in the low-paying sectors is presented in Appendix 5.

Table 3.1 Percentage of Employees Aged 18 and Over Paid the Adult Minimum Wage or Below by Sector/Occupation, 2002–2004

	April 2002		April 2003		April 2004	
Sector/ Occupation	**Percentage paid £4.10–£4.19**	**Percentage paid below £4.10**	**Percentage paid £4.20–£4.29**	**Percentage paid below £4.20**	**Percentage paid £4.50–£4.59**	**Percentage paid below £4.50**
Retail	5.2	4.2	3.6	3.5	5.4	5.2
Hospitality	16.4	12.6	13.7	7.6	15.4	12.1
Cleaning	17.4	4.4	11.1	3.8	13.2	4.1
Security	5.2	1.7	4.9	2.4	4.9	2.0
Nursery nurses	4.1	8.6	3.0	8.1	4.3	9.3
Residential social care	5.9	3.4	4.0	3.7	3.6	1.9
Agriculture	3.7	2.3	1.7	2.8	2.7	1.7
Textiles, clothing and footwear	4.8	2.4	4.8	1.0	5.2	2.0
Hairdressing	10.1	14.0	9.6	13.1	9.2	12.5
All low-paying sectors	7.8	5.7	6.2	4.3	7.8	6.3
Total UK economy	2.2	2.1	1.7	1.7	2.2	2.1

Source: Annual Survey of Hours and Earnings (ASHE), April 2002–2004 without supplementary information.
Note: The adult rate of the minimum wage was £4.10 per hour in April 2002, £4.20 per hour in April 2003 and £4.50 per hour in April 2004.

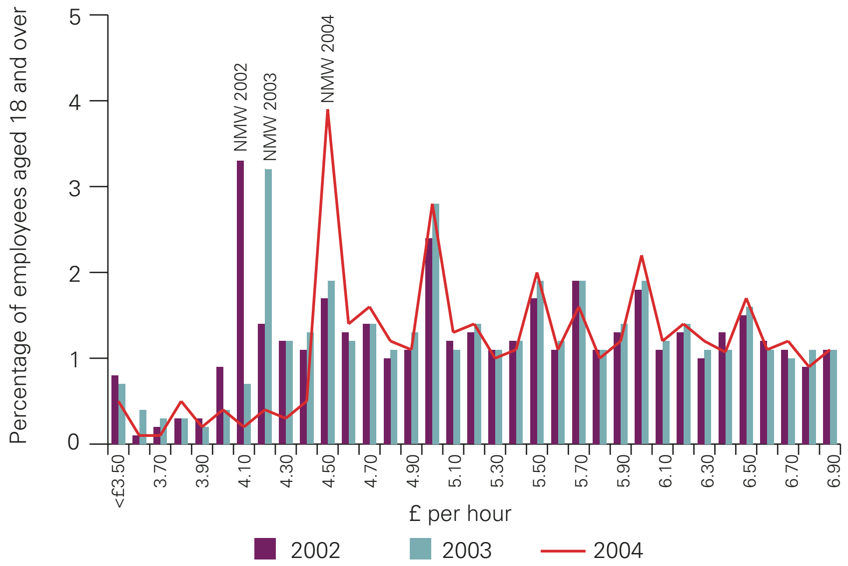
Small Firms

3.8 According to the latest data available from the Small Business Service (SBS), at the start of 2003 there were just over one million firms (comprising the private sector, non-profit organisations and Government) in the UK employing between one and nine workers. A further 170,000 firms employed between 10 and 49 workers. Ninety-seven per cent of firms with employees in the UK employ fewer than 50 people (and are thus commonly defined as a small firm), and they account for 29 per cent of employment (27 per cent of employees) and 31 per cent of turnover. This compares with large firms (those with 250 or more employees), which account for less than 1 per cent of all firms but for 63 per cent of employees and 56 per cent of turnover. The proportion of small firms operating in the low-paying sectors is broadly in line with the economy as a whole.

3.9 In previous reports we found that small firms were disproportionately affected by the minimum wage. Figures 3.5–3.7 demonstrate that the coverage of the minimum wage (the height of the spike at the adult rate of the minimum wage) appears to get smaller as firm size increases, suggesting that smaller firms continue to be more affected by minimum wage upratings.

Figure 3.5

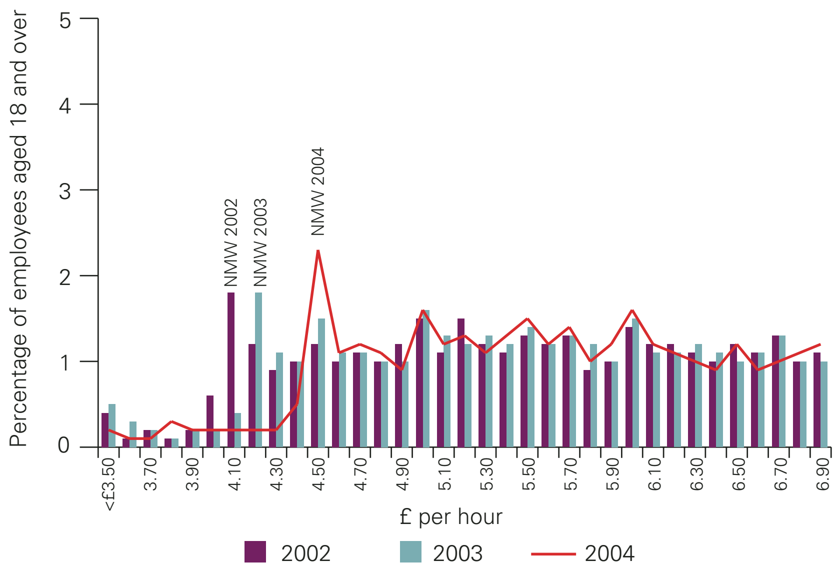
Hourly Earnings Distribution for Employees Aged 18 and Over in Small Firms, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. Businesses with 1–49 employees.
2. NMW label shows the adult NMW rate in April of the given year.
3. Gross hourly earnings excluding overtime.

Figure 3.6

Hourly Earnings Distribution for Employees Aged 18 and Over in Medium-sized Firms, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. Businesses with 50–249 employees.
2. NMW label shows the adult NMW rate in April of the given year.
3. Gross hourly earnings excluding overtime.

Figure 3.7

Hourly Earnings Distribution for Employees Aged 18 and Over in Large Firms, 2002–2004

Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. Businesses with 250+ employees.
2. NMW label shows the adult NMW rate in April of the given year.
3. Gross hourly earnings excluding overtime.

'The NMW is having an increasing impact on small businesses. It is evident that members' clients now have stronger views on the NMW. In 2000 and 1999 the majority of members perceived their clients to be 'indifferent' towards the NMW. In the latest survey, members see their clients as being significantly more 'divided' on the issue, with increasing numbers being either 'for' or 'against'.'

Association of Chartered Certified Accountants evidence

3.10 However, some evidence from our consultation suggests that the minimum wage is having less impact on small firms than was previously the case. Only one per cent of the 7,000 small and medium-sized enterprises with employees in the SBS annual survey of 2003 identified the minimum wage as an obstacle to their success. This compares with 6 per cent in their equivalent 2001 surveys.

3.11 Moreover the Federation of Small Businesses (FSB) advised us that in general the results of its survey of small to medium-sized enterprises, carried out in November 2003, reflected well on the operation of the minimum wage. In the survey, which received over 18,500 responses, 16 per cent of respondents reported having to increase pay for adult workers and 7 per cent for 18–21 year olds following the October 2003 upratings. One in five respondents reported that they would increase pay in order to maintain differentials. The FSB stressed, however, that the impact varied by sector and by region.

3.12 On the other hand, there were some bodies which maintained that small firms continued to be more affected by the minimum wage and that the impact is increasing. One such organisation was the Association of Chartered Certified Accountants. It advised that small businesses often lacked the resources to implement increases. It also noted that businesses in certain sectors are particularly affected by the minimum wage and stated that the impact of the minimum wage on different sectors required more consideration.

3.13 In our fourth report (2003) we found that small firms were often unaware of the information available on the minimum wage, including the National Minimum Wage Helpline. As a result we recommended that the Small Business Service actively promote and disseminate factual information on the minimum wage tailored to the requirement of small firms. The subject did not emerge as an issue in our consultation this time round, suggesting that progress has been made. Moreover, the research we commissioned from Cronin and Thewlis (2004), on small firms' adjustments to the minimum wage, found that nearly all the employers involved knew the current adult rate.

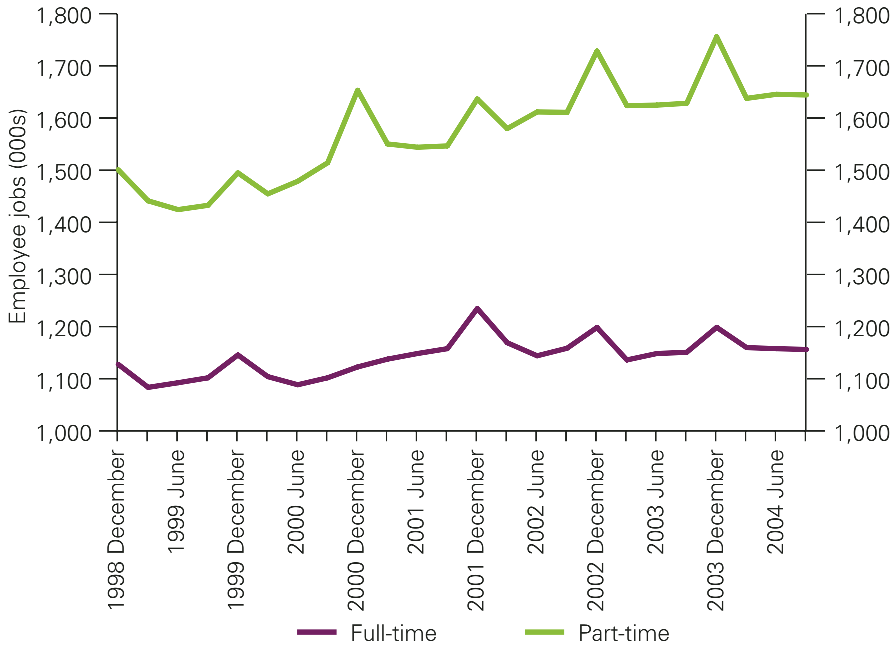
Retail

3.14 Following a period of weaker growth in the retail sector in 2003, 2004 saw a return to the stronger annual growth in retail sales experienced in 2001 and 2002, reaching 7.7 per cent for all retailing in the third quarter of 2004. According to the ONS Retail Sales Index, growth in the predominantly non-food sector outstripped growth within predominantly food stores. The British Retail Consortium (BRC) (BRC-KPMG, 2005) has, however, expressed concern that disappointing Christmas 2004 trading figures were a reflection of a fall in consumer confidence. The BRC-KPMG Retail Sales Monitor indicated that like-for-like sales fell by 0.4 per cent in December 2004 compared with the same period a year earlier, while total sales grew by 2.5 per cent.

3.15 Figure 3.8 shows that the number of employee jobs in the retail sector has increased steadily since the introduction of the minimum wage, but has grown more slowly since 2002. Between September 2002 and September 2004 employee jobs increased by 31,000, compared with an increase of 153,000 between September 2000 and September 2002. In the year to September 2004 the number of full-time and part-time employee jobs increased by 5,000 and 16,000 respectively.

Figure 3.8

Employee Jobs in the Retail Sector, Thousands, 1998–2004

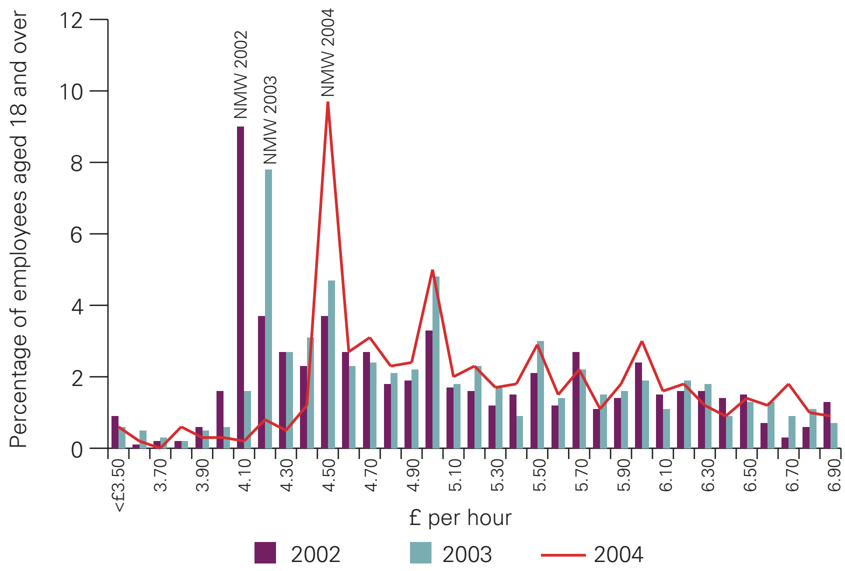


Source: ONS employee jobs series, 1998–2004, GB.

3.16 In previous reports, we noted that in general smaller retailers were more affected by the minimum wage than larger firms. However, evidence received for this report indicated that the minimum wage is now increasingly influencing wage levels for larger firms, particularly since the October 2004 upratings. This can be illustrated by considering trends in the extent to which wage levels are bunched around the minimum wage. For small retail firms, Figure 3.9 shows that the percentage of all workers paid at the adult minimum wage was nearly 10 per cent in April 2004, compared with nearly 8 per cent in April 2003 and 9 per cent in April 2002. For large retail firms (Figure 3.10), 4.4 per cent of workers were paid at the adult minimum wage in April 2004, which represents a slight increase compared with the previous two years. The percentage directly affected by the minimum wage is still higher in small firms, but the most common hourly rate of pay within large firms is no longer substantially above the minimum wage. In 2004, the hourly earnings distribution peaked at £4.60, or 10 pence above the minimum wage, compared with a peak 30 pence above in 2002 and 2003. The minimum wage, previously largely irrelevant to large firms' wage patterns, now has an appreciable effect.

Figure 3.9

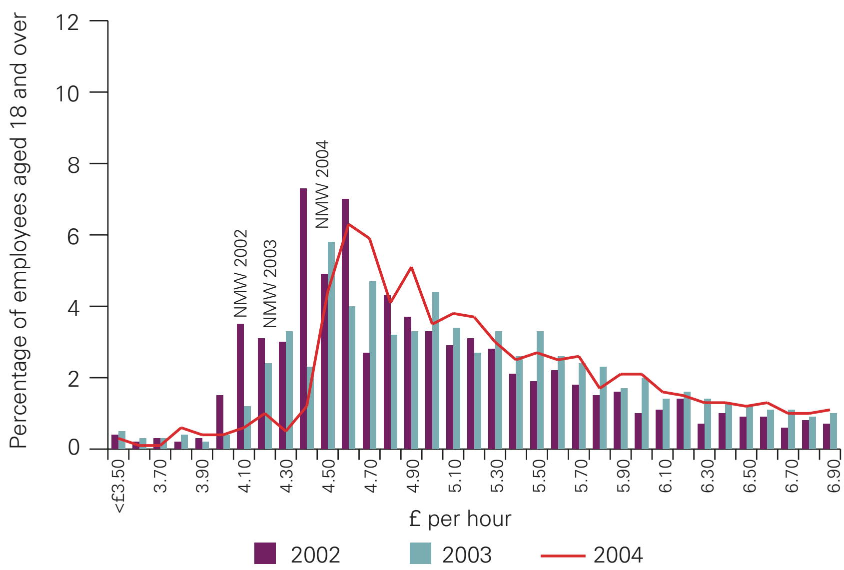
Hourly Earnings Distribution for Employees Aged 18 and Over in Small Firms in the Retail Sector, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. Businesses with 1–49 employees.
2. NMW label shows the adult NMW rate in April of the given year.
3. Gross hourly earnings excluding overtime.

Figure 3.10

Hourly Earnings Distribution for Employees Aged 18 and Over in Large Firms in the Retail Sector, 2002–2004

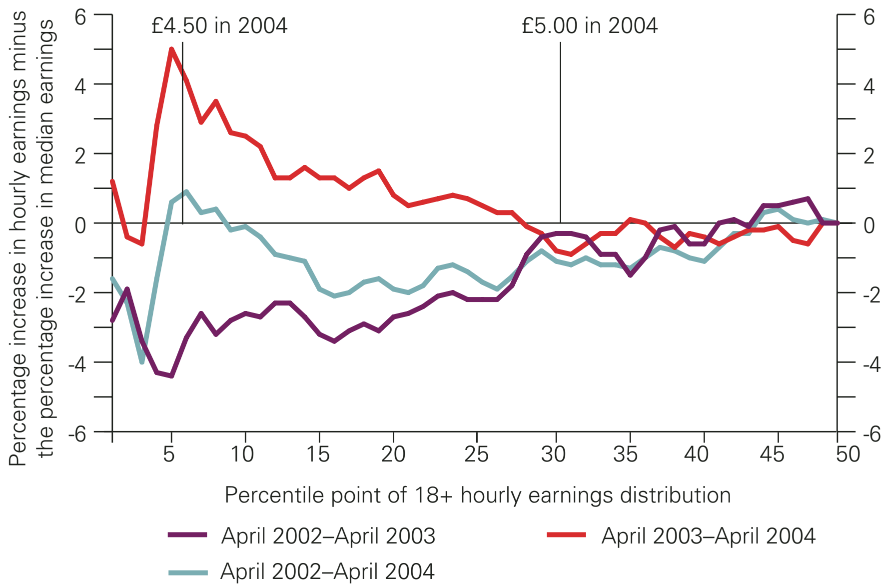


Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. Businesses with 250+ employees.
2. NMW label shows the adult NMW rate in April of the given year.
3. Gross hourly earnings excluding overtime.

3.17 This increasing impact is likely to look more pronounced once we have the April 2005 data, which will also reflect the October 2004 increases. As Figure 3.11 shows, the October 2003 increases did produce some knock-on increases designed to maintain differentials for workers just above the minimum wage. Figure 3.11 also suggests some squeezing of differentials between minimum wage workers and those on, for instance, £5.00 per hour. These effects were, however, reversed in the previous year. The October 2004 increases, coming on top of the significant increases in October 2003, are likely to have a more significant impact on differentials than we have seen before.

Figure 3.11

Increase in Hourly Earnings Minus the Increase in Median Earnings by Percentile for Employees Aged 18 and Over in the Retail Sector, 2002–2004



Source: ASHE April 2002–2004, without supplementary information.

‘Whilst retailers continue to pay above the NMW, unlike two years ago, when retailers’ lowest basic rates were on average twenty to thirty pence higher than the NMW, the average has been reduced to around fifteen pence above.’

BRC evidence

3.18 Qualitative information supports this analysis. The BRC stated in its evidence that ‘the NMW is now having an appreciable detrimental impact on all sizes of retailer, not just SMEs’. In addition Incomes Data Services (IDS) (2004c) noted that the increased ‘bite’ of the minimum wage would now affect most retailers, although pay settlement levels were broadly in line with the trend across the whole economy. The Union of Shop, Distributive and Allied Workers (Usdaw) reported that for the first time, the minimum wage was having an impact on its negotiations.

3.19 The British Shops and Stores Association reported that 43 per cent of respondents to its survey had increased their minimum rates to comply with the minimum wage and responses to our survey (likely to be from those more affected by the minimum wage) suggested that 55 per cent of retailers had been affected by the October 2003 upratings.

Although not directly comparable with our 2002 survey, this was an increase of 15 percentage points compared with firms affected by the 2001 upratings.

3.20 Both Usdaw and IDS (2004b) noted a tendency for employers to move in one of two different directions in response to the increased pressure on the bottom of their pay structures. While some retailers accepted that the minimum wage would now form their lowest rate, others have taken a deliberate decision to move to around £5.00 per hour. This was variously seen as a means to avoid the perceived stigma of being a minimum wage employer, a way to improve staff morale or a response to the tight labour market – or all of the above.

'The NMW is now the lowest rate in many pay structures.... Many of the larger firms are continuing to pursue a policy of maintaining a buffer between their lowest rate and the statutory minimum ... but the increases in the NMW has meant the gap ... has narrowed.'

IDS, 2004c. Pay and Conditions in Retailing 2004/05

3.21 Perhaps partly in response to an increasing minimum wage impact, retailers are taking a range of steps to control wage costs. Case studies and secretariat meetings indicate that some large retailers have reduced Sunday, bank holiday and unsocial hours premiums, although this may be as much a reflection of the trend towards expanded trading hours as a response to the minimum wage. The Association of Convenience Stores told us that smaller retailers in the convenience sector had cut staffing levels by removing supervisory posts but, in some businesses, they could not be cut any further for security reasons. The BRC said that an increasing number of retailers were starting to examine their benefits package as a means to offset further increases. Usdaw noted that a small number of retailers had reintroduced a lower pay band for 18–21 year olds, reversing the long-term trend towards paying adult rates at 18, and the BRC's survey also found increasing use of the youth Development Rate. IDS (2004b) report that companies in the retail sector are moving in different directions in relation to age-related pay. The trend for companies to lower the age at which the full adult rates are paid has continued in some quarters, while others are introducing greater age differentiation into their pay structures.

3.22 Overall the retail sector is clearly being more affected by the minimum wage than previously, and the October 2004 upratings are likely to create some adjustment challenges for many retailers. But there is no sign that the minimum wage has so far had any significant impact on retail sector employment levels.

Salary Sacrifice

3.23 The BRC and a number of large retailers reported that employees in the retail sector who earn the minimum wage (or in some cases slightly more) are unable to participate in a particular type of staff benefit arrangement, usually known as a salary sacrifice scheme. Such schemes generally offer tax and National Insurance Contribution (NIC) advantages to the worker and reduce employer NICs. Salary sacrifice schemes may be used to offer a range of benefits (including pensions and bicycles for travel to work), but the two raised most frequently during our consultation related to childcare vouchers and home computers.

3.24 To participate in these schemes, a worker agrees a change to their contract of employment and accepts an entitlement to a lower salary, usually for an agreed period of time (the 'sacrifice'), in return for another non-cash benefit (which is free of tax and NICs). The minimum wage legislation does not, however, permit workers to accept voluntarily a lower cash wage than the minimum wage. The current minimum wage provisions attach no value to vouchers or stamps or to any benefits-in-kind (with the exception of accommodation), and employers may therefore need to exclude their lowest paid workers from these schemes. Although comments during our consultation were confined to the retail sector, it is possible that larger employers in other low-paying sectors may consider offering these benefits in the future.

3.25 The Commission has some sympathy with the desire of retailers to offer a range of benefits to all staff on an equal basis and regardless of the worker's wage. We also recognise the potential of the salary sacrifice schemes to support Government policy objectives. The Government's Home Computing Initiative seeks to boost computer literacy by encouraging employers to offer home computers to their employees on attractive terms via a hire agreement. And as part of its strategy to provide greater incentives for people to work, the Government has put in place a range of measures to encourage employers to contribute towards the provision of childcare. These include enabling employers to offer a tax and NICs free childcare voucher worth up to £50 per week from April 2005, and the associated administration costs and service charges will also be exempt from tax and NICs.

3.26 On 12 October 2004, the Government invited us to consider whether salary sacrifice schemes involving childcare vouchers should be allowed to count towards minimum wage pay and to report back by the end of 2004. After careful consideration, we informed the Government that we could not provide the advice requested in the short time available and suggested that the task might best be assigned to the period after publication of this report. We believed there were a number of important factors, which need to be weighed very carefully. The

Commission has always believed that the minimum wage should be as simple as possible. This ensures that employers know their responsibilities, workers are clear about their entitlement and the enforcement process remains as straightforward as possible. Any change to the Regulations governing the calculation of minimum wage pay risks making this process more complicated. In addition, low-paid workers claiming the childcare element of the Working Tax Credit may find this a better source of support than childcare vouchers. Furthermore, because a salary sacrifice reduces the amount of NICs that a worker has to pay, it could have an adverse effect on their entitlements to those benefits which are dependent on contributions, in particular the State Second Pension.

3.27 We therefore believe that the issue needs to be reviewed carefully looking at all factors and considering all forms of potential salary sacrifice. **We recommend that the Government invite us to review the issue of salary sacrifice in depth and to report by February 2006.**

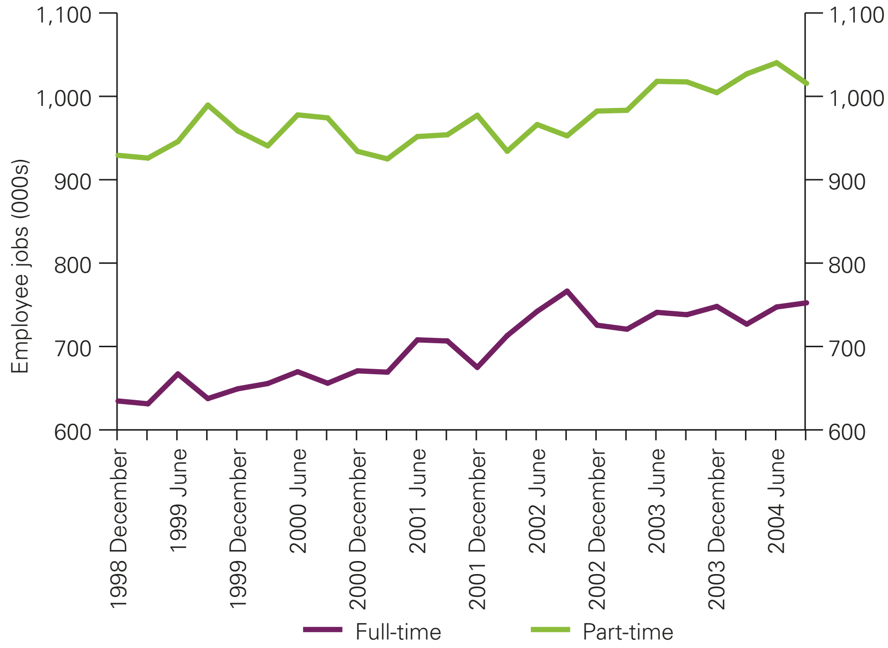
Hospitality

3.28 There are signs that the hospitality sector (which is made up of hotels, providers of holiday accommodation, pubs and bars, restaurants and take away food outlets) has recovered from the sharp decline associated with the foot and mouth crisis and the aftermath of the September 11 attacks in the United States. According to ONS UK National Accounts, output was slightly ahead of growth in the service sector as a whole during the first two quarters of 2004.

3.29 Figure 3.12 shows that the number of employee jobs in the hospitality sector grew by around 140,000 to 1.77 million in the four years to September 2004. Over two-thirds of this growth has been in full-time employee jobs, although like retail, the sector is characterised by a high degree of part-time working (just under 60 per cent of jobs are part-time). Employee jobs growth remained strong in 2002 and 2003 and grew by over 10,000 in the year to September 2004.

Figure 3.12

Employee Jobs in the Hospitality Sector, Thousands, 1998–2004

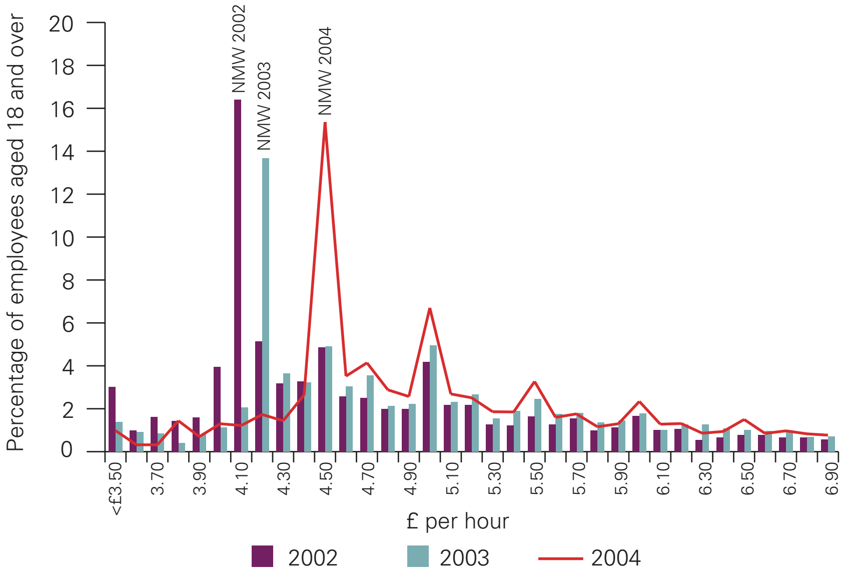


Source: ONS employee jobs series, 1998–2004, GB.

3.30 The minimum wage has had a strong influence on earnings in the hospitality sector, as shown in Figure 3.13. Sixteen per cent of employees were paid at the adult minimum wage in April 2004 according to ASHE 2004a (with supplementary information, not shown), with a further small peak around £5.00 per hour. Increases in lowest decile hourly earnings did not keep pace with the October 2003 uprating of the adult rate (as shown in Appendix 5), rising to £4.44 in Spring 2004. This may reflect the age composition of the workforce in hospitality and fairly widespread use of the youth Development Rate. Twelve per cent of employees were paid less than the adult rate of the minimum wage in Spring 2004. In contrast to the retail sector, in the hospitality sector the shape of the hourly earnings distribution is broadly similar for all firm sizes, although the proportion of employees earning the adult minimum wage is higher in firms with 1–49 employees (19 per cent), than in medium and large firms (12 and 14 per cent respectively).

Figure 3.13

Hourly Earnings Distribution for Employees Aged 18 and Over in the Hospitality Sector, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. NMW label shows the adult NMW rate in April of the given year.
2. Gross hourly earnings excluding overtime.

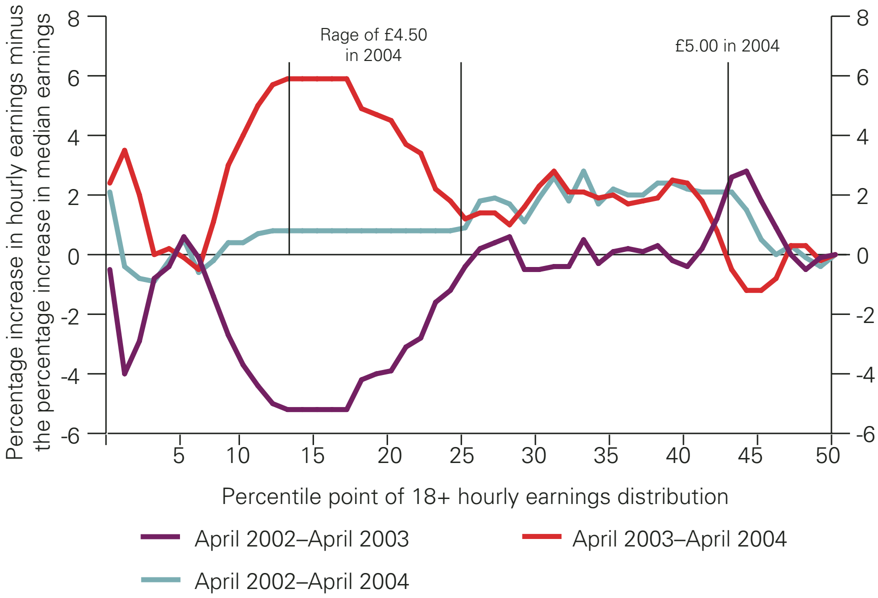
3.31 The hourly earnings data supports evidence from the hospitality industry that the minimum wage is continuing to have a significant impact. Although it should be noted that responses tend to be biased towards those most affected by the minimum wage, 55 per cent of respondents to our survey from the hospitality sector reported that they had been affected by the October 2003 upratings, up seven percentage points compared with responses to our survey on the impact of the 2001 upratings. IDS (2004b) found that most of the hotels it questioned had set their lowest rates at the minimum wage and nearly half had raised rates to comply with the adult minimum wage of £4.50 per hour, up from one third in 2001.

3.32 Hospitality employer associations emphasised the impact on differentials, with companies simplifying pay structures and some reporting difficulties in recruiting and retaining staff. A case study from a major company in the pub and restaurant sector indicated that it had simplified its pay structure from eight to three levels. As a result, differentials to reward experience and skills had largely disappeared, although the company had maintained a higher rate to reflect supervisory responsibilities. The GMB, however, told us that the hotels with which it negotiated had absorbed recent minimum wage upratings with no apparent ill effect and that in many cases the negotiations had sharpened the focus of the companies concerned on attracting and retaining skilled workers.

3.33 Figure 3.14 shows the effects of the 2002 and 2003 upratings of the minimum wage on earnings differentials in the hospitality sector. Employees earning around the level of the adult minimum wage received below median increases following the small October 2002 upratings, but above average increases as a result of the October 2003 upratings. There was also a partial restoration of differentials for employees earning up to about £5.00 per hour following the October 2003 upratings.

Figure 3.14

Increase in Hourly Earnings Minus the Increase in Median Earnings by Percentile for Employees Aged 18 and Over in the Hospitality Sector, 2002–2004



Source: ASHE April 2002–2004, without supplementary information.

3.34 The hospitality sector continues to face high staff turnover, difficulties in recruitment and retention and labour shortages (chefs, for example, continue to be difficult to find), although the British Hospitality Association (BHA) told us that these appear to have eased somewhat in recent months, partly because more staff have been recruited from overseas. The BHA said that, from May to September 2004, about 24,000 workers from eight Eastern European EU accession countries registered to work within the UK hospitality industry.

3.35 While there is no sign that minimum wage upratings have led to job losses, we received evidence that employers have taken a range of actions to control costs, including reducing hours, typically involving 'letting staff leave early if there was no work for them to do during less busy periods' (Cronin and Thewlis, 2004). Although there is some bias towards those most affected, our survey suggested that 47 per cent of

Low Pay Commission Research

A hotel reported that one-quarter of its domestic staff were from eastern Europe ... not only because they were prepared to work at this rate, while local staff were not, but ... the quality of these staff, from a work, service and educational perspective, was considerably higher....

Cronin and Thewlis, 2004. ***Qualitative Research on Firms' Adjustments to the Minimum Wage: Final Report to the Low Pay Commission***

hospitality employers who stated that they were affected by the 2003 upratings had cut overall staffing and 45 per cent had cut basic hours. This sector was also the most likely in our survey to control non-labour costs (41 per cent). Within the pub sector, the British Beer and Pub Association and the CBI both attributed a decline in managed houses to a desire on the part of brewery chains to pass outlets which were not cost-effective to the tenanted sector.

3.36 Overall the hospitality sector is clearly affected by the minimum wage, and the October 2004 increases are likely to create adjustment difficulties for some firms. But the dynamics of hospitality sector employment, and the recruiting difficulties which the sector faces, suggest that the minimum wage so far has had no significantly harmful employment effects.

3.37 We now look at two provisions of the minimum wage legislation which are mainly of interest to the hospitality sector – the accommodation offset and the treatment of tips – before turning to consider the cleaning sector.

Accommodation Offset

3.38 We continue to receive evidence about the level of the accommodation offset. In previous reports we have commented that the offset is not intended to reflect the commercial value of a property or the full cost to the employer of providing accommodation. Rather it has been set so as to strike a balance between these costs, the advantages to the employer of housing workers close to the place of work, and the desire to ensure workers a minimum level of cash wages. In recent years, the accommodation offset has risen in line with increases in the adult minimum wage. It has also been simplified. In our fourth report (2003) we recommended a change to what we considered to be the unnecessarily complicated system of hourly, daily and weekly offset rates. We are pleased that the Government has replaced the old system with a single daily rate, which increased to £3.75 per day from 1 October 2004.

3.39 In evidence, hospitality employer organisations called for a significant increase in the level of the offset to around £40–£50 per week, to reflect the actual costs to employers, to act as an incentive to retain the benefit for workers and to even out differences in pay for those employees who do not receive accommodation. IDS (2004b) found that the majority of hotels charged live-in workers £22–£45 per week for accommodation. Within agriculture, the National Farmers' Union argued that accommodation was a significant benefit and that the minimum

'The rise to £4.85 will add £187,000 to the company's annual wage bill. The company will try to recover this amount principally by cutting hours. So although jobs will not be lost, hours worked and hence take home pay will be affected.'

Brewery employing 1000 people

CBI evidence

'At present the accommodation offset is only around 50% of the average cost of providing accommodation to staff in pubs ... the offset should be increased to be more reflective of accommodation costs.'

British Beer and Pub Association evidence

‘We have received reports of sharing rooms with one or more other workers, where each worker’s wage has been subject to the deduction; substandard, unlettable accommodation; and short-term arrangements which leave workers vulnerable.’

GMB evidence

wage should take greater account of its market value. In contrast, the GMB called for the offset to be frozen for a few years to reflect the significant advantages to the employer of having workers on or near the premises. It was concerned that some employers – particularly in holiday camps – provided accommodation of very low quality.

3.40 We continue to believe that the balanced approach we have taken in previous reports is a fair one, which recognises in part the costs incurred by employers, while ensuring that the value of the minimum wage is maintained for those workers who are provided with accommodation as part of their job. **We therefore recommend once again that the accommodation offset should increase in line with the adult rate of the minimum wage, rising to £3.90 per day from October 2005 and £4.15 per day from October 2006.**

Tips

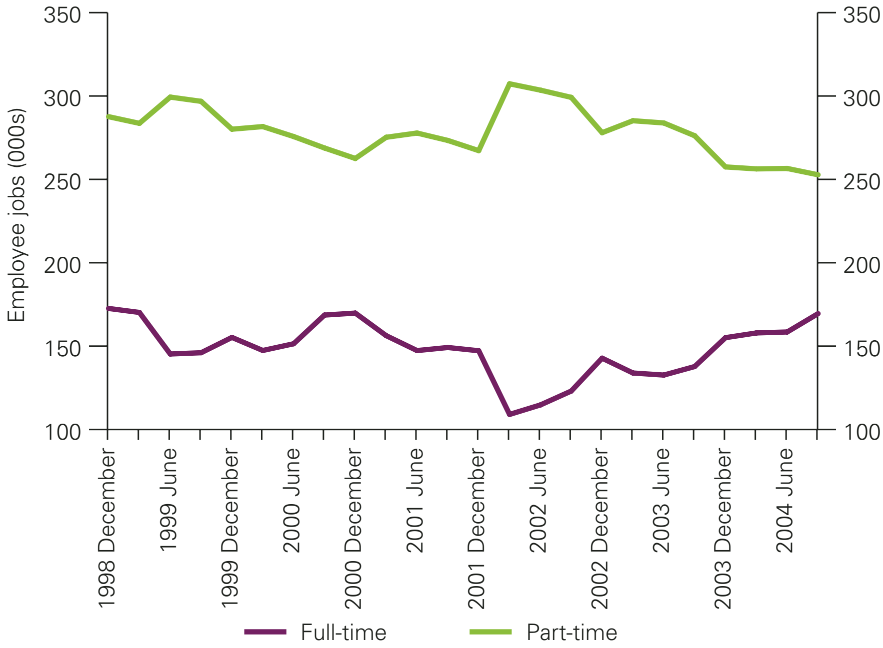
3.41 At present tips can only count towards minimum wage pay if they are collected centrally by the employer and distributed to staff through the payroll. Our research and visits suggest that there continues to be a range of practice, with some employers choosing to put tips through the payroll to make up minimum wage pay and others preferring not to get involved in the collection or distribution of tips and gratuities to staff. While some employer organisations would prefer the rules on the treatment of tips to be relaxed, we believe the current arrangements are working reasonably well and should remain unchanged.

Cleaning

3.42 It is not easy to determine trends in the number of workers in the cleaning sector. The ONS employee jobs series suggests that the number of jobs in the cleaning industry was on a downward trend prior to the introduction of the National Minimum Wage in April 1999, and that this trend continued to December 2001. More recently, the number of employee jobs has levelled off and in the year to September 2004 there was an increase of around 10,000. Figure 3.15 shows that since March 2002 the number of full-time employee jobs has been rising, while the number of part-time jobs has been falling. Although over 60 per cent of employee jobs continue to be held by women, most full-time jobs are held by men. In the period September 2002–September 2004 the number of full-time jobs increased by over 45,000 (about 15,000 were held by men), while the number of part-time jobs fell by a similar amount (although the number held by men rose by over 10,000).

Figure 3.15

Employee Jobs in the Cleaning Sector, Thousands, 1998–2004



Source: ONS employee jobs series, 1998–2004, GB.

3.43 However, the ONS employee jobs series (which reflects jobs in cleaning companies) does not show the whole picture. A significant number of cleaners work directly in-house for companies in other sectors and therefore they will not be included in the employee jobs series. This is evident from the Labour Force Survey (LFS), which shows that the number of cleaning employees is considerably higher than the figure indicated using the ONS employee jobs series alone. The LFS recorded 610,000 employees in cleaning occupations in Summer 2004, but only 180,000 in the cleaning industry. In contrast to the employee jobs series, the LFS data indicate that the number of cleaning employees has increased by over 10,000 since the introduction of the minimum wage. Employers' representatives also report an increase. These divergent trends of cleaning company employees and the number of cleaners may suggest a trend towards bringing cleaning back in-house. Previously the trend was towards contracting out. Such an interpretation is supported by the CBI's evidence, which stated that more large companies were taking their business services back in-house and that there was some concern in the business services industry that smaller firms would follow suit. In contrast, the Business Services Association (BSA) said they saw no incentive for companies to take back outsourced services.

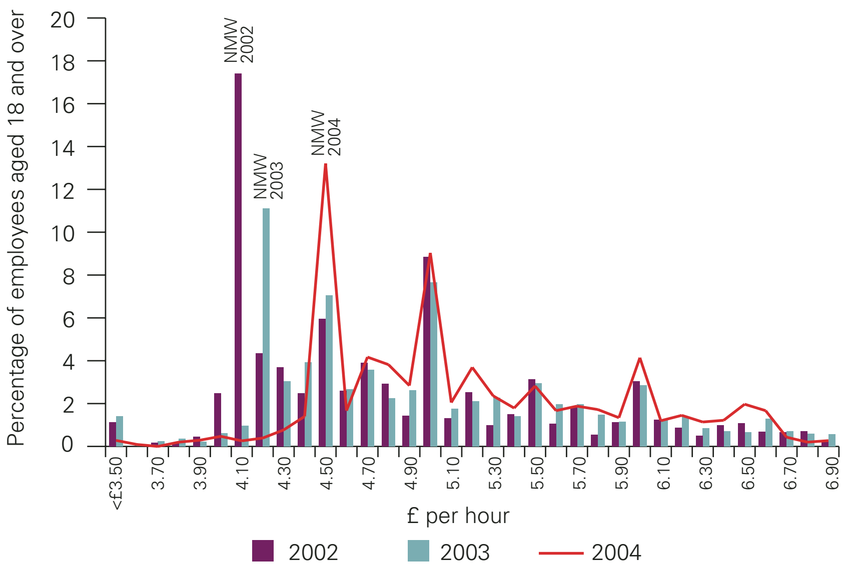
3.44 The Cleaning and Support Services Association (CSSA) estimates that there are even more people working in the cleaning sector. According to their reckoning, there are 850,000 people employed in cleaning and support services, of whom 400,000 are employed in the private sector. In addition, the CSSA estimates that 650,000 people work as domestic helpers in private houses, a number of them in a self-employed capacity. Data from the LFS suggest that in Summer 2004 there were over 50,000 self-employed in the cleaning sector. It is difficult to draw definitive conclusions in the face of such competing and overlapping data, but there does not seem to be any evidence of a significant fall in the number of cleaning jobs, and the number may even have increased since the minimum wage was introduced.

3.45 It can be seen from Figure 3.16 that the minimum wage has had a significant effect on the hourly earnings distribution for employees in the cleaning sector. The spikes in the distribution at the lower end reflect upratings of the adult minimum wage. However the proportion on the adult minimum wage fell to 13 per cent in April 2004, compared with 17 per cent in April 2002 following the sizeable October 2001 upratings. Thus while the minimum wage seems to be having an increased effect in retailing, its impact on cleaning sector wage rates (while still at a higher level than in retailing) is, if anything, reducing. This may indicate that the overall tight labour market is now a more important driver of cleaning sector wages than is the minimum wage. The cleaning sector makes little use of the youth Development Rate.

‘There is evidence that employers absorbed the costs of maintaining differentials for the first minimum wage increases but that subsequent minimum wage increases have put significant pressure on employers’ ability to fund these in recent years. This situation exacerbates the problems of supervisor recruitment and retention.’

CSSA evidence

Figure 3.16
Hourly Earnings Distribution for Employees Aged 18 and Over in the Cleaning Sector, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. NMW label shows the adult NMW rate in April of the given year.
2. Gross hourly earnings excluding overtime.

3.46 Employer organisations reported that squeezed pay differentials had become a significant issue for the industry as a result of the 2003 and 2004 minimum wage upratings. Companies were finding it difficult to maintain differentials and claimed they could not justify the same percentage increase for supervisors as for those on the minimum wage. Firms also reported union pressure to maintain differentials, although in general trade unions told us they had not pressed firms on this issue. In cases where clients were willing to fund the direct cost of minimum wage upratings, employers said that they were unlikely to fund the cost of maintaining pay differentials. Our own survey of employers found that respondents from the cleaning sector were the most likely to increase pay to maintain differentials with those at the minimum wage level.

3.47 Both the BSA and the CSSA continued to report that a key problem in the industry remained an unwillingness by clients to renegotiate long-term contracts (typically 3–5 years) to take account of minimum wage upratings. We commissioned Cronin and Thewlis (2004) to investigate firms' adjustments to the minimum wage, and firms in the cleaning sector reported that clients would generally rather renegotiate a reduced service than increase the price of a contract following minimum wage upratings. Even where prices had been increased or contracts renegotiated they generally did not cover the full costs of increases caused by the minimum wage and other legislation. A small number of employers said they were unable to pass on any increased costs.

3.48 Overall the cleaning sector is difficult to analyse because of the multiple sources of data. The balance of evidence suggests, however, that while the sector is significantly affected by the minimum wage, there has been no major fall in employment as a result of the minimum wage's introduction and upratings, and that if anything the sector is feeling less direct impact from the minimum wage than it did at the time of introduction.

Low Pay Commission Research

What we've noticed is that in those cases where we're dealing with contracts with clients, is that they don't object to a minimum wage but what they do is to ask us to observe the increase while it reduces the number of hours that we're putting into their contract.

South West cleaning/facilities company employing 123 staff.

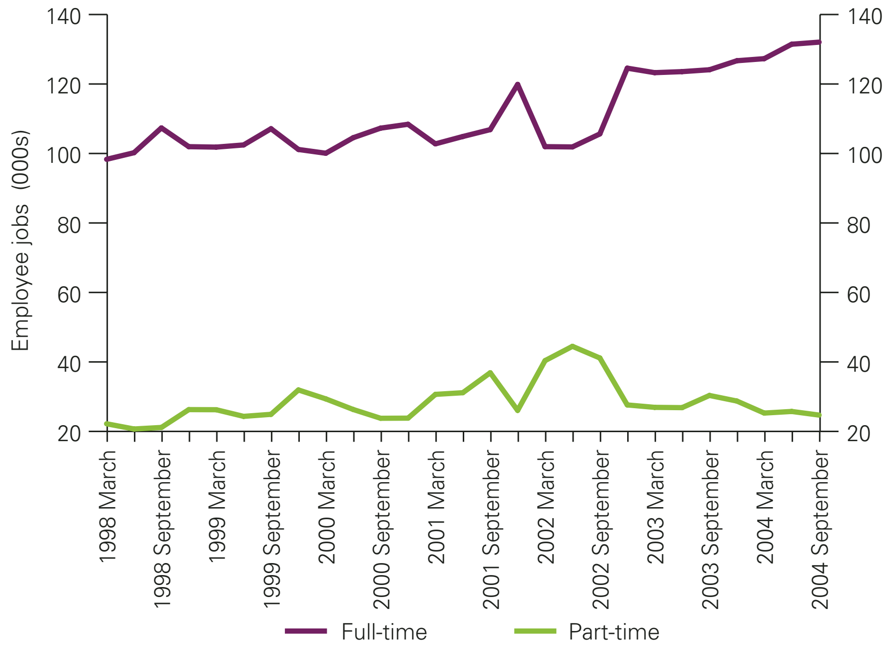
Cronin and Thewlis, 2004. *Qualitative Research on Firms' Adjustments to the Minimum Wage: Final Report to the Low Pay Commission*

Security

3.49 Since the introduction of the National Minimum Wage, the number of employee jobs in the security sector has increased by around 30,000, as shown in Figure 3.17. Indeed, a record number of employee jobs in security were recorded in June 2004. In contrast to the cleaning sector, men make up over three-quarters of the workforce and the vast majority of employees work full-time.

Figure 3.17

Employee Jobs in the Security Sector, Thousands, 1998–2004

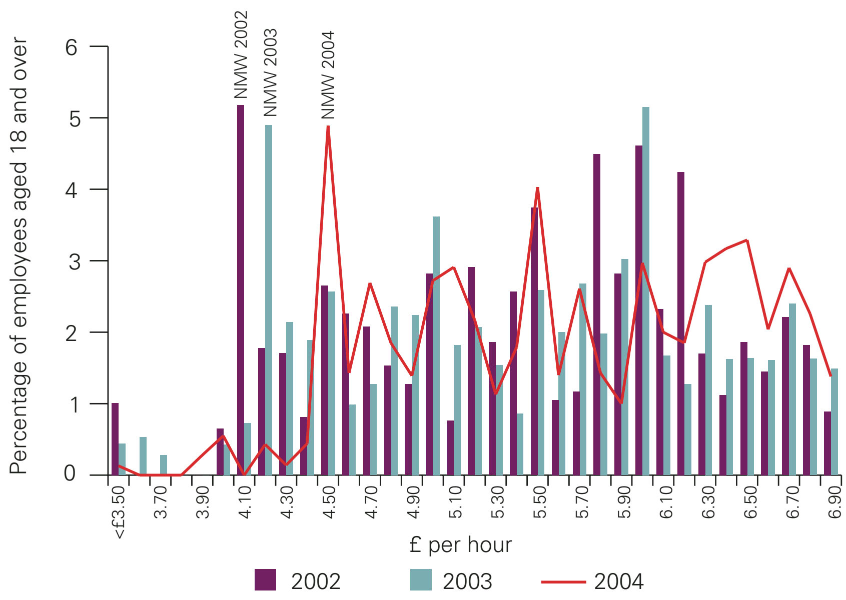


Source: ONS employee jobs series, 1998–2004, GB.

3.50 The adult minimum wage is the most common rate of pay in the security sector, as shown in Figure 3.18, but the percentage paid at the adult rate of the minimum wage in 2004 (about 5 per cent) is much less than in cleaning (13 per cent). And noticeably the percentage paid the minimum wage has declined slightly over the last three years. Lowest decile hourly earnings for security jobs remain above the minimum wage, although in 2003/04 lowest quartile hourly earnings also rose by over 7 per cent. This may reflect a move towards more high tech security provision in the sector and a demand for higher calibre staff, points highlighted during our consultation. As with the cleaning sector, little use is made of the youth Development Rate.

Figure 3.18

Hourly Earnings Distribution for Employees Aged 18 and Over in the Security Sector, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. NMW label shows the adult NMW rate in April of the given year.
2. Gross hourly earnings excluding overtime.

Low Pay Commission Research

Security companies reported gross hourly pay (where information was provided, across all ages) ranged from £4.50 to £6.15. Wages as percentage of costs were estimated as between 50 and 80 per cent.

Cronin and Thewlis, 2004. Qualitative Research on Firms' Adjustments to the Minimum Wage: Final Report to the Low Pay Commission

3.51 In the GMB's view, the minimum wage now forms the baseline for pay in the smaller security companies because their clients are not prepared to factor any further increases into the prices they are willing to pay. Smaller companies do not benefit from the economies of scale or negotiating power of the larger companies. The GMB also reported that low wages and long working hours are characteristic of the industry, with working hours of over 60 hours a week common in the manned guarding sector, often without any overtime premium. The union stated that larger (and unionised) firms, however, pay more and provide other benefits like pensions and higher annual leave entitlement.

3.52 As with the cleaning sector, business services representatives reported that many security companies operate under long-term contracts and face problems in planning for or passing on minimum wage increases to their clients. Labour costs are a significant proportion of total costs and therefore any changes to wage levels may be difficult to pass on. Cronin and Thewlis (2004) reported that when faced with increasing contract prices for security services, some companies responded by reducing their security requirements, with only a small minority accepting the increased minimum wage costs.

'A key problem is that companies are on long-term contracts and have difficulty in passing on minimum wage costs to clients.'

BSA evidence

3.53 Overall the security sector appears to be less affected by the minimum wage than it was at the time of initial introduction.

Childcare

3.54 The childcare sector continues to grow. According to the 2002/03 Childcare and Early Years Workforce Surveys (Department for Education and Skills (DfES), 2004a) the overall workforce (excluding childminders, who are often self-employed) grew by 2 per cent from 202,000 in 2001 to 206,000 in 2002/03. This was driven by the Government's policy of encouraging the expansion of the full daycare sector, thus enabling parents to take up employment, training or educational opportunities.

3.55 Jobs in childcare are distributed across several industries, such as education, health, social and welfare services. It is therefore not possible to use the ONS employee jobs series to identify workers in this sector. The LFS, however, can be used to identify childcare occupations. As shown in Figure 3.19, the LFS estimates that the number of nursery nurses – the childcare occupation most likely to be affected by the minimum wage – has been on an upward trend since Spring 1998. Most of the increase since Spring 2001 has been in the private sector.

Figure 3.19

Number of Nursery Nurse Employees, Thousands, 1998–2004

Source: LFS, 1998–2004.

Note: The classification of occupation in the LFS changed from SOC90 to SOC2000 in Spring 2001; thus direct comparisons between periods before and after should not be made.

3.56 The DfES surveys indicate that about half of full daycare and out of school clubs reported difficulties filling vacancies over the previous 12 months. The main reason was the general lack of applicants as well as a shortage of experience and qualifications. The National Day Nurseries Association told us that the sector has expanded rapidly due to Government initiatives such as Sure Start and there was a lack of experienced staff to feed the growth. The Government's Ten Year Strategy for Childcare (HM Treasury *et al.*, 2004a) announced a commitment to the recruitment and retention of enough workers to support the continuing growth of the sector, and a pay and workforce strategy is scheduled for publication in early 2005.

3.57 Given it is not possible to identify the childcare sector from ONS industry data, in previous reports we have looked at hourly earnings for employees in childcare occupations, i.e. workers in nurseries, playgroups, educational assistants and other childcare related occupations. Data on hourly earnings for all workers in childcare occupations suggest only a small percentage earn around the level of the minimum wage[1], but consultation and research commissioned from IDS highlighted that the minimum wage was having an increasing impact on private sector nurseries and that greater use was being made of age-related pay. We therefore focused our attention on pay for nursery nurses, using ONS occupational data.

3.58 As can be seen in Figure 3.20, the hourly earnings distribution for nursery nurses has shifted upwards in recent years to reflect minimum wage upratings. In April 2004, 4 per cent of all nursery nurses were paid around the adult rate of the National Minimum Wage and 9 per cent received below this rate. This is unchanged from the position in April 2002. But the figures were twice as high in the private sector, with 8 per cent paid around the adult rate and 18 per cent paid below this level.

1 According to ASHE, in April 2004 3 per cent of employees in childcare occupations were paid around the adult rate of the National Minimum Wage. Four per cent of employees were paid less than the adult rate in April 2004, unchanged from the position in April 2003.

Figure 3.20

Hourly Earnings Distribution for Nursery Nurses Aged 18 and Over, 2002–2004

Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. NMW label shows the adult NMW rate in April of the given year.
2. Gross hourly earnings excluding overtime.

3.59 The National Day Nurseries Association told us they viewed the level of pay as the biggest issue facing the sector. Research commissioned from IDS (2004b) found that nearly two-thirds of the 100 independent nurseries in its survey needed to raise their pay rates in order to comply with the October 2003 upratings of the minimum wage. This was significantly more than the 46 per cent of organisations who reported that they had needed to raise rates to comply with the October 2001 upratings (IDS, 2002). Some three-quarters of nurseries predicted that they would be affected by the October 2004 upratings.

3.60 The IDS survey (2004b) found some indications that, since October 2003, nurseries have sought to reduce the size of their workforce, or increase the proportion of unqualified staff. However a number of nurseries observed that they had no flexibility over staffing levels left as they were already operating at the minimum legally required ratios for the number of staff to children. Indeed, our survey found that, among firms affected by the October 2003 upratings, those in the childcare and social care sectors were the least likely to reduce staffing levels.

3.61 Nearly two-thirds of respondents to the IDS survey (2004b) reported that they had raised fees as a result of the increased costs from implementing the October 2003 upratings of the minimum wage. Several mentioned that the increase in fees had led to a drop in the number of children in their nursery and a couple said that they were concerned about the knock on effect this could have on staffing. Our survey found

Low Pay Commission Research

Just under three-fifths (57 per cent) of [private nurseries] said that the last increase in October 2003 had had a significant impact on their organisation.

IDS, 2004b. *Report to the Low Pay Commission on the Impact of the National Minimum Wage* that, among firms affected by the October 2003 upratings, those in the childcare sector were the most likely to have increased prices. Consultation supported the view that the significant upratings of the minimum wage have caused a corresponding increase in childcare fees and some expressed concern at the possibility of overpricing causing a reduction in the demand for childcare.

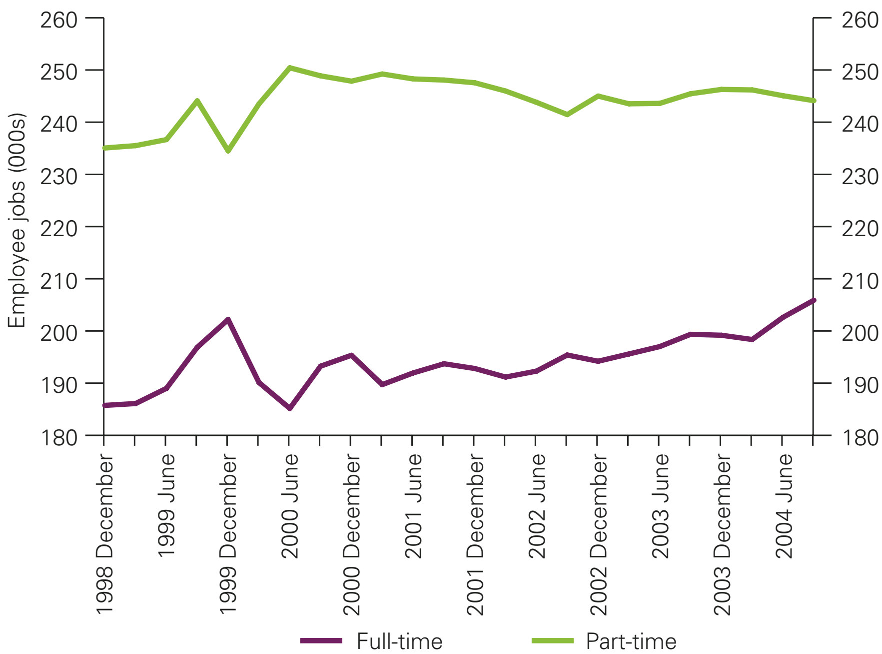
3.62 Overall the evidence on childcare suggests that the minimum wage plays a major role in setting wages within the industry, and that there are adjustment problems as the minimum wage is increased. But these problems are not preventing a robust expansion of this sector.

Social Care

3.63 According to Laing & Buisson (2004), in April 2004 there were an estimated 486,000 places in residential settings for long stay care of older and physically disabled people in the UK. Capacity has decreased by 9,600 since 2003 and by 64,900 since 1999. Laing & Buisson report that the capacity of the UK care home sector expanded up to the mid-1990s, but has since contracted, largely as a result of reforms in the public funding of community care. Occupancy rates have remained firmly above the 90 per cent level for the last four years as capacity shortages have become more common. As can be seen in Figure 3.21, the total number of jobs in the residential social care sector has been rising slowly since the introduction of the minimum wage, with a shift towards full-time jobs.

Figure 3.21

Employee Jobs in the Residential Social Care Sector, Thousands, 1998–2004



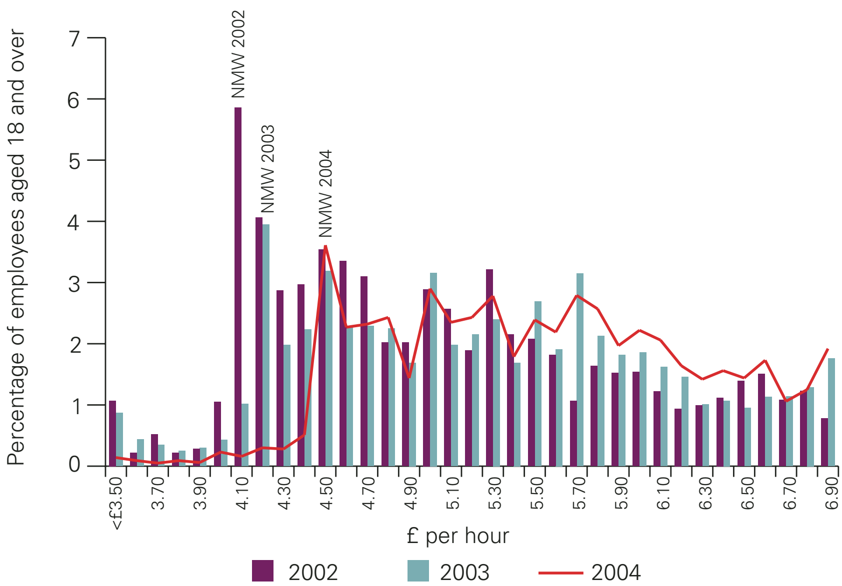
Source: ONS employee jobs series, 1998–2004, GB.

3.64 Laing & Buisson report that the number of home care hours funded by English local authorities has grown in every year but one (1998) since the community care reforms in 1993. They indicate that total contact hours increased by 4 per cent in the year to September 2003, although the number of households receiving home care has been on a downward trend, suggesting a more intensive service is being provided. A survey by the United Kingdom Home Care Association (UKHCA), however, found that total home care provision was little changed since 2000. Its findings suggest there has been a fall in the number of independent domiciliary care workers (97,500 in 2004 compared with 121,500 in 2000) but that each worker is estimated to work on average 25 per cent more hours than in 2000. A significant reduction of workers aged 50 or over was reported, apparently reflecting reluctance on the part of many to undertake further training and acquire additional qualifications.

3.65 The impact of the minimum wage on hourly earnings in the residential social care sector is shown in Figure 3.22. It can be seen that the proportion of employees paid the adult rate did not increase following the October 2003 uprating, remaining at 4 per cent between April 2003 and April 2004 and significantly below the 6 per cent seen in April 2002. This suggests that the impact of the minimum wage in this sector is reducing, with competition from employers in other low-paying sectors (e.g. retailing) now a more important determinant of wage rates.

Figure 3.22

Hourly Earnings Distribution for Employees Aged 18 and Over in the Residential Social Care Sector, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. NMW label shows the adult NMW rate in April of the given year.
2. Gross hourly earnings excluding overtime.

3.66 We have noted in previous reports that regulatory requirements and funding arrangements constrain the ability of the social care sector to respond to the minimum wage. Because minimum staffing ratios are established as a legal requirement, there are clear limits on the scope to reduce staffing levels. As noted earlier, this was borne out by our survey which found that, among firms affected by the October 2003 upratings, those in the social care and childcare sectors were least likely to reduce staff levels. In addition, social care providers are limited in their ability to increase prices due to their reliance on public funding.

3.67 We have recommended in previous reports that the Government should ensure that policies on commissioning care reflect the costs of provision. The Government's evidence reported that, 'between 1996/97 and 2003/04, funding was increased by about 22 per cent in real terms, an average of three per cent per annum. Resources will continue to increase, by an average of about six per cent per annum in real terms, until 2005/06.'

3.68 Evidence from employer organisations, case studies and our own survey, however, continues to highlight problems with public funding failing to meet the additional costs of the minimum wage in social care. The Independent Care Organisations Network (ICON) reported that there were winners and losers – not just between regions but also in terms of the type of care provided.

3.69 Laing (2004) reports that since 2002 'many local authorities facing capacity shortages have increased their fees by amounts in excess of ordinary inflation and a handful have increased their fees by substantial amounts. Despite the progress that is being made, there were still substantial gaps between fair fee rates and the weekly fees paid by social services in 2003/04.' Laing found that the majority of local authorities were willing to pay fees close to the rate appropriate for care homes which have not modernised, but in his view no local authority in England was paying fees appropriate for care homes which have invested in the more demanding physical standards set for 'new' homes first registered since April 2002.

3.70 In addition to some local authorities being unwilling to take full account of forthcoming upratings of the minimum wage, ICON also raised concern about funding the cost of travelling time. Workers must be paid the minimum wage for time spent travelling from one work assignment to the next (excluding rest breaks), but figures from the UKHCA indicated that up to two-thirds of workers were not being paid

'Continued NMW increases well above average earnings, combined with substantially lower increases in fees paid by government, will erode our margins and will make it extremely difficult to maintain differentials and impact our ability to recruit and retain staff, maintain employee motivation and reward career development.'

BUPA Care Services evidence

specifically for travel time, although some of these may receive payment by way of premiums for service user contact time. ICON told us that local authority prices are usually based on service user contact time only and the impact of the minimum wage and the Working Time Regulations has not been factored into prices. Furthermore, we were told that local authorities were increasingly inclined towards purchasing very short visits (15 minutes or less) making it even harder for social care providers to absorb the cost of travel time.

3.71 We recognise that the Government has increased funding for local authorities and note that many local authorities are raising fees to give greater recognition of the costs of provision. But the approach has been variable across the country and some problems remain. **We therefore recommend that the Government continue to make clear to local authorities that policies on commissioning care should reflect the costs of provision, including payment of travelling time. We also recommend that the Government monitor the approach of local authorities, examine the reasons for any uneven provision and, if appropriate, provide further guidance.**

3.72 In addition to the funding problems, consultation also highlighted a few sector specific issues relating to the minimum wage. The first was the application of the minimum wage to 'sleepovers'. 'Sleepovers' cover situations in which a worker is required to sleep on the premises and be available to deal with emergencies, but would not necessarily expect to be woken. In accordance with our previous recommendations, there is no requirement to pay the minimum wage for 'sleepovers', except for the time the worker is awake and expected to be available for work.

3.73 Our fourth report (2003) noted there was an element of uncertainty about the application of the minimum wage to 'sleepovers', resulting from some Employment Appeal Tribunal judgements which held that the minimum wage was payable for the whole period of work in circumstances where the worker was able to sleep at times during the night. We therefore recommended that the Government should examine whether the present uncertainty over the treatment of 'sleepovers' could best be resolved through revised guidance, or whether a change to the Regulations was required.

3.74 In May 2003 the Government published an insert to the *Detailed Guide to the National Minimum Wage* on the issue of 'sleepovers'. The guidance emphasised the need for the employment contract to set out clearly the period when the worker is permitted to sleep and for the employer to provide suitable sleeping facilities. The guidance notes that 'in cases where the employment contract does not specify any sleeping time, however, tribunals seem likely to conclude that the minimum wage should be paid for the full time when the worker is at work'. Consultation suggests that the additional guidance has helped clarify the treatment of sleepovers but that there needs to be greater awareness of the advice.

3.75 The second technical issue raised during consultation concerns on-call arrangements. At present the minimum wage is payable for hours spent on-call at or near the place of work (except for time entitled to be spent at home). Some on-call workers, however, do not have set hours or an annual salary and are deemed to perform 'unmeasured work', e.g. a home care worker may live with the client for a period of time. In these circumstances there should either be a 'daily average' agreement of hours to be worked or the minimum wage must be paid for every hour worked. The GMB expressed concern that the unmeasured work category is open to abuse, since workers may not have the bargaining power to negotiate agreements which are genuinely fair. The GMB and TUC suggested a need for further guidance on 'unmeasured work'. The Department of Trade and Industry's *Detailed Guide to the National Minimum Wage*, however, includes a detailed section on the rules although they may not be widely known about. There may therefore be a case for making the guidance more accessible. Awareness of the minimum wage is considered in Chapter 6.

3.76 ICON also highlighted potential non-compliance with the minimum wage resulting from the Department of Health's initiative enabling social care users to obtain a 'direct payment' to be used to buy services for themselves to meet their social care needs. One option is for the recipient to use the money to employ their own staff and ICON is concerned that people may be unaware of their legal obligations. The Department of Health's *Guide to Receiving Direct Payments From Your Local Council* states, however, that 'if you plan to employ staff, you will need to show that you will meet your legal requirements as an employer' and highlights the need to ensure compliance with the minimum wage. We will keep the issue under review and are grateful to ICON for alerting us to this potential problem.

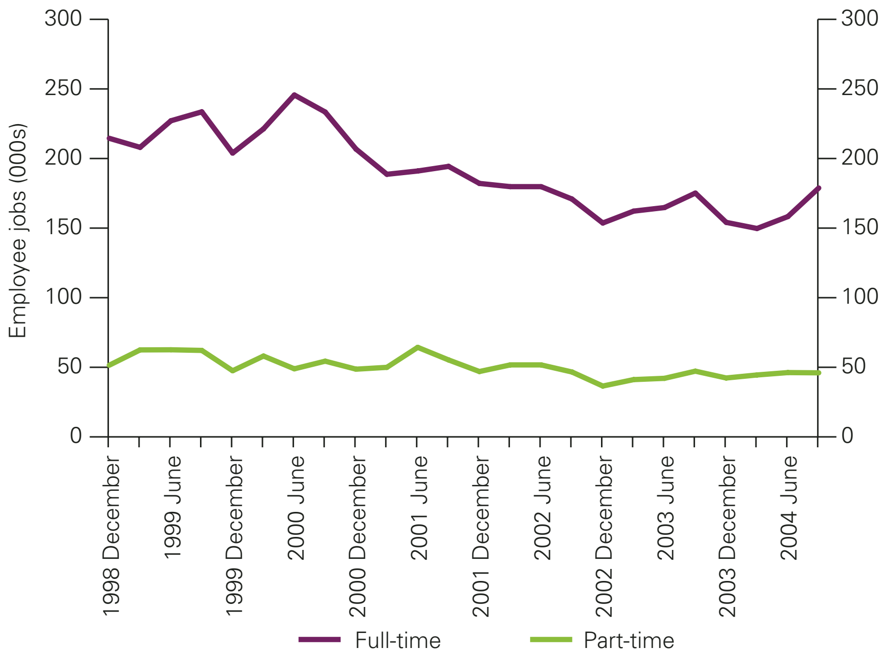
3.77 Overall the social care sector remains one where the minimum wage has a significant effect, and where a number of technical issues create complexity and need to be kept under review. It is also one where the role of local authorities as purchasers of care is crucial, and where society needs to be willing to provide the additional resources required if workers' wages are to rise. But the impact of the minimum wage on the economics of the sector has not increased over recent years: if anything it seems to have diminished slightly.

Agriculture

3.78 While we have seen stable or growing employment in many of the low-paying sectors since the minimum wage was introduced, the decline in employment in agriculture, which has been evident for many decades, has continued. As shown in Figure 3.23, there were 225,000 employee jobs in the sector in September 2004, a fall of 71,000 compared with September 1999. The position has, however, been more stable over the last two years. According to the Department for Environment, Food and Rural Affairs (Defra, 2005b) there were 192,000 agricultural workers in the UK in June 2004 and the total labour force (including farmers, spouses, partners and directors) numbered 546,000.

Figure 3.23

Employee Jobs in the Agriculture Sector, Thousands, 1998–2004



Source: ONS employee jobs series 1998–2004, GB.

3.79 The agricultural sector is unique in that statutory minimum rates for different categories of worker are set by the respective Agricultural Wages Boards (AWB) for England and Wales, Scotland, and Northern Ireland. These cannot be set below the National Minimum Wage. Adult rates apply from the age of 19 and the Boards also determine some other conditions of employment, such as overtime rates and sick pay. The National Minimum Wage has had a direct influence on the lowest agricultural minimum rates in England, Wales and Scotland, and in recent years they have been set at the same level. Accordingly, the Manual Harvest Worker rate used in England and Wales (which may be paid to those employed to undertake manual harvesting tasks only, for a maximum of 30 weeks per 12 month period) and the casual rate used in Scotland (which may be paid for the first ten weeks of employment only) rose to £4.85 for workers aged 19 and above in October 2004. However in Northern Ireland there is a single rate for all agricultural workers, which rose to £5.09 per hour in April 2004.

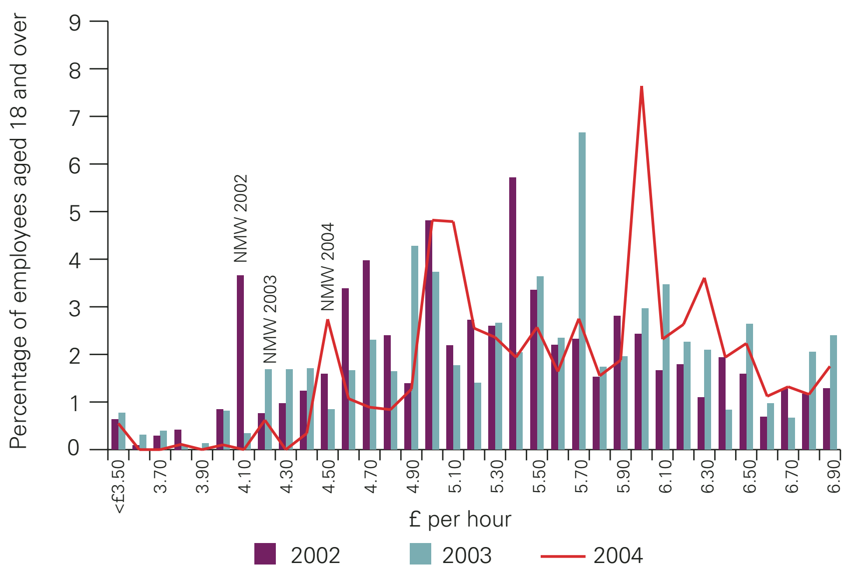
‘Changes to the NMW have been the key driver of the wage rates set by the Agricultural Wages Board.’

National Farmers’ Union evidence

3.80 The hourly earnings distribution (Figure 3.24) shows that a significant proportion of the agricultural workforce is paid at rates well above the National Minimum Wage (and the equivalent AWB rate). This reflects the range of higher statutory minimum rates in place within the agricultural sector, which must be paid to non-seasonal workers and to those with particular qualifications or experience. For example, in England and Wales the minimum rate in April 2004 for those not employed on a seasonal basis was £5.15 per hour (the Standard Worker rate) and the Craft Grade minimum rate was £6.02 per hour.

Figure 3.24

Hourly Earnings Distribution for Employees Aged 18 and Over in the Agriculture Sector, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. NMW label shows the adult NMW rate in April of the given year.
2. Gross hourly earnings excluding overtime.

3.81 According to ASHE 2004a (not shown), only 6 per cent of agricultural workers earned at or below the adult rate of the National Minimum Wage in April 2004. However, it is possible that this April survey does not capture many of the casual or seasonal workers who are employed later in the year to cover the harvest period only. Defra (2005b) records that in June 2004 there were 69,000 seasonal or casual workers in agriculture (36 per cent of all workers) although this figure may again underestimate the total number of non-permanent workers employed over the course of a year.

3.82 The National Farmers' Union (NFU) told us that the significant increases in the lowest agricultural minimum rates, as a direct result of National Minimum Wage upratings, have had a considerable impact on those sectors where the labour requirement (and thus labour costs) is greatest and where the seasonal workforce is concentrated. This includes horticulture (for example fruit and vegetable picking) and general cropping. According to Defra (2005a) 58 per cent (26,000) of the total non-permanent workforce in England in June 2003 were concentrated in these two sectors. Seasonal and casual workers are most likely to be paid at an AWB rate equivalent to the National Minimum Wage and are thus directly affected by minimum wage upratings. Some are likely to be overseas workers, including those who have obtained a permit enabling them to work during the harvest period under the Seasonal Agricultural Workers Scheme. During a Commission visit to Cambridgeshire, we found that local farmers and suppliers were unable to recruit unskilled labour from the local area due to competition from other industries. As a result, a substantial proportion of the casual workforce originated from Eastern Europe, particularly Poland and Lithuania.

3.83 The agricultural sector, and in particular horticulture, also faces significant international competition, as well as pressure from major food retailers and caterers to reduce output prices. Our Cambridgeshire visit demonstrated that some farmers and suppliers had responded to this pressure by creating efficiencies through specialisation and large-scale production of fruit and vegetables. They had also invested in technology to improve the quality of produce and consistency of supply. The CBI's submission also commented that increased competition in horticulture had driven business to other parts of Europe with lower wage costs.

3.84 The NFU reported that the National Minimum Wage had driven increases in all of the AWB minimum rates in place in England and Wales, because of the focus on differentials during the Board's negotiations. Although there has been some compression at the lower end, the percentage differences between the Standard Worker and Craft and Appointment Grades, which have historically been in place, have been maintained. During our visit to Cambridgeshire, one of the farmers we spoke to identified as a serious deficiency the absence of a provision in the Agricultural Minimum Wage legislation to enable employers to reach fair piece rate agreements with their workers. It was suggested that farmers would welcome a change to the Agricultural Wages Act 1948 to mirror the new provisions on fair piece rates introduced under the National Minimum Wage legislation.

3.85 It is difficult to assess the impact of the National Minimum Wage within the agricultural sector. Employment has been falling since long before the introduction of the National Minimum Wage and we received conflicting evidence about whether the minimum wage had any contributory role in accelerating this decline. The vast majority of workers in the sector earn significantly more than the National Minimum Wage, indicating that its direct impact is small. But this direct impact is likely to fall disproportionately on certain sectors such as horticulture. The minimum wage also has a strong influence on the higher statutory minimum rates set by the Agricultural Wages Boards.

Textiles, Clothing and Footwear

3.86 The textiles, clothing and footwear industries continue to contract as a result of increasing competition from low-wage economies and the transfer of high volume manufacturing capacity offshore, a process that started well before the introduction of the minimum wage.

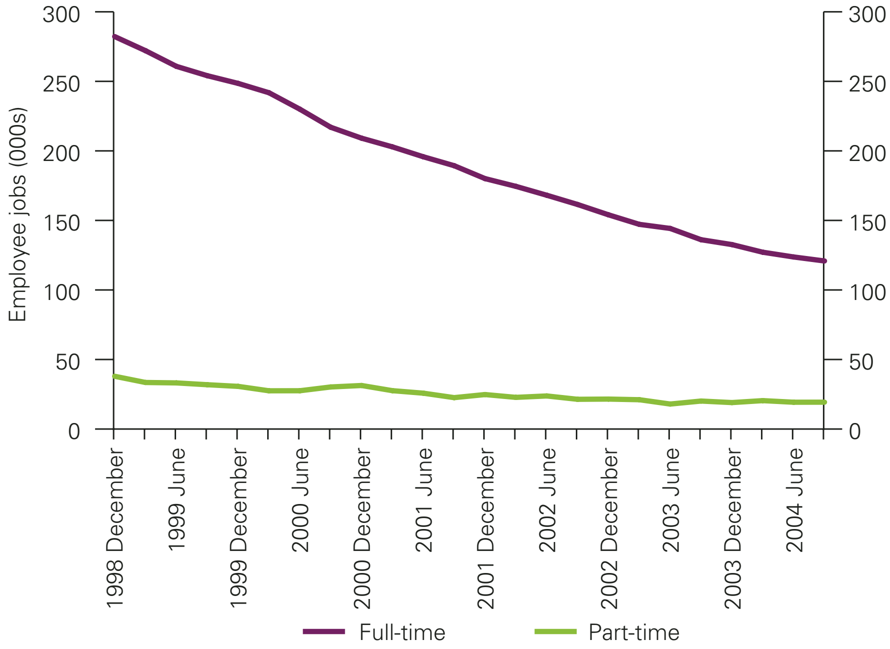
3.87 Low cost imports have resulted in continuing price deflation on the high street, with UK companies unable to remain competitive in traditional volume areas of the market. Many UK companies are now focusing on high value, niche markets. This decline in output is reflected in the sharp reduction in the number of employee jobs in the textiles, clothing and footwear sectors. As shown in Figure 3.25, the number of jobs stood at 140,000 in September 2004, down by over a half since the introduction of the minimum wage. Nearly 200,000 jobs have been lost in these three industries since March 1998. Even in the last two years the number of jobs has fallen by nearly a quarter. The reduction in the number of full-time employee jobs mirrors the general fall in jobs, while the number of part-time jobs also declined rapidly from March 1998 to March 2002, but has since remained steady.

‘Some companies have sought to address the decline through new technology and changes in their customer base, but these measures take a number of years to come to fruition.’

British Apparel & Textile Confederation

Figure 3.25

Employee Jobs in the Textiles, Clothing and Footwear Sector, Thousands, 1998–2004

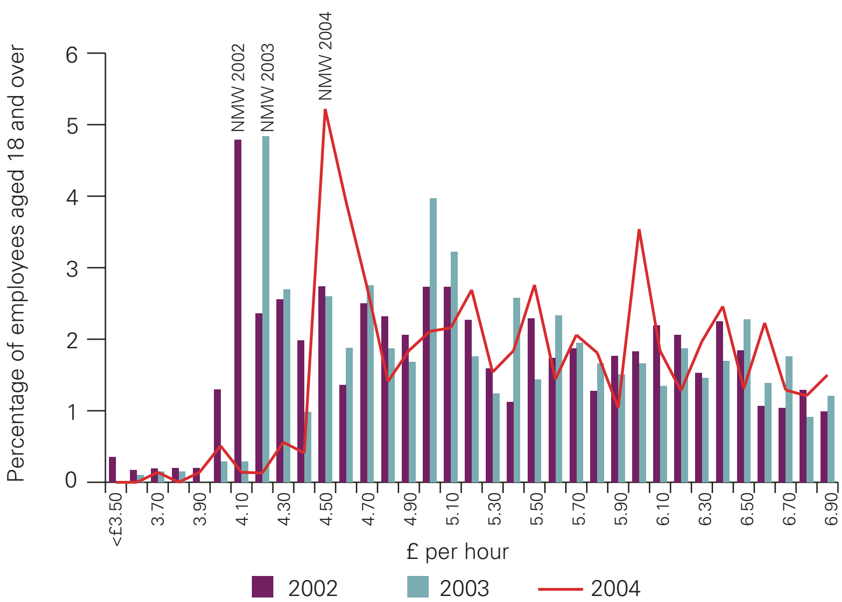


Source: ONS employee jobs series, 1998–2004, GB.

3.88 The National Minimum Wage continues to have an important role in setting wage rates in the textiles, clothing and footwear sector. This is clearly evident in Figure 3.26, with the main spikes reflecting the adult minimum wage rates. According to ASHE 2004a (not shown), 5 per cent of the workforce in these sectors earned the adult rate of the minimum wage in April 2004. A further 7 per cent earned between the minimum wage and £4.85.

Figure 3.26

Hourly Earnings Distribution for Employees Aged 18 and Over in the Textiles, Clothing and Footwear Sector, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.

Notes:

1. NMW label shows the adult NMW rate in April of the given year.
2. Gross hourly earnings excluding overtime.

3.89 The extent to which the minimum wage is accelerating the decline in the sector, if at all, is not known. The British Apparel & Textiles Confederation accepts that the main reason for decline lies elsewhere but considers that the minimum wage is a contributory factor. This view is supported by the CBI, which reports that the textiles industry has been significantly affected by the minimum wage, with companies finding it increasingly difficult to maintain margins due to increased cost pressures in the UK, combined with competition from abroad. However, this view is not shared by Community, the GMB or the TUC, all of whom regard globalisation as overwhelmingly responsible for the loss of jobs in the sector.

3.90 Written and oral evidence from employer and worker organisations describes companies making a variety of adjustments to address the decline in the sector and the impact of the minimum wage. These include the introduction of new technologies and changes in customer base that have led to improved productivity and efficiencies. Our own employers' survey found that textiles and clothing companies were the least likely to regard themselves as experiencing any benefit from the minimum wage.

3.91 Traditionally these sectors make particular use of incentive pay systems. In oral evidence, employers' representatives reported that recent increases in the minimum wage have had a negative impact on incentive pay systems, with a higher proportion of piece rate workers now being affected than when the minimum wage was first introduced. They argued this had reduced the incentive to be productive, with more capable workers unable to earn much more than those who are less efficient. However, workers' representatives and others took a different view and reported that many employers had successfully addressed this problem through multi-skilling frameworks which had reduced the number of low-skilled jobs.

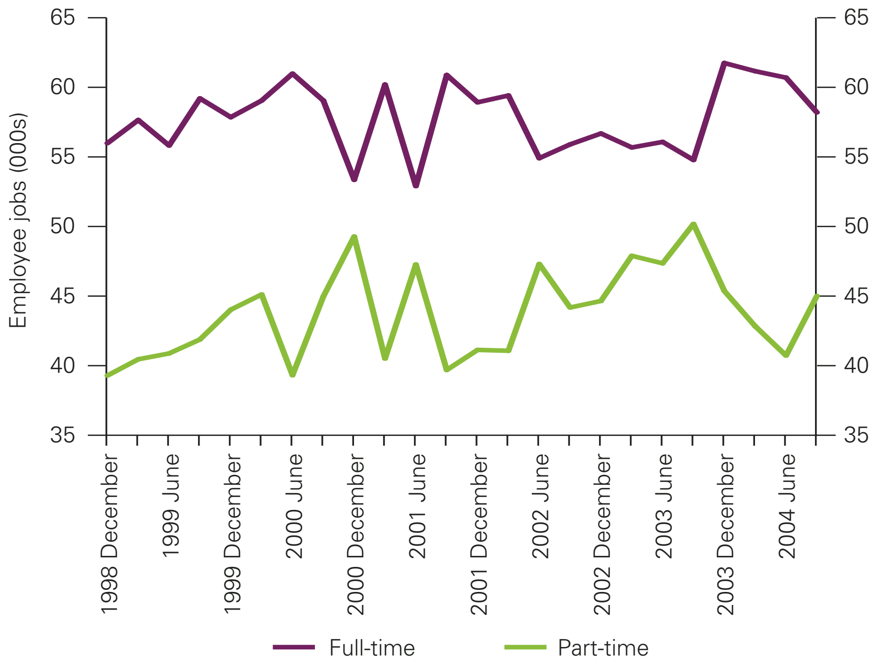
3.92 Our overall assessment of the textiles, clothing and footwear sectors is that while the minimum wage clearly has an impact on some wage rates within these sectors, and may have played a subsidiary role in speeding employment decline, the dominant factor has been external competition. Competition from low-wage economies is likely to continue to reduce employment levels in this sector until a floor is reached, leaving a UK industry that is concentrated on high value, niche products, rather than on an ability to compete on labour costs.

Hairdressing

3.93 Official ONS data are not available on the turnover or gross value added of the hairdressing sector, although the National Hairdressers' Federation (NHF) and the Hairdressing Employers Association (HEA) believe the sector to be growing. The number of employee jobs in the hairdressing sector has remained largely unchanged at just over 100,000 in the two years to September 2004, as demonstrated in Figure 3.27. However, as noted earlier in this Chapter, there has been a noticeable rise in the level of self-employed hairdressers. In Summer 2004 there were 101,000 self-employed hairdressers, compared with 95,000 in Summer 2002 and 83,000 in Spring 1998. Moreover, the trade associations calculate that the informal economy could account for as many as a further 35,000 hairdressers.

Figure 3.27

Employee Jobs in the Hairdressing Sector, Thousands, 1998–2004

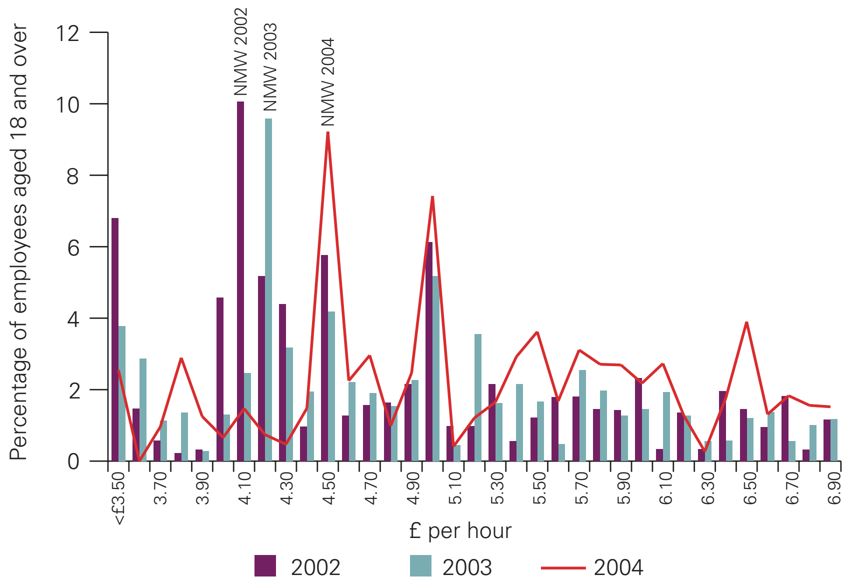


Source: ONS employee jobs series, 1998–2004, GB.

3.94 Figure 3.28 illustrates that the minimum wage continues to have an impact on the hairdressing sector, with a clear spike in the hourly earnings distribution at the adult minimum wage of £4.50 per hour in April 2004. There is a further large spike at £5.00 per hour. According to ASHE 2004a (not shown), 8 per cent of employees aged 18 and over were paid the adult rate in April 2004, and around 13 per cent of employees were paid less than £4.50 per hour. The relatively high percentage of employees paid below the adult minimum wage is consistent with our findings in previous reports and demonstrates the use of the youth Development Rate and the exemptions for apprentices.

Figure 3.28

Hourly Earnings Distribution for Employees Aged 18 and Over in the Hairdressing Sector, 2002–2004



Source: ASHE, April 2002–2004 without supplementary information.
Notes:
1. NMW label shows the adult NMW rate in April of the given year.
2. Gross hourly earnings excluding overtime.

3.95 As identified in previous reports, the biggest issue facing the hairdressing sector continues to be the impact of the minimum wage on training. Although recruitment of both skilled staff and trainees remains difficult in some areas, the NHF and HEA wrote that the vast majority of small salons remain reluctant to employ trainees above the age of 17 because of cost. They emphasised the additional costs of funding training and said that, although trainees could obtain a National Vocational Qualification level 2 within two years, they would be unlikely to have built-up a client base to contribute to the economy of the salon in less than three years. Training opportunities for older workers were severely limited. The NHF and HEA therefore proposed that all workers should be exempt from the minimum wage for the duration of the apprenticeship or accredited training. We consider the treatment of young people and trainees in Chapter 5.

3.96 The NHF and HEA also suggested that changes in the minimum wage commence on a Sunday or Monday. They argued that most people on the minimum wage were paid weekly and that needless administration problems were caused from paying workers different rates during the week that the new rate took effect. We believe that no change is necessary and note that the Regulations implementing upratings include a transitional provision making clear that the provisions do not apply to any pay reference period beginning before 1 October.

‘For smaller or marginal businesses ... more firms now believe that it is probably more cost efficient to entice trained personnel from other employers.... On completion of the training programme in hairdressing employees require a further period of time to gain experience, establish a commercial working speed, and develop a client base.’

NHF and HEA evidence

Conclusion

3.97 The minimum wage appears to have bedded down in a number of the sectors where it was formerly seen as a cause of grave concern: while still significant, its impact on the cleaning, social care and security sectors seems if anything to have reduced slightly. Our consultation and research also suggest that it is no longer such a significant problem for a majority of small firms. We note, however, that some larger firms, particularly in the retail sector, are becoming more concerned about the impact of recent upratings, and in particular the October 2004 increase to £4.85. Maintaining pay differentials is a common issue across many of the nine low-paying sectors we examined. Overall, we conclude that the October 2003 upratings have been absorbed without negative impact on employment and that, in general, firms have adjusted well to the upratings. There is currently only limited data available relating to the October 2004 upratings.

3.98 A potential conflict between salary sacrifice schemes and the National Minimum Wage was brought to our attention during consultation and in October 2004 the Government asked us to advise whether childcare vouchers should be allowed to count towards minimum wage pay. Salary sacrifice arrangements can be complex and cover a range of staff benefits in addition to childcare, and we believe a number of important factors need to be weighed very carefully before a conclusion can be reached. We recommend that the Government ask us to review the issue of salary sacrifice in depth and to report by February 2006.

3.99 Concerns remain about funding in the social care sector. We recognise the progress that has been made on funding in relation to the minimum wage, but the approach by local authorities has been variable across the country. We therefore recommend that the Government continue to make clear to local authorities that policies on commissioning care should reflect the costs of provision. We also recommend that the Government actively monitor the approach taken by local authorities to the funding of social care. A further area of concern is the lack of understanding of the application of the minimum wage to 'sleepovers' and on-call arrangements. We believe this could be successfully addressed by more targeted publicity.

3.100 The provision of accommodation to some employees is most common in two of the low-paying sectors: hospitality and agriculture. We have considered the evidence submitted regarding the level of the maximum daily accommodation offset and recommended an increase in line with the adult rate.

3.101 In this Chapter we considered the impact of the minimum wage on the low-paying sectors. Some of these sectors are characterised by employing particular groups of workers, for example the overwhelming majority of nursery nurses are female, most of the employees in the security sector are male and the hairdressing sector employs a significant number of young trainees. In Chapter 4 we look specifically at groups of workers who are likely to be more affected by the minimum wage.

Groups of Workers and Specific Enforcement Issues

Women, ethnic minority and disabled workers are disproportionately represented among the beneficiaries of the minimum wage. Two-thirds of the beneficiaries of the 2004 upratings are estimated to be women workers.

We found clear evidence suggesting that the minimum wage has had a major impact in narrowing the gap between the pay of women workers and that of men at the lower end of the earnings distribution. Although still significant, the gender pay gap has also been narrowing slowly for some time in the middle range of the pay distribution independently of any influence of the minimum wage. The minimum wage has now had such a marked effect at the bottom of the distribution that only a very large uprating in relation to average earnings would have much further effect.

Upratings of the minimum wage have also helped to raise the wages of disadvantaged workers, particularly those with work-limiting disabilities, without harming their employment opportunities. In common with the rest of the labour market, the employment situation of disadvantaged groups has improved in recent years. Indeed, in many respects, those groups whose position in the labour market was weakest have demonstrated the greatest gains in employment.

The pattern of pay by ethnic group is complex. Although some minority ethnic groups suffer a pay penalty compared with the white majority, others do not. Indeed, some men from minority ethnic groups tend to earn more than their white counterparts and black women earn more on average than white women. However, some minority ethnic groups (such as those originating from Bangladesh and Pakistan) continue to earn considerably less than the average. The minimum wage has improved the position of these disadvantaged ethnic groups without adverse employment effects. Indeed employment rates of disadvantaged ethnic groups, though lower than those of white workers, are increasing.

The analysis in this Chapter also reveals the poor position of part-time workers relative to full-time workers. Part-time work is more commonly available in low-paying occupations. While female full-time workers have made significant progress in closing the earnings gap with male full-time workers, the same is not as true of female part-time workers. However, there is no gap between the earnings of female part-time workers and male part-time workers over most of the distribution. This suggests that while the labour market for full-time workers has strengthened, the pay and conditions of both male and female part-time workers has trailed behind.

Homeworkers are a largely hidden workforce. It is estimated that there may be up to one million of them, of whom 90 per cent are probably women, many of them from minority ethnic groups. These workers face particular difficulties in enforcing their rights to the minimum wage. We believe that the new system of fair piece rates, which replaced the fair estimate agreement system, will help improve the situation of homeworkers. However, we continue to believe that this is an important area for enforcement activity. We would welcome any steps taken by the Government to heighten awareness of the minimum wage among these vulnerable workers.

We continue to believe that people with disabilities should be entitled to the minimum wage and recognise that the Government's revised guidance since the publication of our fourth report (2003) has helped resolve many of the uncertainties about entitlement to the minimum wage. But we wish to highlight the fact that minimum wage upratings can result in some disabled people reducing the number of hours they spend in paid employment to avoid breaching the £20.00 per week earnings disregard. We would encourage the Government to take this into account as part of its efforts to increase work incentives for those with disabilities.

Some voluntary sector organisations have pointed to a lack of clarity about the position of volunteers. We recommend that the Government should review and draw together existing guidance into a single source to provide clear and accessible advice to the voluntary sector.

Introduction

4.1 We were asked in our terms of reference to take account of the impact of the minimum wage on different groups of workers, and to be mindful when making new recommendations of the likely impact on these groups, especially on those most disadvantaged in the labour market.

This Chapter focuses on outcomes in terms of pay and employment by gender, disability, and ethnicity, and on the interaction of these outcomes with the minimum wage. We also examine the position of volunteers, homeworkers and therapeutic workers. Another vulnerable group of workers – young people – is considered separately in Chapter 5.

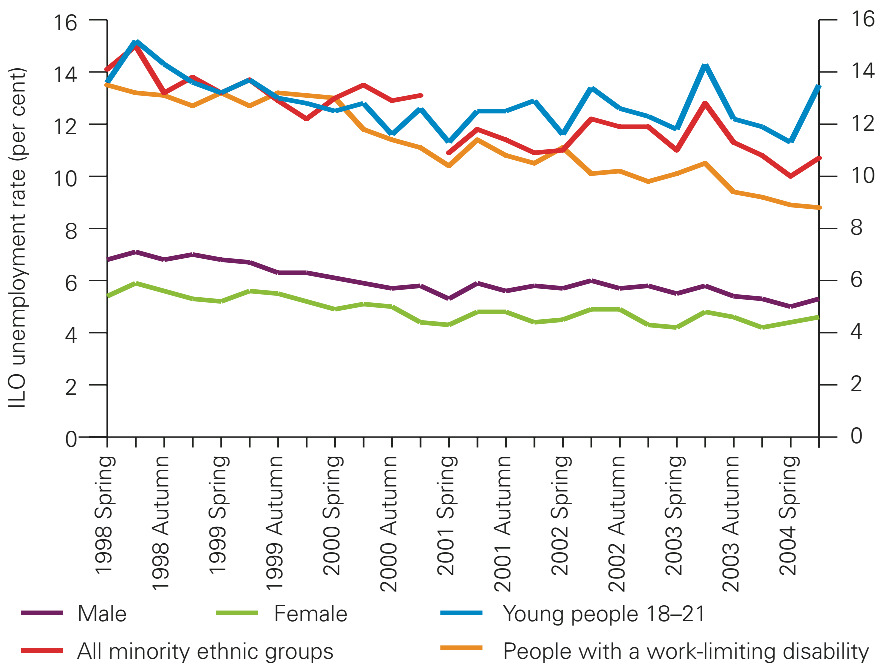
4.2 We were also asked to look at the impact of the minimum wage on the gender pay gap and the earnings of different ethnic groups and the disabled. The quality of data available to study the gender pay gap is superior to that available for studying the impact on the disabled and ethnic groups. Nevertheless, we are able to make some general comments on the pay and employment of minority ethnic groups and the disabled.

Employment, Unemployment and Inactivity

4.3 When the minimum wage was first introduced there was concern that it would lead to an increase in the level and rate of unemployment, particularly for those groups most likely to be low-paid. These fears have not materialised. The unemployment rate for all these groups – women, those with work-limiting disabilities and minority ethnic groups – has fallen since the introduction of the minimum wage in Spring 1999 as shown in Figure 4.1.

Figure 4.1

Working Age Unemployment Rates of Various Groups, 1998–2004



Source: Labour Force Survey (LFS), 1998–2004.

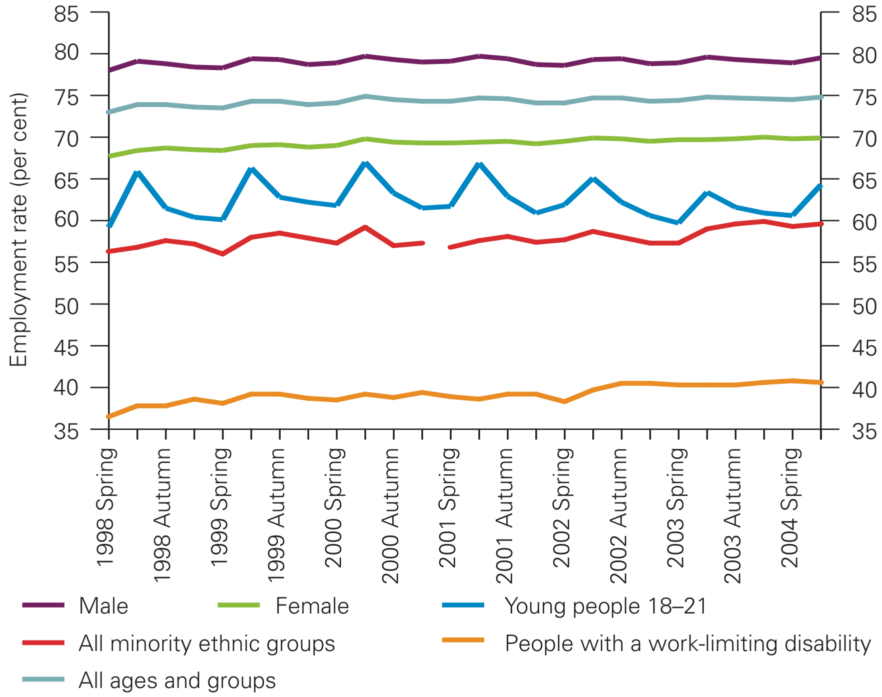
Notes:

1. The definition of ethnic groups in the LFS changed in Spring 2001 to be consistent with the 2001 Census classifications; thus direct comparisons between the periods before and after should not be made.

4.4 Because the unemployment rate has been so low, the focus more recently has turned to employment rather than unemployment. Working age employment rates of various groups are shown in Figure 4.2. It also paints an encouraging picture for those groups most affected by the minimum wage. There is no evidence to suggest a harmful effect of the minimum wage on the employment rates of these groups.

Figure 4.2

Working Age Employment Rates of Various Groups, 1998–2004



Source: LFS, 1998–2004.

Notes:

1. The definition of ethnic groups in the LFS changed in Spring 2001 to be consistent with the 2001 Census classifications; thus direct comparisons between the periods before and after should not be made.

4.5 Important features of the labour market in the last 20 to 30 years have been the increased participation of women and an increase in the inactivity rate for men. Table 4.1 shows inactivity rates and confirms the increasing labour market attachment of women and non-white minority ethnic groups since the introduction of the minimum wage. However, the falls in inactivity rates in the late 1990s and into the early 2000s have levelled off and there are now initial signs that inactivity rates may have started to rise.

Table 4.1 Working Age Inactivity Rates, 1998–2004

Inactivity rates	Female	Disabled	Non-white ethnic groups	Male
Spring 1998	28.4	57.8	34.9	16.3
Spring 2000	27.5	55.8	34.6	15.9
Spring 2002	27.3	56.9	35.2	16.7
Summer 2003	26.8	55.0	32.3	15.5
Spring 2004	27.0	55.2	34.1	16.9
Summer 2004	26.8	55.5	33.3	16.0

Source: LFS, 1998–2004.
Note: The definition of ethnic groups in the LFS changed in Spring 2001 to be consistent with the 2001 Census classifications; thus direct comparisons between the periods before and after should not be made.

Labour Market Outcomes by Gender

Employment

4.6 Although women have traditionally had lower unemployment rates than men, they have also had lower labour force participation rates. Since the introduction of the minimum wage, the female unemployment rate has been consistently lower than that for males, as shown in Figure 4.1. Prior to the introduction of the minimum wage in 1999, the unemployment rate for men in 1998 was 6.8 per cent, but by the Summer of 2004 it had fallen to 5.3 per cent. By contrast, the unemployment rate for women in Summer 2004 was 4.6 per cent versus a rate of 5.4 per cent just prior to the introduction of the National Minimum Wage.

4.7 Further evidence of a strengthening position of women in the labour market can be gleaned from Figure 4.2 which shows that the employment rate of women increased by around two percentage points from Spring 1998 to just under 70 per cent in Summer 2000 and has remained at this higher level since then. This contrasts with an employment rate for working age men in the Autumn of 2004 of 79.3 per cent.

4.8 Nevertheless, a high percentage of women continue to work part-time at some stage of their working lives. In any given year almost half of women workers work part-time (43 per cent in Autumn 2004). The consequence of this for the pay and earnings of women is explored below.

Gender Pay Gap

4.9 While the minimum wage appears not to have harmed the job prospects of women, it has had a major beneficial influence on the aggregate earnings of women. As estimated in Chapter 2, two-thirds of the estimated beneficiaries of the 2004 upratings of the minimum wage are women workers. Of these beneficiaries, a large number are part-time workers. Indeed, around half of the beneficiaries of the minimum wage are women part-time workers.

4.10 While women continue to earn less than men on almost all relevant measures, the gender pay gap has been closing gradually for some time, even prior to the advent of the National Minimum Wage. In a report for the Women and Equality Unit, Anderson *et al.* (2001) found that the mean full-time hourly earnings of women rose from 64 per cent of men's in 1973 to 82 per cent in 2000. However, the pace of improvement over this period has been far from steady. The gap narrowed and the ratio increased quite dramatically in the early years, from 66 per cent in 1974 to 74 per cent in 1976, a move that was probably precipitated by the passage of the Equal Pay Act of 1970. It then stabilised before rising, albeit at a slower rate, from 1987 onwards.

‘The minimum wage has been an effective instrument for ensuring equality at the low paid end of the labour market’

TUC evidence

4.11 The issue to be considered here, therefore, is whether the introduction and upratings of the minimum wage have produced any additional narrowing of the pay gap, above and beyond the rate implied by the long-term trend.

4.12 The size of the gender pay gap and the conclusions drawn about it depend greatly on how it is measured. Men spend more hours in (paid) employment per annum than women, so the pay gap derived from a measure of annual earnings is larger than that for monthly earnings, which in turn is larger than that for hourly pay. For instance, the April 2004 Annual Survey of Hours and Earnings (ASHE) survey showed median annual earnings of women (all employee jobs) as amounting to only 57 per cent of men's equivalent median annual earnings.

4.13 Researchers instead usually focus on the hourly wage rate but there remain complexities to be considered. The pay gap between the hourly earnings (excluding overtime pay) of all men workers and all women workers as derived from the Annual Survey of Hours and Earnings (ASHE) data for April 2004 is 25 per cent, i.e. the ratio of the median earnings of all women to the median earnings of all men was 75 per cent. However, as discussed below, the circumstances of part-time and full-time workers vary quite substantially, and it is probably not optimal for the purposes of analysis to group them all together. We also separate out workers aged 18–21 (those entitled to the youth Development Rate) from adult workers entitled to at least the full National Minimum Wage. Hence, for the rest of this section on gender differences in pay, part-time and full-time workers are considered separately, as well as those aged 18–21 and those aged 22 and above.

4.14 Differences in hourly pay can be used to illustrate the pay gap between the hourly pay of male full-time and female full-time workers, as well as the gap between female part-time workers and male part-time workers. As there are relatively few men working part-time – men make up 19 per cent of part-time workers and only 9 per cent of men in employment work part-time – most researchers in this area focus on the gap between the pay of female part-time workers and male full-time workers. The data in Tables 4.2 and 4.3 show differences along all these lines based on average hourly pay for these various categories of worker.

Table 4.2 Hourly Earnings of Men Working Full-time and Women Working Full-time and the Gender Pay Ratio, 1998–2004

	Gross hourly earnings (excluding overtime)					
	£ Men		£ Women		Ratio of women/men	
Year	Median	Mean	Median	Mean	Median	Mean
1998[1]	8.74	10.65	7.22	8.39	82.6	78.8
1999[1]	9.07	11.10	7.58	8.83	83.6	79.5
2000[1]	9.35	11.53	7.83	9.20	83.7	79.8
2001[1]	9.84	12.24	8.23	9.79	83.6	80.0
2002[1]	10.26	12.92	8.67	10.32	84.5	79.9
2003[1]	10.58	13.28	9.04	10.70	85.4	80.6
2004[1]	11.10	13.78	9.52	11.27	85.7	81.8

Source: ASHE, April 1998–2004, without supplementary information.

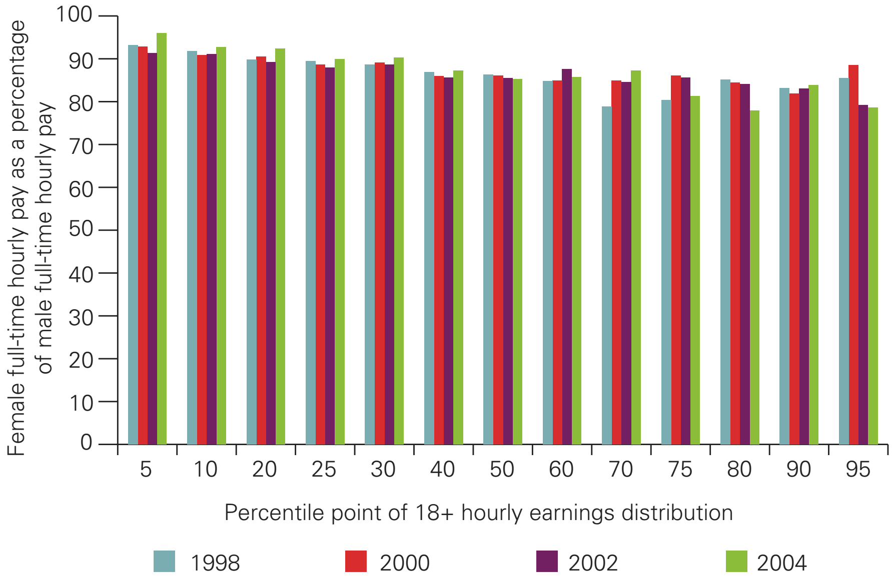
4.15 Two summary statistics of the earnings distributions, the median and the mean, are presented in Table 4.2. Recent commentary on the pay gap has been based on the median, not the mean, because the median is viewed as the more representative and less volatile measure. The earnings distribution has a long tail at the upper end of the distribution, and the mean is more sensitive to these very high earnings, including annual bonuses, than the median. This makes it more difficult to discern long-term trends. Because of this resulting sensitivity, and because men are much more prevalent among very high earners than women, using the mean suggests a larger gender pay gap.

4.16 According to ASHE 2004 without supplementary information, the hourly pay gap for full-time workers in 2004 as measured by the median, was 14.3 per cent – i.e. the median gross hourly wage rate of women was 85.7 per cent that of men. Using the mean as the summary statistic rather than the median shows the pay gap to be 18.2 per cent.

4.17 From Table 4.2 it can also be seen that the pay gap for full-time workers has reduced since 1998, the year before the minimum wage was introduced, when the ratio of women's pay to men's pay stood at 78.8 per cent as measured by the mean and 82.6 per cent as measured by the median. Figure 4.3 also bears this out and the likely influence of the minimum wage can be detected in the visible reduction of the pay gap in the first decile. The comparison refers only to monetary remuneration. Non-cash forms of remuneration, such as childcare vouchers, private medical insurance and pension benefits, are excluded because of the difficulty of collecting and valuing this information. It is thought that the inclusion of these other forms of payment would have the effect of widening the pay gap, with men reaping more of these benefits than women.

Figure 4.3

Full-time Gender Pay Ratio by Percentile for Employees Aged 18 and Over, 1998–2004



Source: ASHE, April 1998–2004, without supplementary information.

4.18 In contrast to the narrowing of the gender pay gap visible in Table 4.2, Table 4.3 shows that female part-time workers have made little progress in closing the gap with male full-time workers, with the ratio improving by only 0.9 percentage points. However, women part-time workers are paid slightly more than men who work part-time. During the period over which the minimum wage has been in existence, the position of women part-time workers has slipped by 1.5 percentage points compared with women working full-time. They earn an hourly rate worth only two-thirds of that earned by women full-time workers and 56.8 per cent of the rate earned by men full-time workers. It is likely that the wage floor established by the minimum wage has prevented the ratio from deteriorating any further.

Table 4.3 Median Gross Hourly Earnings Excluding Overtime by Gender and Hours of Work, 1998–2004

	Male £		Female £		Female part-time as percentage of male full-time	Female part-time as percentage of male part-time	Female part-time as percentage of female full-time
	Full-time	Part-time	Full-time	Part-time			
1998	8.7	4.7	7.2	4.9	55.9	104.0	67.7
1999	9.1	5.0	7.6	5.1	56.2	102.6	67.3
2000	9.4	5.1	7.8	5.3	56.3	103.5	67.2
2001	9.8	5.3	8.2	5.5	55.9	103.8	66.8
2002	10.3	5.7	8.7	5.7	55.7	100.5	65.9
2003	10.6	6.0	9.0	6.1	57.5	101.3	67.3
2004	11.1	6.1	9.5	6.3	56.9	104.5	66.4

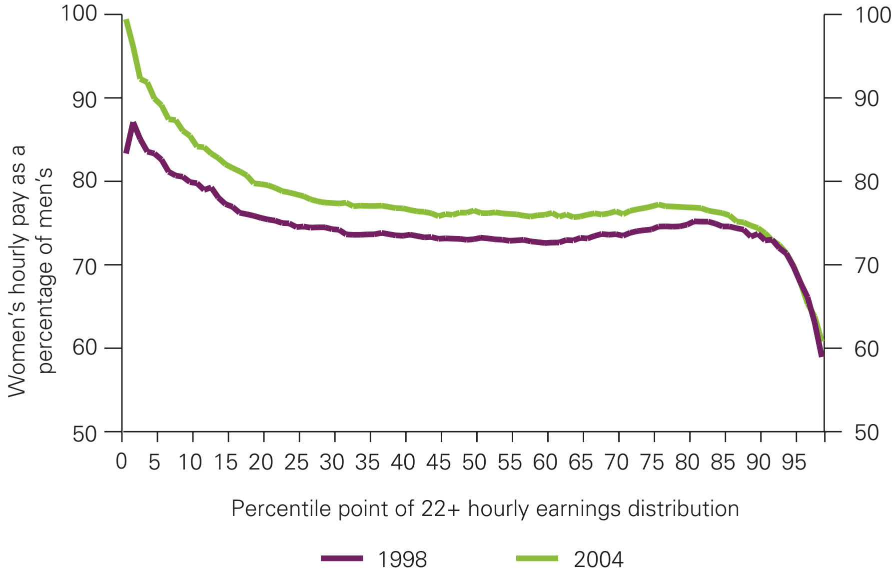
Source: ASHE, April 1998–2004, without supplementary information.

4.19 In order to focus on whether the minimum wage has had any influence in closing the gender pay gap, we need to study changes in earnings at the bottom end of the distribution. Other things being equal, if more women are low-paid than men, and more women benefit from upratings of the minimum wage than men, upratings would result in a narrowing in the gap of the mean pay of women relative to the mean pay of men. As Table 4.2 shows, the pay gap as measured by the median narrowed by 3.1 percentage points since the introduction of the minimum wage, and that as measured by the mean by 3.0 percentage points.

4.20 The changes in the ratio of women's to men's earnings across the entire distribution can be seen in Figures 4.4–4.6 below. Examining the position for adult workers first (those aged 22 and above), Figure 4.4 strongly suggests that the minimum wage has had a major impact, substantially reducing the pay gap at the very bottom of the earnings distribution, and helping to close the gap further up the distribution through the impact on differentials. The pay gap has also appeared to continue to close, independently of minimum wage upratings, in the middle of the distribution. The only area where there has been no progress in reducing disparities is from the ninetieth percentile and above. At the highest levels of pay women remain considerably disadvantaged with respect to men, but this is clearly not a disadvantage on which the minimum wage can have any influence.

Figure 4.4

Women's Hourly Pay as a Percentage of Men's by Percentile for Employees Aged 22 and Over, 1998 Compared with 2004

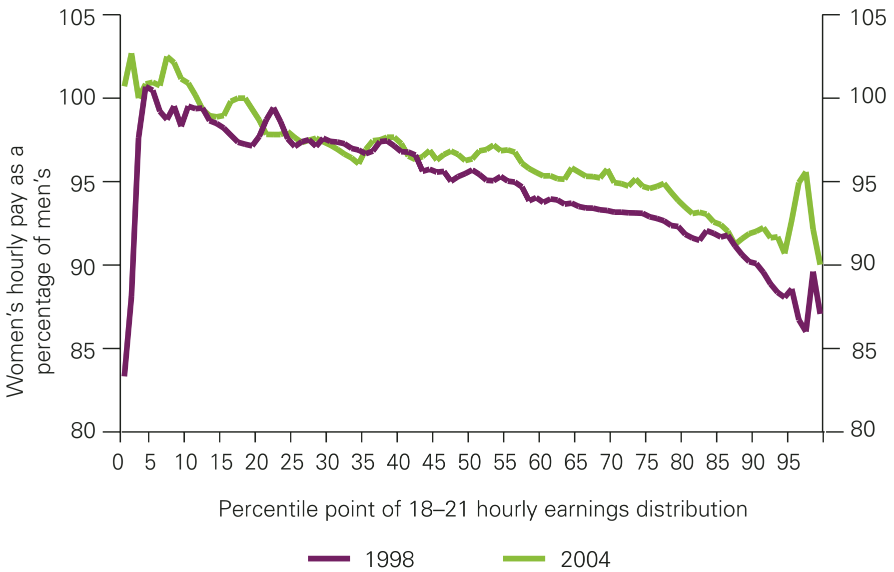


Source: ASHE, April 1998–2004, without supplementary information.

4.21 Among young people aged 18–21 the minimum wage has had similarly powerful effects on the gender pay gap, with women in the lowest five percentiles now paid roughly the same as men, versus about 15 per cent below in 1998 (see Figure 4.5).

Figure 4.5

Women's Hourly Pay as a Percentage of Men's by Percentile for Employees Aged 18–21, 1998 Compared with 2004

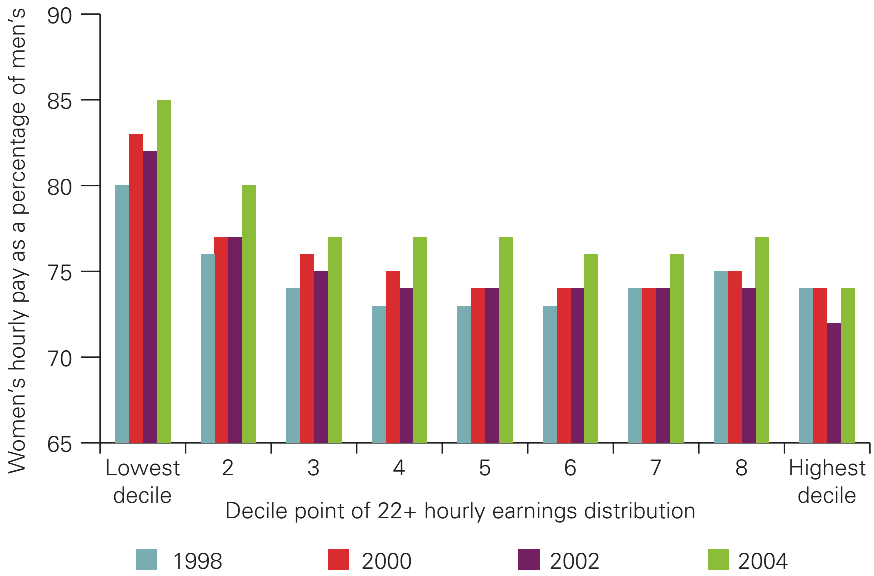


Source: ASHE, April 1998–2004, without supplementary information.

4.22 Figure 4.6 shows changes in the ratio of women's earnings to men's by decile for adult workers. The pay gap is now considerably smaller for the lowest decile than the others, clearly illustrating the part played by the minimum wage in closing the gap.

Figure 4.6

Women's Hourly Pay as a Percentage of Men's by Decile for Employees Aged 22 and Over, 1998–2004



Source: ASHE, April 1998–2004, without supplementary information.

4.23 A key factor underlying the remaining gender pay gap is that women are more likely to be in part-time work than men and part-time workers are paid less than full-time workers. According to the LFS, in Autumn 2004 43 per cent of female employees were working part-time, as opposed to 10 per cent of male employees. As Figure 4.7 demonstrates, there is no significant gender pay gap among part-time workers except at the very top of the earnings tables. However, in the ASHE data for April 2004, the gap between the median pay of women working full-time and women working part-time was as high as 33.7 per cent. In a study for the Women and Equality Unit, Manning and Petrongolo (2004) found that women working part-time tend to be younger, to have less education, and to have more children than women working full-time. They also found that almost 25 per cent of women part-time workers worked in low-paid occupations as care assistants, cleaners, or shop assistants.

'Women experience a pay penalty for working part-time and the prevalence of women working part-time in the UK economy is a key factor affecting the gender pay gap. The clustering of women into low paid part-time work, and the associated under-utilisation of women's skills are key issues to be tackled if the gender pay gap is to be eliminated.'

Equal Opportunities Commission evidence

Figure 4.7

Part-time Gender Pay Ratio by Percentile for Employees Aged 18 and Over, 1998–2004

Source: ASHE, April 1998–2004, without supplementary information.

4.24 The longer-term trend indicates that the gender pay gap was closing gradually for several decades, long before the minimum wage was introduced. Overall, the data examined strongly suggest that the minimum wage has exerted a major influence in narrowing the pay gap at the lower end of the earnings distribution. To fully disentangle these effects and establish what portion of the narrowing of the gap is down to the minimum wage, and what portion is due to other influences, would be difficult and may be the subject of future research.

Disability

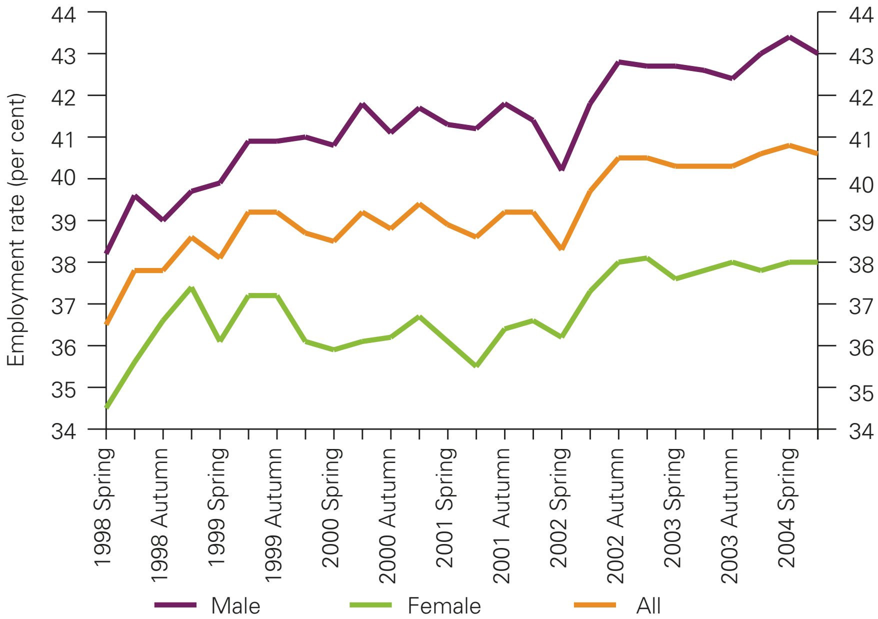
Employment

4.25 Unsurprisingly, employment rates for those with a work-limiting disability are much lower than for those without. However, the labour market prospects of those with a work-limiting disability have been improving. One of the sharpest declines in unemployment rates in recent years has taken place among those with work-limiting disabilities, having fallen by two percentage points in the year to Summer 2004. Since the announcement of the introduction of the minimum wage in Spring 1998, the employment rate of those with a work-limiting disability has risen from 36.5 per cent to nearly 41 per cent in Summer 2004. It seems clear that this group has not been further disadvantaged in terms of employment and unemployment since the introduction of the minimum wage, nor as a result of any of the subsequent upratings.

4.26 Figure 4.8 shows that men with work-limiting disabilities have higher employment rates than comparable women. The increase in the employment rate is common to both men and women.

Figure 4.8

Working Age Employment Rates of Those with Work-limiting Disabilities by Gender, 1998–2004

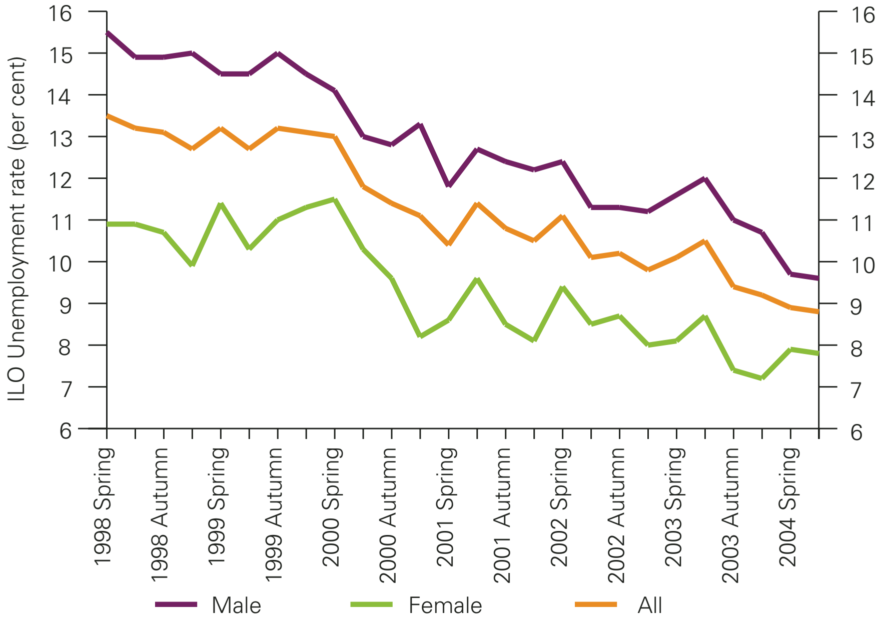


Source: LFS, 1998–2004.

4.27 Figure 4.9 shows that men with work-limiting disabilities also have higher unemployment rates than comparable women. However, in the six years to Spring 2004, the decline in the male unemployment rate has been nearly six percentage points compared with about three for women.

Figure 4.9

Working Age Unemployment Rates of Those with Work-limiting Disabilities by Gender, 1998–2004



Source: LFS, 1998–2004.

Pay

4.28 The earnings data in this section is drawn from the LFS, while the discussion in the earnings section on gender was grounded in data from the ASHE. The ASHE is a superior source of data for the analysis of earnings. Thus, where possible we have used ASHE data, for example in arriving at our best estimate of beneficiaries of the minimum wage. However, data for the earnings of those with a work-limiting disability are only available from the LFS. Although there are problems with the earnings variables in the LFS, particularly the derived hourly earnings variable, it is plausible that LFS data do at least reflect relativities, for example between the pay of those with work-limiting disabilities and those without.

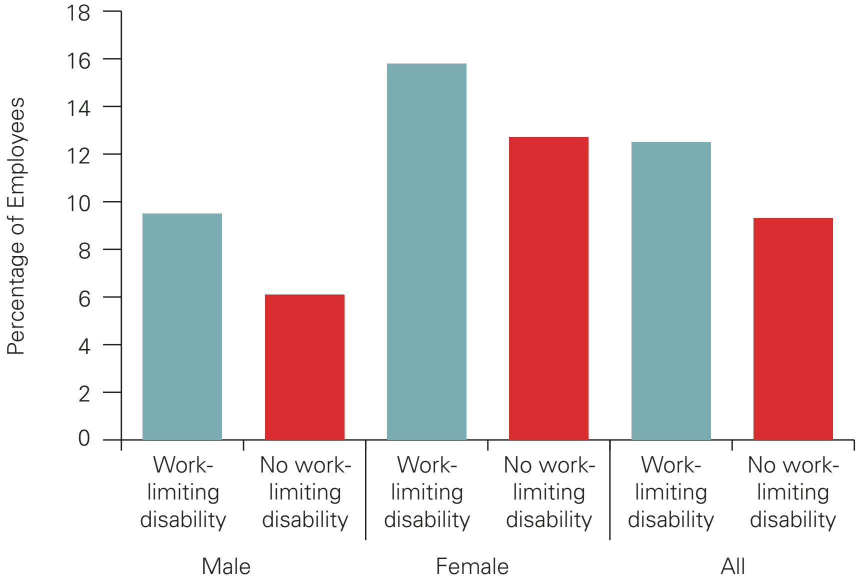
‘A national survey of 100 employers and 100 disability employment advisers found general agreement across both samples that the National Minimum Wage had benefited disabled people by making low paid jobs better paid.’

Disability Rights Commission evidence

4.29 The employment prospects of those with a work-limiting disability have not been harmed by the introduction of the minimum wage and we calculate from the derived hourly pay variable that 12.5 per cent of all jobs held by those with work-limiting disabilities should benefit from the 2004 upratings of the National Minimum Wage. This contrasts with 9.6 per cent of all jobs, as calculated from the LFS. (The numbers of beneficiaries calculated from the ASHE as a percentage of all jobs is significantly lower.) The effect on the pay of female workers with work-limiting disabilities is particularly evident. As shown in Figure 4.10 (which also appears in Chapter 2), nearly 16 per cent of jobs held by women with a work-limiting disability stand to benefit from the 2004 upratings, compared with 13 per cent of all jobs held by women without a work-limiting disability.

Figure 4.10

Percentage of Employees Benefiting from the 2004 Upratings of the Minimum Wage by Disability



Source: LFS, Spring 2004. LPC estimates based on ONS low pay methodology.

4.30 As Table 4.4 demonstrates, the larger impact of the 2004 upratings of the minimum wage on the pay of those with a work-limiting disability follows from the fact that the typical hourly wages for those with a work-limiting disability are lower than those without such a disability.

Table 4.4 Median Gross Hourly Pay Excluding Overtime by Work-limiting Disability for Employees Aged 18 and Over, 1998–2004

£ per hour	1998	2000	2002	2004
Work-lmiting	5.54	5.91	6.68	7.07
Not work-limiting	6.35	6.85	7.58	8.11

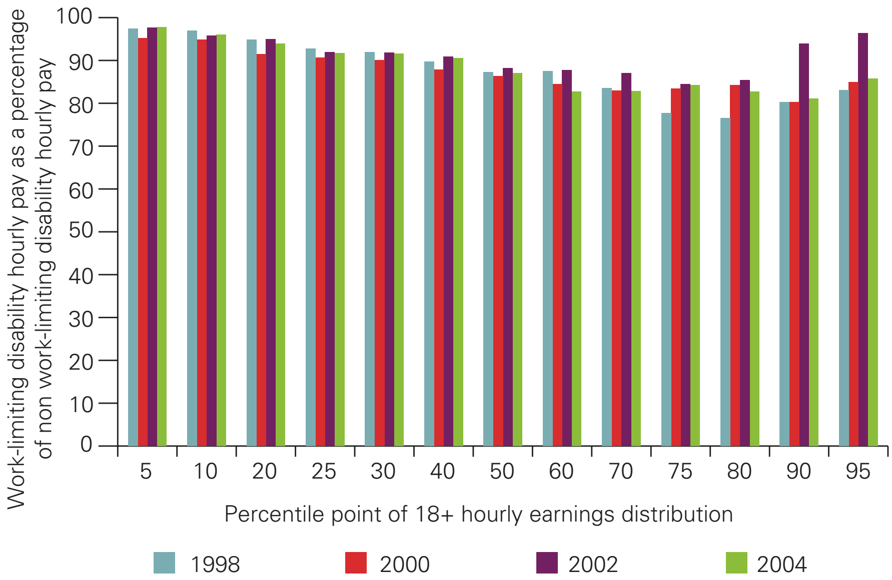
Source: LFS, 1998–2004. LPC estimates based on ONS low pay methodology.

4.31 Unlike the gender pay gap, there has not been a consistent fall in the gap between the earnings of those with a work-limiting disability and the pay of other workers since the introduction of the minimum wage. Average (mean) hourly pay for those with a work-limiting disability was just under 85 per cent of those without a work-limiting disability in Spring 1998, this rose to nearly 89 per cent in 2002, before falling back to 85 per cent in Spring 2004. Similarly, using the median as the measure of the pay gap, it is almost identical in 1998 and 2004, with the gap standing at 12.8 per cent.

4.32 Of course, these trends refer to the central tendency, or midpoint, of the earnings distribution of those with work-limiting disabilities. It is possible, as in the case of gender, that the minimum wage may have had a role to play in narrowing the pay gap at the bottom end of the earnings distribution. However, in this case the data do not support such a suggestion. Figure 4.11 shows that for the bottom two deciles, there is no sign of the gap having narrowed between 1998 and 2004.

Figure 4.11

Disability Pay Ratio for Employees Aged 18 and Over, 1998–2004



Source: LFS, 1998–2004.

Ethnicity

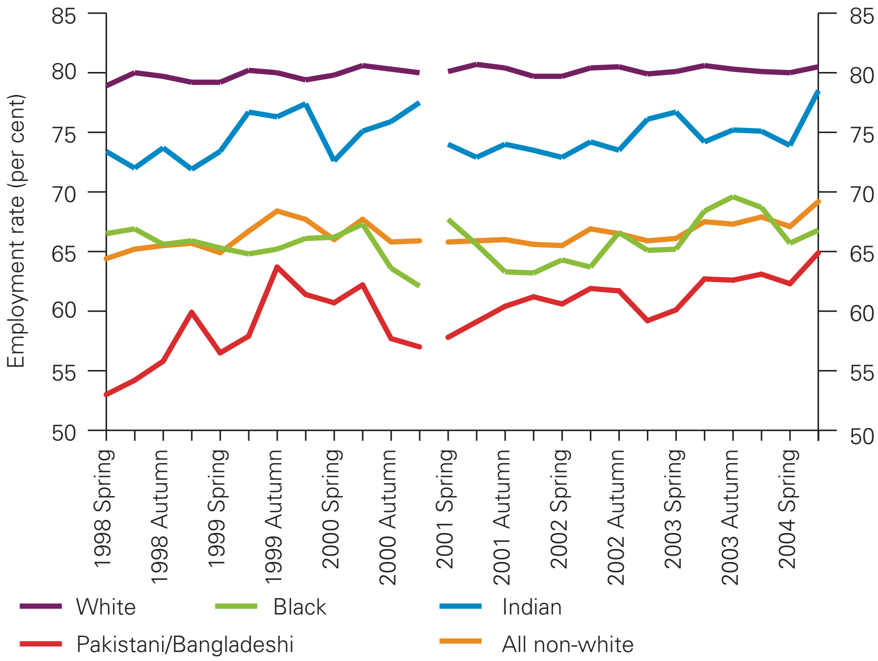
Employment

4.33 Even in the context of the overall strength of the labour market, there has been a particularly sharp increase in the employment rate of minority ethnic groups. Taken as a whole, the employment rate for minority ethnic groups has risen by over three percentage points since Spring 2000 to just less than 60 per cent in Summer 2004. There has been a corresponding decline in unemployment rates, which have fallen by two percentage points in the year to Summer 2004. In our discussion of this topic we have followed the classification of ethnicity adopted by the 2001 Census. In conducting this analysis, however, we recognise the difficulties inherent in any attempt to categorise people in terms of ethnicity, and the fact that no such system of classification can be entirely free of arbitrary delineations.

4.34 Using the self-reported classification in the LFS, there are significant differences in employment rates among the different minority ethnic groups. Figure 4.12 shows that whites have the highest male employment rates. Indians have the next highest. Blacks have similar rates to minority ethnic groups in general, while Pakistanis and Bangladeshis have the lowest. The male employment rate has increased from Spring 1998 to Summer 2004 for all the groups. The largest increase in these employment rates in this period has been among those with the lowest employment rates, namely Pakistanis and Bangladeshis.

Figure 4.12

Working Age Male Employment Rates for Ethnic Groups, 1998–2004



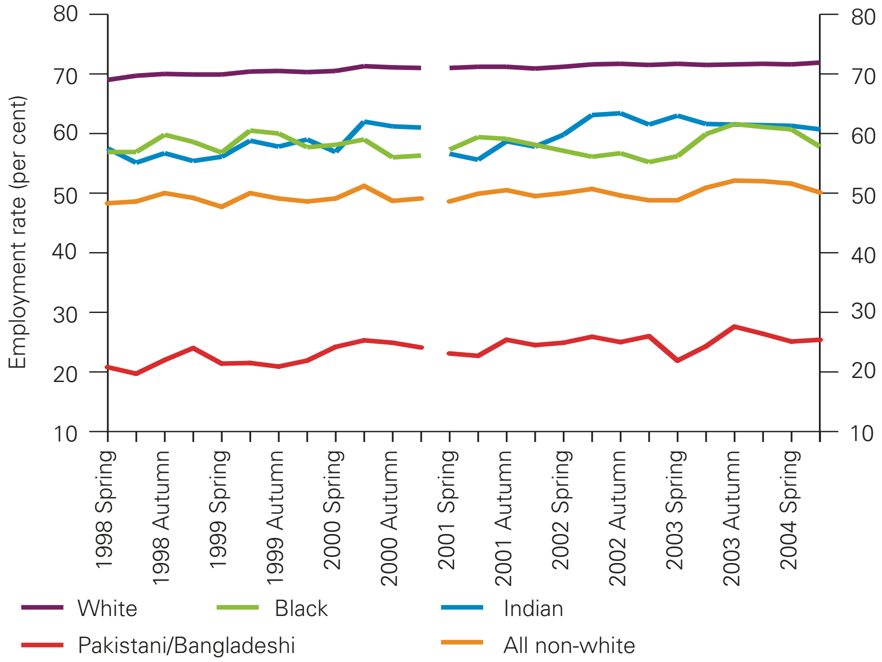
Source: LFS, 1998–2004.

Note: The definition of ethnic groups in the LFS changed in Spring 2001 to be in line with the 2001 Census classifications; thus direct comparisons between the periods before and after should not be made.

4.35 Figure 4.13 shows a similar pattern to men for women, although the employment rates are lower for all ethnic groups. Black women, however, have very similar employment rates to Indians. Pakistani and Bangladeshi women have very low employment rates.

Figure 4.13

Working Age Female Employment Rates for Ethnic Groups, 1998–2004



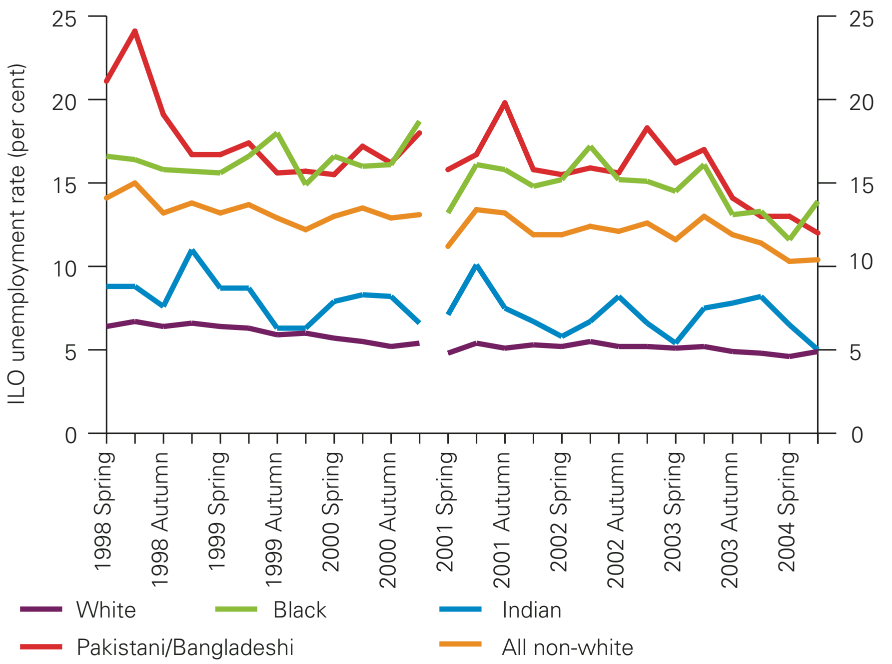
Source: LFS, 1998–2004.

Note: The definition of ethnic groups in the LFS changed in Spring 2001 to be in line with the 2001 Census classifications; thus direct comparisons between the periods before and after should not be made.

4.36 A similar picture is suggested when we look at unemployment rates for men (Figure 4.14) which have fallen for all ethnic groups. Pakistani, Bangladeshi and black men, however, have significantly higher unemployment rates than other ethnic groups.

Figure 4.14

Working Age Male Unemployment Rates for Ethnic Groups, 1998–2004



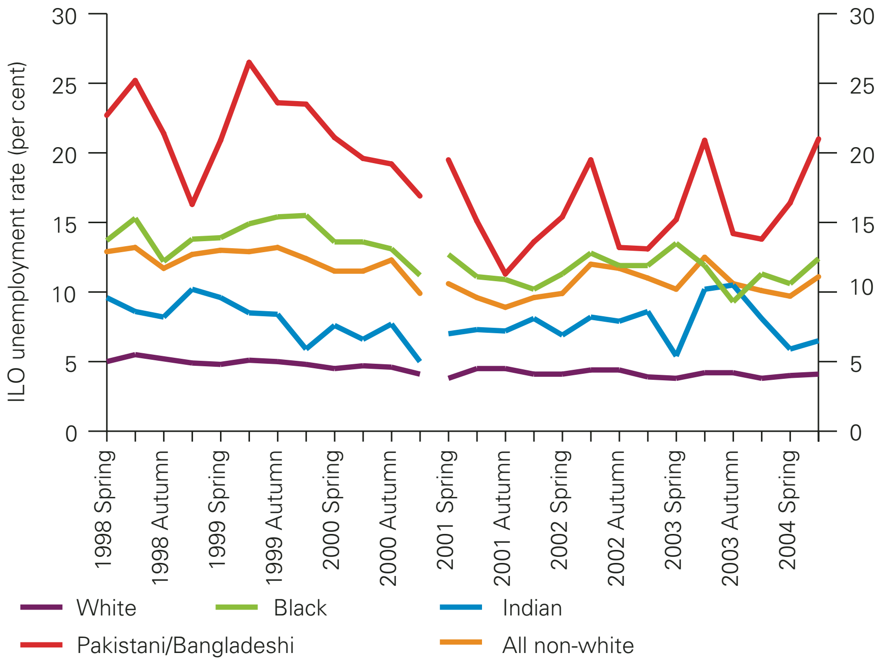
Source: LFS, 1998–2004.

Note: The definition of ethnic groups in the LFS changed in Spring 2001 to be in line with the 2001 Census classifications; thus direct comparisons between the periods before and after should not be made.

4.37 Similar unemployment rate patterns for women are shown in Figure 4.15 although it should be noted that black women have higher unemployment rates than Indian women, even though their employment rates are similar.

Figure 4.15

Working Age Female Unemployment Rates for Ethnic Groups, 1998–2004



Source: LFS, 1998-2004.

Note: The definition of ethnic groups in the LFS changed in Spring 2001 to be in line with the 2001 Census classifications; thus direct comparisons between the periods before and after should not be made.

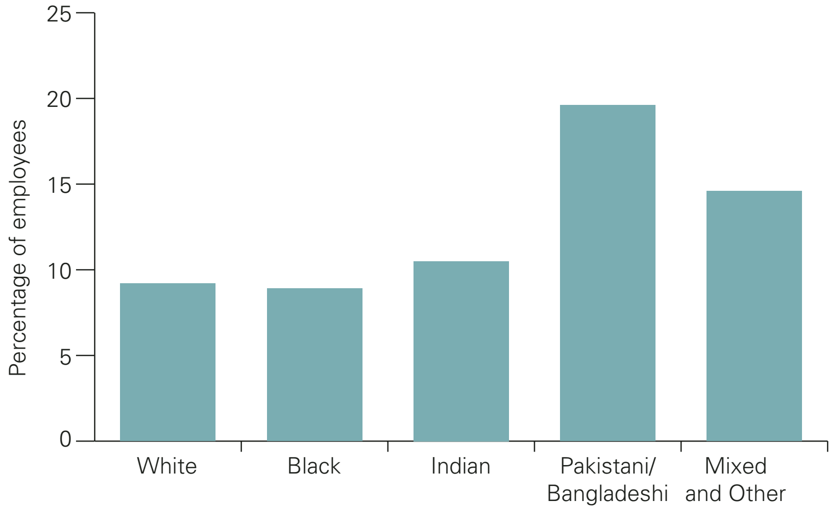
4.38 Overall, one important message to emerge from all available data is that there is no evidence to suggest that the introduction of the minimum wage has harmed the employment prospects of these vulnerable groups in the labour market. On the contrary, the employment levels of those with the lowest rates of employment have strengthened the most. It is also possible that the introduction of the minimum wage has created incentives which led to higher levels of labour market participation among some of these groups.

Pay

4.39 Minority ethnic groups number disproportionately among the beneficiaries of the 2004 upratings of the minimum wage. While about 6 per cent of the adult working population belong to minority ethnic groups, we estimated that some 8 per cent of the beneficiaries of the 2004 upratings belonged to a minority ethnic group. The disaggregated situation with respect to the different groups is shown in Figure 4.16, which is also shown in Chapter 2. It is clear that, in terms of minority ethnic population groups, the largest percentage of workers from a particular population group to benefit from the 2004 upratings of the minimum wage were workers of Pakistani and Bangladeshi origin.

Figure 4.16

Percentage of Employees Benefiting from the 2004 Upratings of the Minimum Wage by Ethnicity



Source: LFS, Spring 2004. LPC estimates based on ONS low pay methodology.

4.40 We now turn to look at the ethnic pay gap. Our preferred source of data, (ASHE), does not have breakdowns by ethnicity. Therefore, as with the disability pay gap, we turn to the LFS as the most authoritative alternative source available.

4.41 Table 4.5 shows that overall, white workers get paid more per hour than non-white workers, but this conceals much diversity among minority ethnic groups overall and by gender. The lowest paid workers are of Pakistani and Bangladeshi descent. In contrast, workers from an Indian background tend to be paid the same if not more than white workers. Although white male workers earn more on average than black male workers, black women earn more than white women. This may be due to the fact that a larger proportion of white women work part-time and, as we have seen, part-time work is not as well paid as full-time work.

Table 4.5 Median Hourly Pay by Ethnicity for Employees Aged 18 and Over, 1998–2004

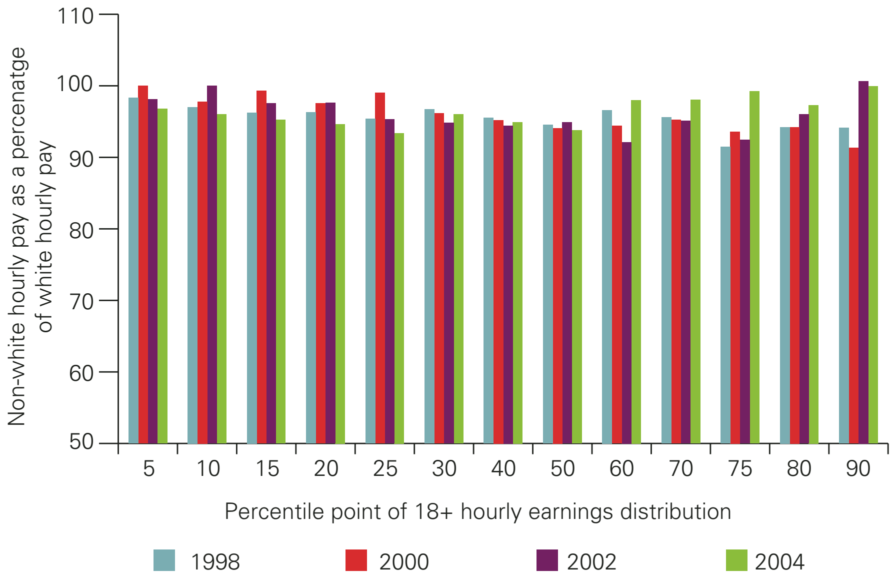
£ per hour	1998	2000	2002	2004
White	6.29	6.76	7.51	8.00
Non-white	5.95	6.36	7.13	7.50
Black	5.83	7.04	7.41	7.33
Indian	6.11	6.57	7.00	8.41
Pakistani/Bangladeshi	5.24	4.94	5.80	6.25
Mixed/other	6.54	6.00	7.75	7.60

Source: LFS, 1998–2004. LPC estimates based on ONS low pay methodology.

4.42 Figure 4.17 suggests that the ethnic pay gap is much smaller than the corresponding pay gaps for both gender and disability. However, in calculating the ethnic pay gap we had to treat all non-whites as a single group because of small sample sizes, and this will have concealed some significant differences between groups. Even so, the pay gap shown in Figure 4.17 increases as we move up the earnings distribution to the median, before decreasing at the upper end. As the ethnic pay gap was small to begin with, and as it has not changed significantly since the introduction of the minimum wage, we can conclude on the basis of available data that the minimum wage has not had much overall impact on the ethnic pay gap.

Figure 4.17

Ethnic Pay Ratio for Employees Aged 18 and Over, 1998–2004



Source: LFS, 1998–2004. LPC estimates based on ONS low pay methodology.

4.43 Table 4.6 shows that, as a whole, white male workers are paid higher hourly wages than non-whites. In Spring 2004, the difference was about £1.80 per hour. Pakistani and Bangladeshi men, however, were paid on average about £3.00 per hour less than white male workers. In contrast, it appears that men of Indian descent were paid much the same as white male workers.

Table 4.6 Median Hourly Pay by Ethnicity for Male Employees Aged 18 and Over, 1998–2004

£ per hour	1998	2000	2002	2004
White	7.19	7.75	8.63	9.31
Non-white	6.43	6.36	7.73	7.54
Black	6.00	7.04	8.03	7.00
Indian	7.92	7.00	7.76	9.56
Pakistani/Bangladeshi	4.93	4.94	6.00	6.25
Mixed/other	7.84	5.50	8.10	7.60

Source: LFS, 1998-2004. LPC estimates based on ONS low pay methodology.

4.44 The pattern for women from minority ethnic backgrounds is very different, as illustrated in Table 4.7. Non-white female workers as a whole get paid about 70 pence an hour more than white women. Only Pakistani and Bangladeshi women are paid lower hourly rates than white women. Black, Indian and mixed and other women are paid much higher hourly rates than white women. This surprising finding may be a result of the fact that white women are far more likely to work part-time than women workers from other ethnic groups.

Table 4.7 Median Hourly Pay by Ethnicity for Female Employees Aged 18 and Over, 1998–2004

£ per hour	1998	2000	2002	2004
White	5.39	5.84	6.46	7.06
Non-white	5.71	6.40	6.51	7.50
Black	5.66	7.32	7.00	8.27
Indian	5.05	5.88	6.51	7.60
Pakistani/Bangladeshi	6.62	5.00	5.52	6.24
Mixed/other	6.23	6.45	7.07	7.58

Source: LFS, 1998–2004. LPC estimates based on ONS low pay methodology.

4.45 When comparing the ethnic distribution of the earnings of full-time and part-time women workers, marked differences emerge. However, there is no ethnic pay gap among full-time women workers. As in the case of men, it is impossible to conclude from the available data that the National Minimum Wage has had any significant impact in lowering pay disparities among women from different ethnic groups.

4.46 We turn next to the impact of the minimum wage on three specific groups of workers: homeworkers, volunteers, and those undertaking therapeutic activity. We also consider some specific enforcement issues arising from the treatment of these groups under the National Minimum Wage.

Homeworkers

4.47 Our previous reports have highlighted the problems which some homeworkers have encountered in the operation of the National Minimum Wage. While we are aware that there are homeworkers, particularly in skilled occupations, who earn well above the minimum wage, our focus continues to be on those carrying out low-paid, unskilled manual work at home. This might include assembly, finishing or packing of such goods as clothing, textiles and electrical items. It is difficult to assess accurately the size and characteristics of this largely hidden workforce, but a 2004 Oxfam Briefing Paper, building on earlier work by the National Group on Homeworking, suggested that there might be up to one million homeworkers undertaking this type of manual work, of whom 90 per cent were likely to be women and up to 50 per cent were likely to be from a minority ethnic group.

4.48 Firms employing homeworkers benefit from a flexible workforce which is able to respond very quickly to changes in demand. For the worker, undertaking these tasks at home may provide a valuable source of income which can be fitted around caring or other responsibilities. Homeworkers may, however, face particular difficulties in enforcing their rights to the minimum wage. This is often because they work in isolation, their employment status is unclear and they fear that if they complain the work will simply be transferred to someone else.

4.49 It has been common practice for homeworkers to be paid according to the amount of work they complete (often known as piecework), rather than being paid according to the number of hours spent on a task. Following the introduction of the minimum wage, employers were required either to pay homeworkers for every hour worked, or to come to a fair estimate agreement of the number of hours to be worked. The Regulations required that a fair estimate of the time the worker was likely to spend on output work could not be less than four-fifths of the time which an average worker would take to complete the task. In practice this meant that those undertaking output work might legally receive only four-fifths of the minimum wage. For previous reports we received evidence that fair estimate agreements were rarely used and, where they were, that they had often either been misunderstood or abused. We recommended in our third report that the Government consult on the case for a change to the Regulations.

4.50 In February 2003 the Government consulted on introducing a system of fair piece rates to replace the fair estimate agreement system. We supported the proposals in our response to the Government's

‘Between 2000 and 2003, NGH was contacted by a total of 17 homeworkers engaged in [Christmas] cracker assembly and packing; their rate of pay varied from 73p to £1.40 an hour.’

National Group on Homeworking, Oxfam and TUC, 2004. Made at Home: British Homeworkers in Global Supply Chains

‘We welcome the arrangements for a new fair piece rate system for output workers … and we will seek to monitor its application, particularly in relation to homeworkers, and report to the DTI on any problems with implementation.’

GMB evidence

consultation and welcome the new provisions which came into force on 1 October 2004 together with the accompanying guidance for workers and employers. Employers are now required to pay the minimum wage either for every hour worked or according to a fair piece rate, derived from the time that a person working at average speed would take to produce the piece in question. They are also required to carry out tests on at least a sample of workers to determine the average output rate. From April 2005, employers will have to increase the fair piece rate by a factor of 1.2 so that the majority of workers (not just those whose rate of work is above average) will receive at least the minimum wage.

4.51 In our fourth report (2003), we commented that the new rules for output work should be accompanied by effective, proactive, targeted enforcement to improve compliance, particularly in relation to homeworking. While we are aware that the Inland Revenue has established a specialist homeworkers team, which is able to investigate complaints and give advice to other enforcement teams, we continue to believe that this is an important area for enforcement activity. As noted in Chapter 6, we are also concerned that awareness of the minimum wage is lower in particular groups of vulnerable workers, including homeworkers. The Government is considering the introduction of a rolling programme of publicity and enforcement which will target a different low-paying sector each year. This is an initiative which we strongly support and we consider it important that homeworking is included among the sectors targeted early on in the programme.

Volunteers

4.52 In preparing our earlier reports, we received evidence indicating uncertainty within the voluntary sector about the circumstances in which voluntary workers may be entitled to the minimum wage. Genuine volunteers are not entitled to the minimum wage since they are not covered by the definition of the term 'worker' under the National Minimum Wage Act 1998. Paid employees working in the voluntary sector are entitled to the minimum wage like any other worker, but the Act also exempts voluntary workers employed by charities, voluntary organisations and similar bodies, provided they receive only reasonable subsistence, accommodation or expenses, but no other monetary payments or benefits-in-kind. In addition, a genuine 'honorarium', or one-off gift with no expectation or obligation and of a reasonable amount, should not normally imply an entitlement to the minimum wage. The subject of voluntary workers was not raised in our fourth report (2003) and we received evidence on this topic from only one organisation in preparing this report. This may indicate that voluntary sector organisations are now more familiar with the operation of the National Minimum Wage, but that some problems remain.

4.53 The Central Council of Physical Recreation (CCPR) reported that there may be circumstances in which a sports club genuinely believes that an individual member is acting as a volunteer (and the member also believes this is the case), but an entitlement to the minimum wage could be inferred because a small non-cash benefit is offered, or where an 'honorarium' has become customary for holders of a particular office. The CCPR gave a number of other examples, including a scenario where a coach is paid for his or her time, but freely volunteers to give extra lessons at the same club with no expectation of payment for the additional hours. In such circumstances, the club might find it difficult to demonstrate that separate arrangements exist. It was also concerned that the requirement to keep records of hours worked could place a burden on organisations which operate on a not-for-profit basis and are run largely by volunteers. Some of the issues highlighted in the CCPR's evidence are discussed in existing guidance and we note that there are ongoing discussions between the Inland Revenue, the Department of Trade and Industry and the CCPR. We hope that these will help to resolve some of the outstanding concerns identified in the CCPR's evidence.

4.54 While those working in the voluntary sector who are entitled to the minimum wage must not be disadvantaged, we recognise that many sports clubs and other community activities depend on people who gladly give their time for scant financial reward. We would not wish the operation of the minimum wage to act as a disincentive to those who wish to participate in an activity on a genuinely voluntary basis. The Government's evidence to the Commission indicated that there might be areas where Inland Revenue compliance officers could spend less time, in order to free up time for tackling important breaches in low-paying sectors. We would support the application of this kind of proportionate enforcement approach to the voluntary sector, provided that genuine cases of non-compliance are not overlooked.

4.55 Nevertheless it remains important that voluntary sector organisations are clear about their responsibilities under the minimum wage legislation. Although some useful guidance for the voluntary sector exists, the booklet in question – *National Minimum Wage, Guidance for the Voluntary Sector* – was produced several years ago and may not be fully up to date. In addition, some voluntary organisations may be unaware of relevant information contained in the DTI publication, *The Minimum Wage and 'Therapeutic Work.'* **We recommend that the Government should review and draw together existing guidance into a single source (adding any new points of clarification arising from the DTI and Inland Revenue's discussions with the CCPR and any other relevant organisations) to provide clear and accessible advice to the voluntary sector.**

Therapeutic Activity

4.56 In preparing our fourth report (2003) a considerable amount of evidence was received concerning the application of the minimum wage to people with a disability or a mental health problem. We have always maintained that people with disabilities should be covered by the minimum wage, and accordingly the legislation makes no distinction between the disabled and non-disabled, nor does it make any reference to a worker's productivity. But a range of activities are provided for people with disabilities or mental health problems and, as we noted in our previous reports, it is not always easy to distinguish between an activity focused on providing therapeutic benefits for the individual, and activities that should be regarded as work and attract the minimum wage.

4.57 The Government produced a guidance note on the minimum wage and therapeutic activity in December 2000, following a recommendation in our second report. Uncertainty remained, however, and we subsequently discussed with a range of organisations the question of where the boundary should lie between work (attracting the minimum wage) and non-work activity. As a result we suggested in our fourth report that an activity should not be regarded as work if the following four conditions all applied:

- The activity is demonstrably focused on meeting the needs of the individual involved rather than the needs of the organisation;
- The individual is referred to the activity – and monitored and supported on an ongoing basis – by a health or social care organisation;
- The arrangement has been agreed with the individual and not made over her/his head; and
- The tempo of the activity, and of any output or delivery target, reflects the needs of the individual rather than those of the organisation.

'A further concern is that some day centres who previously paid expenses and gave those undertaking work-like therapy free meals have withdrawn these provisions for fear of falling foul on the minimum wage rules.'

TUC evidence

4.58 Our fourth report shortly preceded the publication of revised Government guidance. We recommended that the Government should monitor its impact very closely and ensure that uncertainty about the minimum wage did not adversely affect people doing therapeutic activity. The Government subsequently wrote to interested organisations in August 2003 and July 2004 inviting feedback on the revised guidance. The Government's evidence stated that 'limited feedback was received but the anecdotal evidence is that the guidance has reduced the uncertainty about therapeutic work and the minimum wage'.

'Some organisations employing people with learning disabilities were either not aware of their duties under the NMW, confused about NMW application, simply avoiding the issue or scaling back the employment provision they were offering.'

Department of Health and Department for Work and Pensions Working Group on Learning Disabilities and Employment, report forthcoming

4.59 We welcome the Government's revised guidance and believe it has helped resolve most of the uncertainty about whether an activity would be classed as work for minimum wage purposes. Certainly few respondents raised this issue in their evidence. But there was some concern that the guidance has not been widely disseminated and a few examples of the minimum wage adversely affecting people performing therapeutic activity were also highlighted.

4.60 Disability organisations told us that some providers previously paying disabled workers £10–£15 per week had withdrawn payments to avoid being liable for the minimum wage. The Disability Rights Commission (DRC) had limited experience of the complaints procedure but felt that more efforts could be made to ensure that these were accessible to the range of disabled people. The DRC was concerned that the minimum wage guidance on therapeutic activity might not prevent exploitation, and that the emphasis should be on supporting people in open employment. The DRC saw value in an Inland Revenue investigation of pay and conditions in the day care and related sectors, and believed that doing a real job for real pay was integral to progressive employment policies.

4.61 The joint Department of Health and Department for Work and Pensions Working Group on Learning Disabilities and Employment (report forthcoming) considered the impact of the National Minimum Wage. The Group wants to maximise the opportunities for people with learning disabilities to undertake meaningful or supported employment – receiving at least the minimum wage. However, members of the Working Group were aware of a number of learning disability projects (including Local Authority operated schemes) failing to pay staff in line with the minimum wage. The Group wants key interested parties to come together and consider how to ensure all organisations that employ people with learning disabilities recognise their obligations under the minimum wage. It wishes to avoid employment projects being closed either due to ignorance of the rules or from fear of being liable for back payment of wages. The Group believes that an effective adjustment strategy to highlight and improve awareness of employers' responsibilities under the minimum wage is critical, and that employment projects should be able to seek additional advice in order to ensure their provisions comply with the minimum wage.

4.62 On a Low Pay Commission visit to South-East England we saw how one social enterprise (MCCH Society Ltd) had successfully managed to transform its services in response to the minimum wage. The organisation has divided its services to people with learning disabilities into three parts: the Training and Work Preparation Scheme which is unpaid and voluntary; Internal Supported Employment Placements where service users are paid the minimum wage; and External Supported Employment Placements which are voluntary for the first six weeks but with the intention of employment becoming permanent. MCCH Society Ltd reported that it viewed the minimum wage 'as a positive step to reducing stigma, discrimination and workplace exploitation. In our organisation the introduction of the minimum wage has acted as a catalyst to change and modernise the services with far reaching and beneficial results both to our practice and to the lives of service users.'

4.63 We continue to believe that people with disabilities should be entitled to the minimum wage and recognise that the Government's revised guidance has helped resolve many of the uncertainties about entitlement to the minimum wage. But some problems remain. We understand that a number of employment projects are failing to pay staff in line with the minimum wage. In other cases, payments have been withdrawn, with organisations perhaps unaware that reasonable expenses can be paid to those undertaking therapeutic activity without creating an entitlement to the minimum wage. Awareness of the revised guidance needs to be improved and social enterprises should also be helped to adapt their practices to comply with the minimum wage. We discuss awareness and enforcement of the minimum wage in Chapter 6.

4.64 A further concern raised by respondents relates to the interaction between the minimum wage and benefits paid to people because of illness or disability. The Permitted Work Lower Limit enables people to earn up to £20.00 per week without requiring their benefits to be reassessed – equivalent to about four hours work on the minimum wage. Some concern continues to be expressed that the earnings disregard is not increased in line with minimum wage upratings, resulting in workers with disabilities or mental health problems reducing the number of hours they work per week. We are also aware that some organisations believe that rather than simply raising the earnings disregard, other changes to the benefits system are required.

4.65 It is beyond our remit and expertise to advise on the design of the benefits system but we wish to highlight the fact that minimum wage upratings are leading some disabled people to reduce the number of hours spent in paid employment. The minimum wage could therefore be having unintended consequences for disabled people who are capable of working more than four hours per week, but who are reluctant (or whose carers are reluctant) to do so for fear of losing Income Support and associated benefits. This may also discourage these workers from seeking to gradually increase their working hours over a period of time. As part of its efforts to increase work incentives for those with disabilities, we would encourage the Government to take into account the fact that minimum wage upratings are reducing the number of hours that can be worked before reaching the £20.00 per week earnings disregard.

Conclusion

4.66 The overall message of this Chapter is an encouraging one. The minimum wage has not led to a reduction in employment opportunities for any of the groups considered, with the possible exception of workers undertaking therapeutic work. It is also encouraging that most members of the groups examined here, including those disadvantaged in various ways, earn wages significantly above the level of the minimum wage.

4.67 On average, women still earn less than men, although the gap has been closing steadily. The effect of the minimum wage in narrowing the gender pay gap at the bottom of the earnings distribution is particularly striking in the data presented.

4.68 As between different groups of minority ethnic workers, the minimum wage has not been a clear driver of narrowing pay gaps, but that largely reflects the fact that pay gaps by ethnic groups are much less pronounced than by gender, and that the pattern is complex with some minority ethnic groups doing better than whites. Nor has the minimum wage closed pay gaps between workers with a work-limiting disability and others not similarly affected.

4.69 But across all the groups considered – women, minority ethnic groups and workers with work-limiting disabilities – the minimum wage has clearly benefited a large number of low-paid workers, and workers in these groups are disproportionately represented among the beneficiaries.

4.70 There is some evidence that compliance needs to be tightened and awareness of the minimum wage increased in the case of homeworkers. This is discussed in more detail in Chapter 6. In the next Chapter we look at two other groups of workers who may be particularly affected by the minimum wage, namely young people and trainees.

Young People and Trainees

The number of jobs held by 18–21 year olds that benefited from the October 2004 uprating of the youth Development Rate is estimated at 120,000; this compares with 70,000 benefiting from the October 2003 uprating. In addition, many young people received pay rises as a result of increases in the adult rate. All the available evidence indicates that the minimum wage has not harmed the employment prospects of young people. Employment rates for 18–21 year olds have remained largely unchanged following the October 2003 increases in the minimum wage, though they are below the peaks reached in 2000/01. Total employment levels of young people are increasing, including in low-paying sectors.

The introduction of the 16–17 year old rate in October 2004 benefited up to 45,000 jobs. We will consider the impact of the minimum wage for 16–17 year olds in future reports.

In line with previous experience following a large uprating, the number of young people's jobs being paid below the adult rate of the minimum wage has increased, with a number of firms introducing age-related pay to offset the cost of minimum wage upratings. But other firms are moving in the opposite direction and there is no clear long-term trend. Age-related pay is not widespread and, even in the minority of firms that employ it, its use is often restricted to certain positions or new recruits in the first few months of employment. Where firms have introduced age-related pay, there is evidence that the minimum wage has resulted in age 22 being established as the threshold for payment of full adult rates of pay, whereas previously lower ages tended to be used.

The forthcoming implementation of the Equal Treatment Directive (2000/78/EC) outlawing age discrimination at work increases the need to ensure an appropriate youth Development Rate. We are strongly convinced that there is a need for a youth Development Rate which is lower than the adult rate and that adverse consequences for some young people would result if employers were not able to pay some younger workers below the adult minimum wage level. But we believe that the

most appropriate cut-off point between the youth Development Rate and the adult rate is at the 21st birthday. We therefore again recommend that 21 year olds should receive the adult rate of the National Minimum Wage.

The exemptions from the minimum wage for apprentices continue to work well, while the older workers' Development Rate remains little used. We believe that implementation of the Equal Treatment Directive will necessitate a change to the present requirement that apprentices must be under the age of 26 for the 12 months exemption from the minimum wage to apply. Our provisional conclusion is that the older workers' Development Rate should be abolished from October 2006, and that, simultaneously, the 12 months exemption from the minimum wage should be extended to cover all apprentices aged 19 and over. We recommend that the Government invite the Commission to review these provisional conclusions and make firm recommendations on these matters by February 2006.

Introduction

5.1 Since the initial introduction of the National Minimum Wage we have aimed to ensure that young people are not priced out of the labour market. We have also been concerned that the minimum wage should not reduce training opportunities.

5.2 The evidence demonstrates that young people's wages are significantly lower than those of older workers and that young people are more likely to suffer unemployment. Research shows that youth unemployment can scar a person's employment prospects in later life and international evidence suggests that any potential adverse effects of national minimum wages are more likely to be felt among young people than adults. It is for these reasons that we have consistently recommended a youth Development Rate for 18–20 year olds, set at around 85 per cent of the adult rate.

5.3 We believe that the youth Development Rate offers valuable flexibility to employers and provides scope for a higher adult rate without risking the job prospects of young people. But we also consider that, to be credible, the youth Development Rate should only apply to those needing protection. It is a matter of judgement where the cut-off for the adult rate should apply, but we have always recommended that 21 year olds should be entitled to the adult rate. In the past the Government has disagreed and, in responding to the recommendation in our fourth report (2003), the Government commented that 'analysis of the employment and unemployment rates for young workers suggests a mixed performance on the part of 21 year olds, and we do not want to jeopardise their job prospects'.

5.4 Our fourth report (2003) established that young people had fared worse than average in the labour market in the year following the October 2001 upratings, and our 2004 report found that the labour market performance of young people continued to decline in the year to Autumn 2003. We considered it unlikely that the fall in the employment rate of 18–21 years olds was caused by the minimum wage but nevertheless we recognised the need for some caution on the youth Development Rate.

5.5 The fourth report also found that a number of full-time jobs for 16–17 year olds offered very low pay and little or no training. We were pleased that the Government subsequently accepted our recommendation that we should advise on whether a minimum wage for 16–17 year olds could be introduced which would put a stop to exploitation, without either encouraging young people out of education or harming the supply of training places. Our 2004 report concluded that this balance was possible and the Government accepted our recommendation of a minimum wage of £3.00 per hour for 16–17 year olds. This was implemented in October 2004 and we will assess its impact in future reports.

5.6 In this Chapter we first consider the impact of the October 2003 upratings on young people's labour market performance. Second we estimate the number of beneficiaries of the latest upratings and consider the impact on earnings. We then assess recent trends in the use of age-related pay and consider the role of the youth Development Rate, including its age coverage. Finally we consider training and workforce development, the role of the older workers' Development Rate and the minimum wage exemption for apprentices. Additional information on the labour market position of 18–21 year olds can be found in Appendix 6.

Employment, Unemployment and Participation of Young People

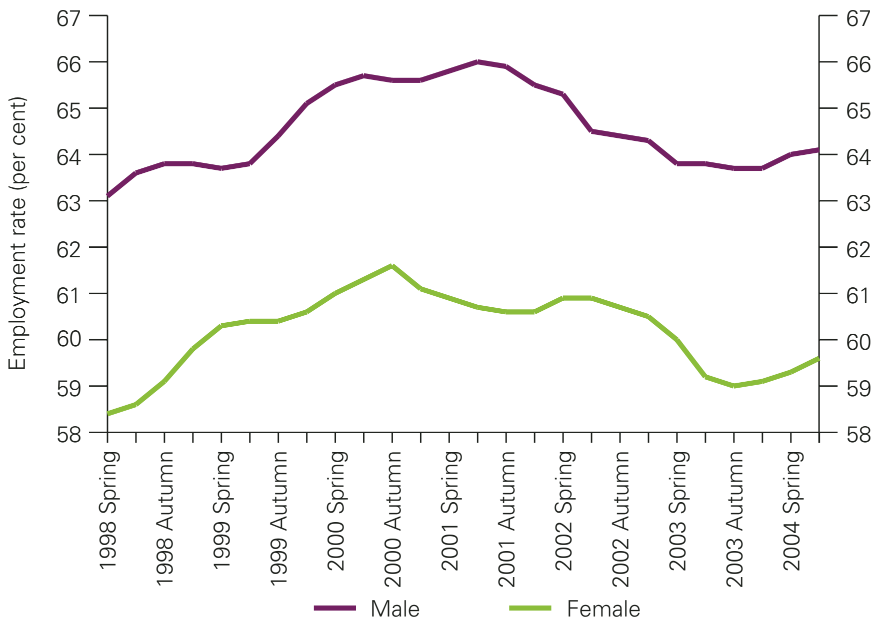
5.7 The overall UK labour market has remained remarkably robust since the introduction of the minimum wage. Young people, however, have fared less well. Our previous reports found that in the two years following the October 2001 upratings there was a decline in the employment rate of 18–21 year olds and a slight rise in their unemployment rate. They also showed that the employment rate of 16–17 year olds has been on a declining trend since mid-1997. We consider here whether these trends have continued, looking separately at the labour market performance of 18–21 and 16–17 year olds.

Labour Market Position of 18–21 Year Olds

5.8 Employment rates of 18–21 year olds rose steadily from 1994–2001, appearing unaffected by the initial introduction of the minimum wage. But as Figure 5.1 shows, they fell during the period Summer 2001–Summer 2003, by 2.2 and 1.5 percentage points for men and women respectively. We commented on this decline in our fourth report (2003), and though we had no reason to believe that it had been produced by the 2001 upratings of the minimum wage, we flagged the need for caution looking forward. Since Summer 2003, however, there has been a slight increase in the employment rate of both men and women, despite the significant October 2003 upratings. Unemployment rates for 18–21 year olds have largely mirrored the employment trends, as illustrated in Figure 5.2.

Figure 5.1

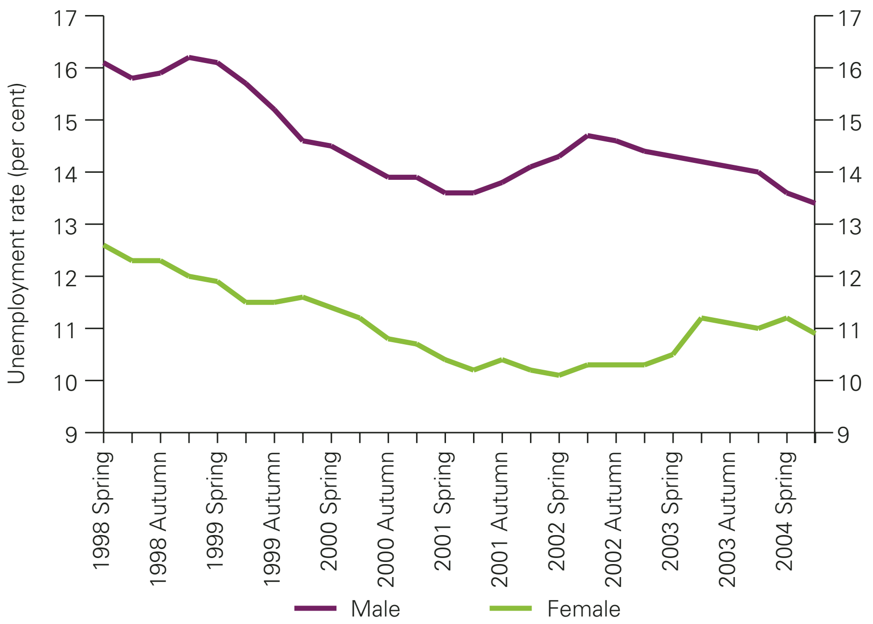
Employment Rates for 18–21 Year Olds by Gender, 1998–2004



Source: Labour Force Survey (LFS), four quarter moving average, 1998–2004.

Figure 5.2

Unemployment Rates for 18–21 Year Olds by Gender, 1998–2004

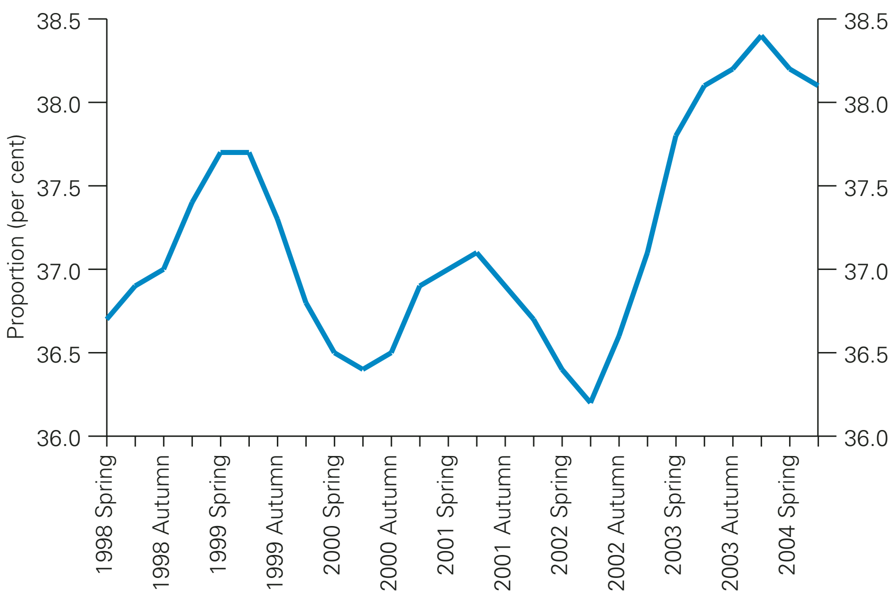


Source: LFS, four quarter moving average, 1998–2004.

5.9 To understand the dynamics of the labour market for 18–21 year olds, it is essential to look separately at those in full-time education (FTE), and those not, and to consider the impact of the changing balance between these two groups. Figure 5.3 shows that the proportion of the total age cohort in FTE is increasing slowly. This in itself would tend to have a mildly depressive effect on the trend in the employment rate, since people in FTE are less likely to be in employment.

Figure 5.3

Proportion of 18–21 Year Olds in Full-time Education, 1998–2004



Source: LFS, four quarter moving average, 1998–2004.

5.10 However over the period 2001–2004, this gradual shift towards FTE was not the dominant factor at work, since employment rates fell and then began to rise again in both the FTE and non-FTE segments. Figure 5.4 shows the employment rates for those in FTE, with falls for women between 2001–2002, and for men between 2002–2003, but with both trends now reversed. Figure 5.5 shows employment rates for those not in FTE, with the male employment rate falling between 2001–2002 and then stabilising, while the female rate fell from 2002–2003 and then stabilised.

Figure 5.4

Employment Rates for 18–21 Year Olds in Full-time Education, 1998–2004

Source: LFS, four quarter moving average, 1998–2004.

Figure 5.5

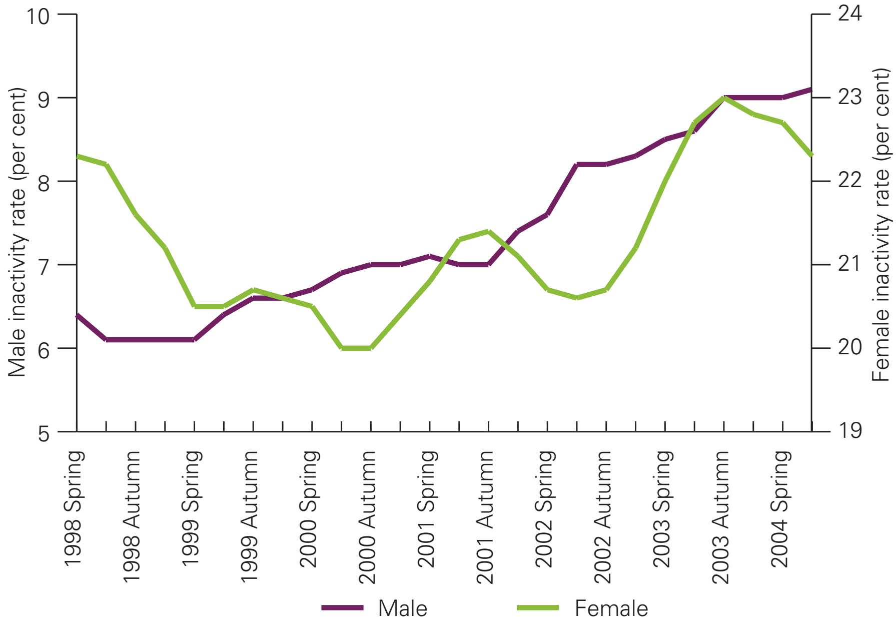
Employment Rates for 18–21 Year Olds Not in Full-time Education, 1998–2004

Source: LFS, four quarter moving average, 1998–2004.

5.11 The reasons for the oscillations are unclear. We have found no evidence that they are linked to upratings of the minimum wage. And the most sustained change occurring is not the emergence of an increasing number of young people looking for work but failing to find it, but rather a rise in the inactivity rate, with a rise in the proportion of both young men and young women who are not in FTE, not in employment, but also not looking for work. Such a rise, illustrated in Figure 5.6, is more likely to be driven by wider social factors than by a deficiency of demand for labour caused by too high a minimum wage.

Figure 5.6

Inactivity Rates for 18–21 Year Olds Not in Full-time Education, 1998–2004

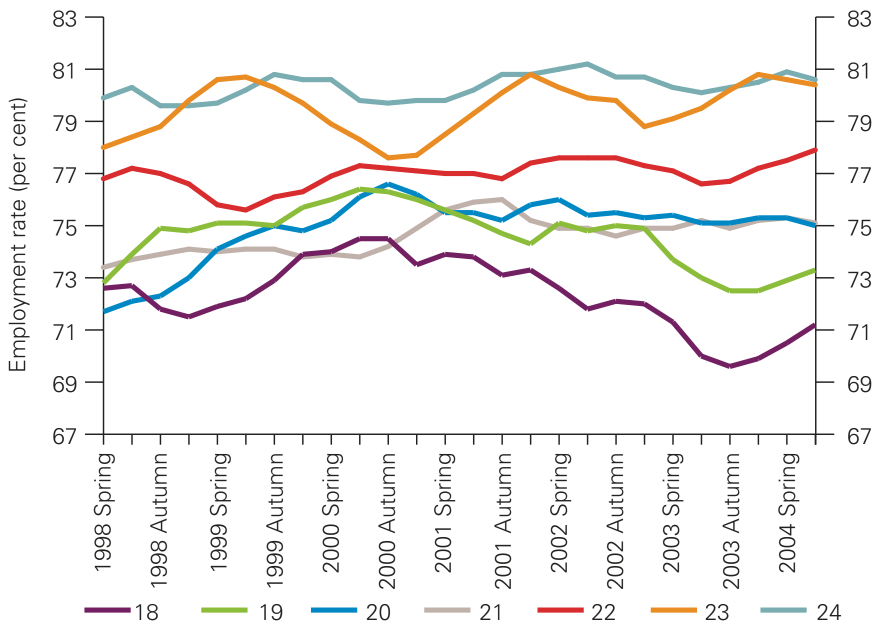


Source: LFS, four quarter moving average, 1998–2004.

5.12 Whatever the precise drivers of the trends it is clear that any concerns should be primarily focused on 18 and 19 year olds rather than slightly older age groups. As Figure 5.7 shows, the employment rate for 18 year olds not in FTE fell by 4.9 percentage points between Autumn 2000 and Autumn 2003, and that of 19 year olds by 3.8 percentage points. Among 20 and 21 year olds the changes were minimal.

Figure 5.7

Employment Rates of Young People Not in Full-time Education by Age, 1998–2004

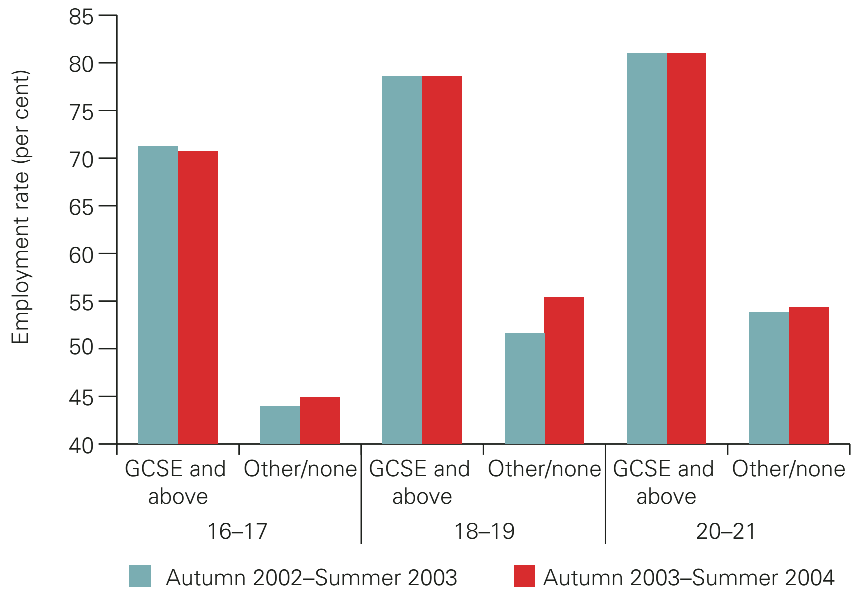


Source: LFS, four quarter moving average, 1998–2004.

5.13 If the minimum wage were harming the employment prospects of young people, we would expect most impact to occur among those with the lowest qualifications. Figure 5.8 shows that there was no change in the employment rates of 18–19 and 20–21 year olds with qualifications at GCSE level and above, but the employment rates for 18–19 year olds with no qualifications increased by 3.7 percentage points. This shows that the labour market has improved marginally for those without any qualifications, suggesting that the October 2003 upratings have not adversely affected their employment opportunities. The Figure also clearly demonstrates the higher employment rates for those with qualifications.

Figure 5.8

Employment Rates of Young People Not in Full-time Education by Qualification Level, Autumn 2002–Summer 2003 Compared with Autumn 2003–Summer 2004

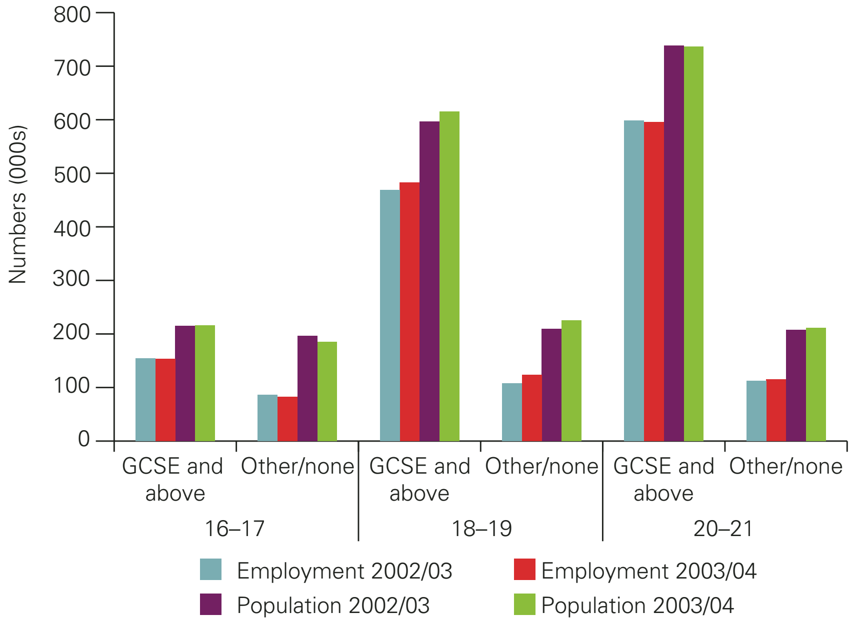


Source: LFS, averaged over Autumn–Summer quarters, 2002–2004.

5.14 Comparing the average of four quarters from Autumn 2003–Summer 2004 with the average of four quarters from Autumn 2002–Summer 2003, Figure 5.9 shows that employment levels were largely unchanged for 20–21 year olds not in FTE, but increased among their counterparts aged 18–19. Employment levels for 18–19 year olds not in FTE rose by 16,000 (mirroring the increase in population) among those with no qualifications and 14,000 (while the population increased by 18,000) for those with qualifications. Since the introduction of the minimum wage six years ago, employment levels for 18–19 year olds not in FTE have risen by 4,000 for those with no qualifications (the corresponding population increased by 11,000) and by 13,000 (the corresponding population increased by 31,000) for those with qualifications.

Figure 5.9

Employment and Population Levels of Young People Not in Full-time Education by Qualification Level, Thousands, Autumn 2002–Summer 2003 Compared with Autumn 2003–Summer 2004



Source: LFS, averaged over Autumn–Summer quarters, 2002–2004.

5.15 To summarise, since 1998 there have been slight increases in employment rates for 18–21 year olds and a fall in unemployment rates. However, in the period between Summer 2001 and Autumn 2003 there was a significant worsening in the labour market position of 18–21 year olds, particularly for those aged 18–19. The reasons for this are unclear. This decline appears to have halted since the October 2003 upratings and there is no evidence of an adverse employment effect among those with the lowest qualifications.

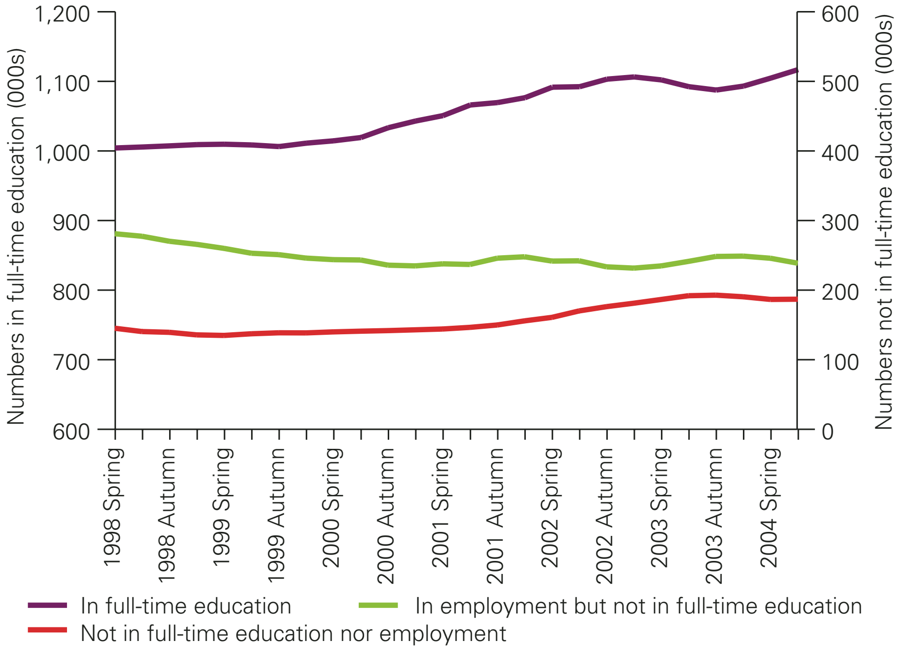
Labour Market Position of 16–17 Year Olds

5.16 The minimum wage for 16–17 year olds (above compulsory school age) was introduced in October 2004 to prevent exploitation, while neither encouraging young people out of education nor harming the supply of training jobs. It is too early to assess its impact, but in this section we consider trends in the labour market performance of 16–17 year olds.

5.17 According to the LFS, the population of 16–17 year olds fell between Spring 1998 and Winter 2000, but has since grown by around 150,000 (four quarter moving average), a rise of 10.5 per cent. Small sample sizes and proxy responses mean that data on labour market activities for 16–17 year olds need to be treated with caution, with emphasis placed more on trends over time rather than small deviations in particular years. But it can be seen from Figure 5.10 that the number of 16–17 year olds in FTE has been on an upward trend. Among those not in FTE, since Winter 2000 there has been a slight fall in the number of employed 16–17 year olds but the number not in employment has increased by just above a third (38.2 per cent for men and 31.0 per cent for women). Figure 5.11 shows that the proportion of 16–17 year olds neither in FTE nor employment has been rising, while the proportion employed but not in FTE has fallen.

Figure 5.10

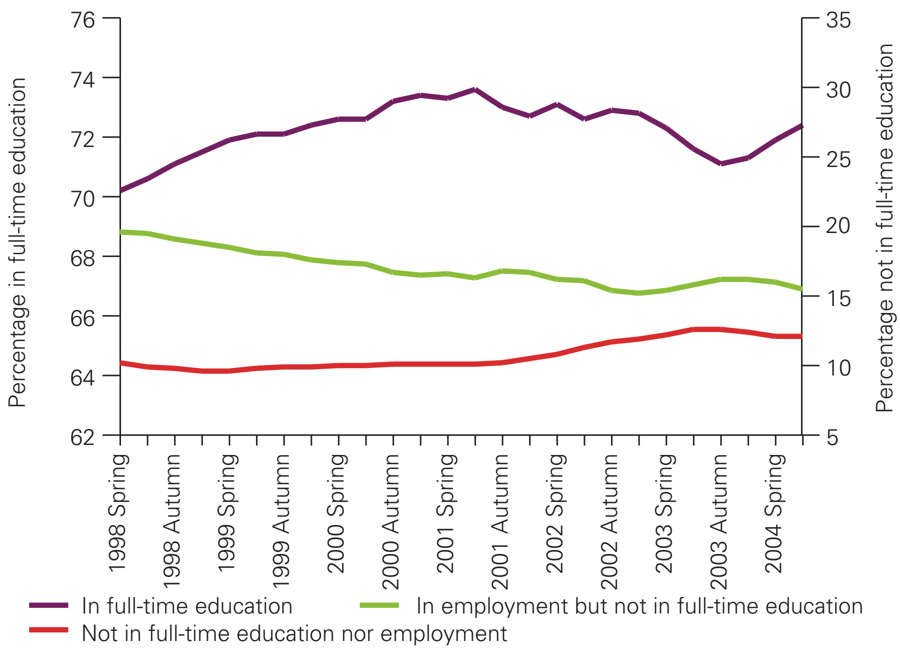
Number of 16–17 Year Olds by Education and Labour Market Status, Thousands, 1998–2004



Source: LFS, four quarter moving average, 1998–2004.

Figure 5.11

Proportion of 16–17 Year Olds by Education and Labour Market Status, 1998–2004



Source: LFS, four quarter moving average, 1998–2004.

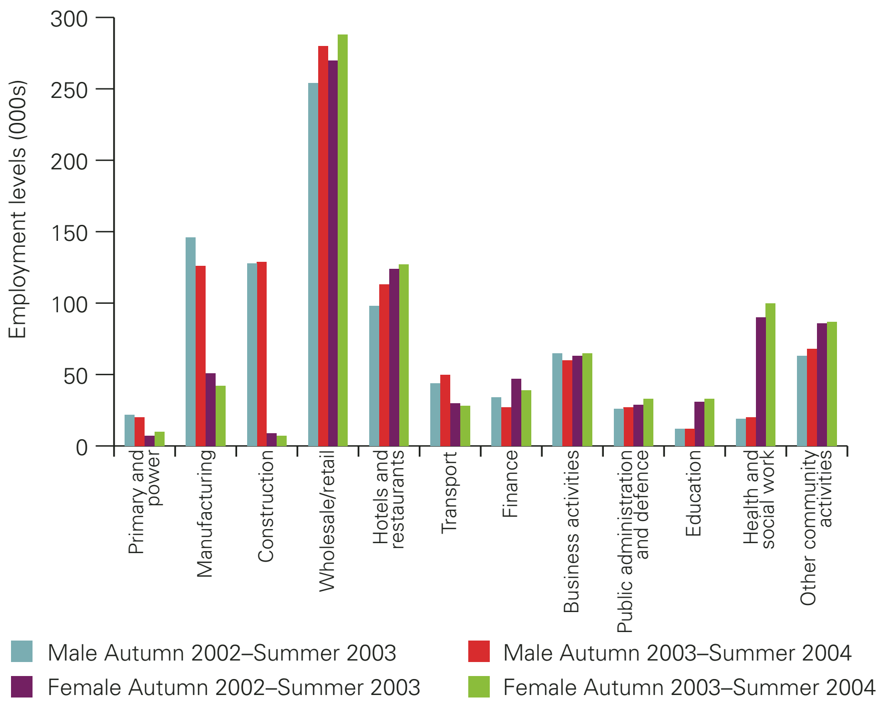
Demand for Young People

5.18 In Chapter 3 we assessed the effects of the National Minimum Wage in low-paying sectors and found that, in the year to September 2004, the overall number of employee jobs had increased in many of these sectors. In this section we consider whether these increases led to higher employment rates for young people and if there is any evidence of low-paying sectors altering their demand for young people.

5.19 Low-paying sectors are important employers of young people. About 70 per cent of employed 18–21 year old students work in retail and hospitality, attracted by the availability of work which can be fitted around their studies. Employment of 18–21 year old non-students is distributed more evenly across sectors, with 27 per cent in retail, 12 per cent in manufacturing and 10 per cent in both construction and hospitality. Figure 5.12 shows there has been an increase in the number of 18–21 year olds working in low-paying sectors such as retail and hospitality but a fall in the level of employment in manufacturing (a generally higher-paying sector). These changes are in line with general trends for the UK economy.

Figure 5.12

Employment Levels for 18–21 Year Olds by Industry Sector, Thousands, Autumn 2002–Summer 2003 Compared with Autumn 2003–Summer 2004

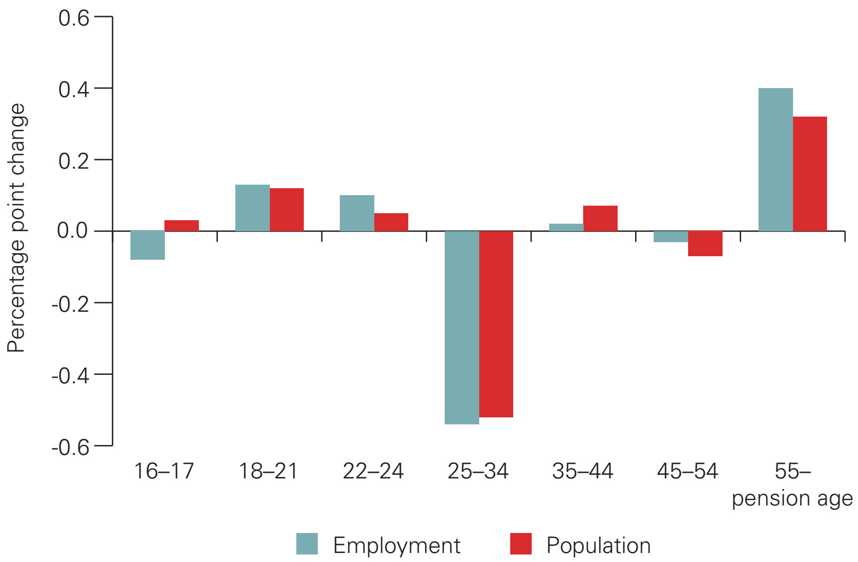


Source: LFS, averaged over Autumn–Summer quarters, 2002–2004.

5.20 It is possible that the National Minimum Wage, by changing the relative price of different types of labour, could lead firms to substitute employment either towards or away from young people. In order to determine whether there has been any such substitution effect, we examined the change in employment share by age group and compared it with the change in population share by age group. As can be seen in Figures 5.13 and 5.14, the employment data do not indicate any adverse substitution effects for 18–24 year olds either in the year to Summer 2004 or indeed since the introduction of the minimum wage.

Figure 5.13

Change in Employment and Population Share by Age, Autumn 2002–Summer 2003 Compared with Autumn 2003–Summer 2004



Source: LFS, averaged over Autumn–Summer quarters, 2002–2004.

Figure 5.14

Change in Employment and Population Share by Age, Autumn 1998–Summer 1999 Compared with Autumn 2003–Summer 2004.

Source: LFS, averaged over Autumn–Summer quarters, 1998–2004.

5.21 In our own survey of employers, the overwhelming majority of those who were affected by the October 2003 upratings reported that it had not changed the likelihood of their employing workers in different age groups. Table 5.1 shows there to be no difference in the proportion of employers who were more or less likely to employ 18–21 year olds as a result of the October 2003 upratings.

Table 5.1 Have the October 2003 Increases Made You More or Less Likely to Employ Workers in Different Age Groups?

	Percentage
Workers aged 16–17	
More likely	5
Less likely	8
No change	87
Workers aged 18–21	
More likely	7
Less likely	7
No change	86
Workers aged 22 or over	
More likely	4
Less likely	7
No change	89

Source: Low Pay Commission survey, 2004.
Base: All firms affected by the October 2003 upratings of the National Minimum Wage in any way.

‘No evidence of business substituting 18–21 year olds i.e. cheaper workers in place of adults.’

Federation of Small Businesses evidence

5.22 Commissioned research and consultation responses provide no indication that firms are responding to the minimum wage by seeking to substitute employment either towards or away from young people. Neathey, Ritchie and Silverman (2004) reported little evidence of a link between the minimum wage and decisions to employ young workers of various ages. Their case study findings ‘indicated that employment of young people is often based on pragmatic considerations such as the availability of labour. However, some employers showed a preference for slightly older workers as compared to those in the lowest age group (16–17), and were often seeking to increase the proportion of slightly older workers in their workforce.’

5.23 In summary, the decline in the labour market position of 18–21 year olds between Summer 2001 and Autumn 2003 appears to have halted. We have not observed any evidence of a substitution effect, nor of a decline in employment levels among those young people with the lowest qualifications. And the outcome of our consultation exercise supports the view that the minimum wage is more likely to have had an impact on young people’s hourly earnings than on their employment prospects.

Beneficiaries

5.24 Our 2004 report estimated that the number of jobs held by 18–21 year olds which would benefit directly from the October 2003 uprating of the youth Development Rate (i.e. those jobs where the wage needed to increase by more than the growth in average earnings or prices to comply with the minimum wage) was between 70,000 and 90,000. Between 110,000 and 130,000 jobs were forecast to benefit from the October 2004 uprating of the youth Development Rate. These estimates have proven to be reasonably accurate. We now calculate that about 70,000 jobs for those aged 18–21 (around 4.3 per cent of all jobs for this age group) directly benefited from the October 2003 uprating of the youth Development Rate, and 120,000 jobs (around 6.3 per cent of all jobs for this age group) gained from the October 2004 uprating.

5.25 Our 2004 report estimated that about 40,000 jobs would benefit from the introduction of the £3.00 per hour minimum wage for 16–17 year olds in October 2004. We now estimate that up to 45,000 jobs (7.5 per cent) benefited from the 16–17 year old rate, although this is likely to be an upper estimate given that the exemption for apprentices and those on pre-apprenticeship programmes will significantly reduce the number of beneficiaries.

Earnings

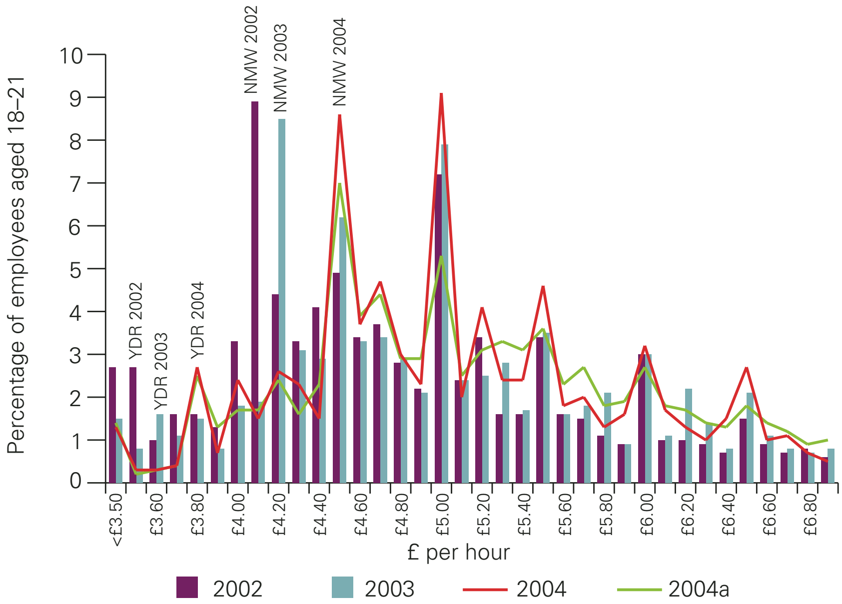
5.26 Figure 5.15 shows that 18–21 year olds also continue to benefit from upratings of the adult rate. The main peaks in the hourly earnings distribution for Spring 2004 are at the then adult rate of £4.50 per hour and a mezzanine level of £5.00 per hour. Nearly three times as many jobs for 18–21 year olds pay the adult rate as pay the youth Development Rate. According to the Annual Survey of Hours and Earnings 2004 with supplementary information (ASHE 2004a), in Spring 2004 7.0 per cent of jobs of 18–21 year olds were paid at or just above the then adult rate of £4.50, compared with just 2.5 per cent paid at or just above the then youth Development Rate of £3.80.

'Workers under 21 years old are not prepared to accept the lower level NMW (especially in London) as they feel that it does not apply to them despite having minimal experience or training. This creates barriers to employment of younger staff.'

English Community Care evidence

Figure 5.15

Hourly Earnings Distribution for Employees Aged 18–21, 2002–2004



Source: ONS central estimate methodology using ASHE and LFS without supplementary information, Spring 2002–2004. ONS ASHE with supplementary information for 2004a.

Notes:

1. Gross hourly earnings excluding overtime.
2. NMW label shows the adult NMW rate in April of the given year. YDR label shows the youth Development Rate in April of the given year.

5.27 We have indicated in previous reports that an increasing proportion of employers tend to make use of the flexibility offered by the youth Development Rate immediately following a sizeable uprating of the adult rate. The data suggest that this pattern continued following the October 2003 upratings. Table 5.2 shows that in Spring 2004 the proportion of young people's jobs paying below the adult rate increased to 16.0 per cent, compared with 14.1 per cent in Spring 2002. Conversely, the smaller October 2002 upratings had seen a reduction in the proportion of young people's jobs paid below the adult rate (11.0 per cent in Spring 2003). This includes around 35,000–45,000 (just over 2.0 per cent) earning less than the youth Development Rate. These young people may be earning below the youth Development Rate for legitimate reasons; for example, they may be serving an apprenticeship.

5.28 Table 5.3 looks at those young workers paid in April below the minimum wage rates due to be implemented later that year. As expected, coverage of those paid below the forthcoming youth Development Rate and the adult rate increases when the minimum wage upratings are higher, such as in 2001 and 2004 when around a third of all 18–21 year olds were paid below the forthcoming adult rate. The proportion falls to between a fifth and a quarter when the scheduled minimum wage upratings are smaller.

Table 5.2 Employees Aged 18–21 Earning Below the Youth Development Rate and the Adult Rate

Data year (April)	Adult rate (in April) (£)	YDR (in April) (£)	18–21 year olds earning below adult rate	18–21 year olds earning below YDR	Percentage of jobs held by 18–21 year olds paying above adult rate	Percentage earning below adult rate	Percentage earning below YDR
1999	3.60	3.00	270,000	37,000	82.8	17.2	2.4
2000	3.60	3.00	173,000	34,000	89.3	10.7	2.1
2001	3.70	3.20	164,000	37,000	90.4	9.6	2.1
2002	4.10	3.50	245,000	46,000	85.9	14.1	2.7
2003	4.20	3.60	186,000	38,000	89.0	11.0	2.3
2004	4.50	3.80	262,000	38,000	84.0	16.0	2.3
2004a	4.50	3.80	297,000	45,000	84.1	15.9	2.4

Source: ONS central estimates using ASHE and LFS for 1999–2004. Estimates using ASHE with supplementary information for 2004a.
Note: YDR = Youth Development Rate.

Table 5.3 Employees Aged 18–21 Earning Below the Forthcoming Youth Development Rate and the Adult Rate

Data year (April)	Forthcoming adult rate (October)	Forthcoming YDR (October)	Jobs held by 18–21 year olds earning below new adult rate	Jobs held by 18–21 year olds earning below new YDR	Percentage of jobs held by 18–21 year olds paying above new adult rate	Percentage of jobs held by 18–21 year olds paying below new adult rate	Percentage of jobs held by 18–21 year olds paying below new YDR
1999	3.60	3.00	270,000	37,000	82.8	17.2	2.4
2000	3.70	3.20	315,000	84,000	80.4	19.6	5.2
2001	4.10	3.50	513,000	97,000	70.0	30.0	5.6
2002	4.20	3.60	400,000	93,000	76.9	23.0	2.7
2003	4.50	3.80	431,000	84,000	74.5	25.1	5.0
2004	4.85	4.10	572,000	68,000	65.1	34.9	6.2
2004a	4.85	4.10	531,000	148,000	71.5	28.6	7.9

Source: ONS central estimates using ASHE and LFS for 1999–2004. Estimates using ASHE with supplementary information for 2004a.
Note: YDR = Youth Development Rate.

5.29 Table 5.4 shows that lowest decile hourly earnings rise with age, which reflects the level of skills and experience and the fact that young people are disproportionately represented in low-paying sectors. In April 2004 the lowest decile hourly earnings for 18 and 19 year olds were £3.85 and £4.18 per hour respectively, compared with £4.45 per hour for 20 year olds, £4.50 per hour for 21 year olds and £4.75 per hour for 22 year olds. Between 2003 and 2004 there was a slight widening in the lowest decile hourly earnings of 21 and 22 year olds, perhaps reflecting a greater use of paying adult rates from the age of 22.

Table 5.4 Gross Hourly Earnings (Excluding Overtime) for Young People by Age, 2002–2004

Age	Lowest decile			Lowest quartile			Median		
	2002	2003	2004	2002	2003	2004	2002	2003	2004
16	£3.00	£2.60	£3.11	£3.50	£3.40	£3.70	£3.84	£3.99	£4.04
17	£3.12	£3.06	£3.41	£3.57	£3.60	£3.81	£4.08	£4.20	£4.28
18	£3.58	£3.60	£3.85	£4.09	£4.20	£4.35	£4.50	£4.70	£4.82
19	£3.88	£4.00	£4.18	£4.20	£4.43	£4.60	£4.81	£5.10	£5.21
20	£4.07	£4.20	£4.45	£4.41	£4.58	£4.77	£5.13	£5.38	£5.50
21	£4.12	£4.32	£4.50	£4.68	£4.88	£5.02	£5.51	£5.77	£5.98
22	£4.29	£4.50	£4.75	£5.00	£5.17	£5.41	£6.20	£6.35	£6.50

Source: ASHE, 2002–2004 without supplementary information.

5.30 In summary, we have seen that the October 2003 uprating of the youth Development Rate directly benefited about 70,000 jobs held by 18–21 year olds, and this number increased to 120,000 following the October 2004 uprating. A maximum of 45,000 jobs directly benefited from the introduction of the 16–17 year old rate in October 2004. In addition, many young people also gained from the uprating of the adult rate. However an increased proportion of jobs held by 18–21 year olds was paid below the adult rate following the October 2003 upratings. The reasons for this increase are considered in more detail in the next section.

‘It is clear that some companies have used NMW age rates as a justification for re-introducing age rates, against the long-term trend towards their decline, in order to reduce costs. However, we are continuing to negotiate them out of our collective agreements, using arguments around equity and recruitment and retention.’

GMB evidence

Age-related Pay

5.31 On 12 October 2004 the Government asked the Low Pay Commission to investigate whether there was any evidence of an increase in employers paying lower rates to 18–21 year olds, and to provide an economic explanation for any such change. This followed concern expressed by a number of trade unions that some employers were increasingly paying workers aged 18 to 21 lower rates than adults aged 22 and above.

5.32 Evidence from trade unions and youth organisations about employers introducing or re-introducing age-related pay largely referred to findings from Incomes Data Services (IDS). Research we commissioned from IDS (2004a and 2004b) highlighted diverse approaches to age-related pay in response to minimum wage upratings. IDS found that a number of companies had abolished age-related pay entirely (typically firms that cater for younger customers, such as fashion retailers). They also found that, increasingly, rates for workers aged under 18 had been combined into a single junior rate for the grade. But IDS also observed that the fast food industry, nurseries and some pubs and restaurants in particular were moving in the opposite direction. Most of the organisations introducing age-related pay said they had changed their practices specifically as a result of the minimum wage legislation. But such firms also needed to ensure that staff recruitment was not jeopardised and IDS commented that some of the same companies relaxed their policy of age-related pay in harder-to-recruit locations.

5.33 In our latest survey a fifth of respondents reported using age-related pay, with use most common in the hospitality, retail and hairdressing sectors. Although the results are not directly comparable, this is 2 percentage points higher than in the 2002 survey. The most common reasons given were to take account of employees' level of experience and the National Minimum Wage (cited by 71 and 55 per cent of firms respectively). There is some evidence to suggest that firms using age-related pay are raising the age threshold for paying their adult rates to 22 – 6 per cent of firms responding to the 2004 survey reported having age-related pay structures with adult rates starting at age 22, compared with 4 per cent of firms responding to the 2002 survey. Questions about the use of age-related pay are open to interpretation and so firms were also asked about the age from which workers were entitled to adult rates. Just over half the firms that provided information reported paying their adult rates from the age of 18 or below, with 78 per cent paying from age 21 or younger.

5.34 Our survey is likely to provide an upper estimate of the use of age-related pay, since we targeted the sectors most likely to be affected by the minimum wage and respondents are more likely to have been significantly affected than non-respondents. The Greater Manchester Low Pay Unit's (GMLPU) annual survey (2003) of job vacancies and rates of pay in Greater Manchester Jobcentres indicates a much lower use of age-related pay. GMLPU found that only 1.6 per cent of 7,280 vacancies surveyed in April 2003 gave age-related rates, with about half of these paying the adult rate from the age of 22. The GMLPU 2002 survey found that 4.3 per cent of vacancies gave age-related rates.

5.35 We commissioned IDS (2005a) to conduct a small research project on the changing use of age-related pay since the introduction of the minimum wage, including investigation of the reasons for introducing any changes and the manner in which changes were implemented. The report focuses on 31 employers – 21 companies and 10 industry agreements – all of whom had used age-related pay for 18–21 year olds at some point since 1999. It did not consider 16–17 year olds since the minimum wage for this age group was only introduced in October 2004.

5.36 The report emphasised that age-related pay was not widespread, particularly for those aged 18 and over. Even in the minority of companies using age-related pay, IDS (2005a) state that 'it is often just for the lowest-paid job in the company, the minimum or recruitment rate that is not in widespread use, or just for new recruits in the first few months of employment'. There was also no clear trend in the use of age-related pay. In the sample of 31 employers with age-related pay between 1999 and 2004, eight employers raised the age at which adult rates were paid (including one which subsequently reversed the policy) and six employers lowered the age at which adult rates were paid. Among the eight employers who raised the age threshold for paying adult rates, seven took it up to age 22 and the other to age 21, before lowering it again.

'Recent research would indicate that the NMW may have served to institutionalise 22 as the threshold for payment of full adult rates of pay, so that younger workers (particularly those aged 21) in some firms are no longer treated as adults for pay purposes, even though in the past this would have been the case.'

Institute for Employment Studies evidence

5.37 IDS found that 'every case of raising the age for adult rates was part of a move to offset the cost of meeting the minimum wage'. This approach was common among fast food employers, which are large-scale employers of young people. A number of companies concerned about the cost of minimum wage upratings have re-examined their pay structures and questioned the case for paying adult rates from the age of 18. Where companies have concluded that the threshold for paying adult rates should be increased, IDS report that 'typically, employees aged 22 and over received the increase necessary to take them to the new NMW while younger employees received lower increases or a pay freeze'.

5.38 IDS found that the reasons for lowering the age threshold for paying adult rates were more varied, with employers citing a number of issues. The main factors highlighted were: as a result of a general review of the pay system; because the previous system was considered anomalous or unfair; to make the company more competitive in the labour market; and to reward staff skills and contributions effectively. There was little evidence on the impact of reducing the age threshold, although one employer reported a marked reduction in staff turnover after an overhaul of the pay system that included removing age-related pay for the over 18s.

5.39 The earnings data considered earlier in the Chapter show that the number of young people's jobs being paid below the adult rate of the minimum wage increases after large upratings. Table 5.5 demonstrates that this applies to both young men and young women, but in general young women are more likely to be paid below the adult rate of the minimum wage than young men.

Table 5.5 Employees Aged 18–21 Earning Below the Adult Rate

Data year (April)	Adult rate (in April) £	Percentage earning below adult rate	Percentage of young men earning below adult rate	Percentage of young women earning below adult rate
1999	£3.60	17.2	16.6	17.8
2000	£3.60	10.7	9.9	11.5
2001	£3.70	9.6	8.2	10.9
2002	£4.10	14.1	12.3	16.1
2003	£4.20	11.0	10.7	11.4
2004	£4.50	16.0	14.9	17.1

Source: ASHE, 1999–2004 without supplementary information.

5.40 The earnings data suggest that an increasing proportion of employers make use of the flexibility offered by the youth Development Rate following a sizeable uprating of the adult rate. This is supported by research, which indicates that a number of fast food restaurants, nurseries and some pubs and restaurants have introduced age-related pay to help offset the cost of minimum wage upratings. Consultation also highlighted the possibility that use of the youth Development Rate will increase following further upratings of the adult minimum wage. But even so, the use of age-related pay is not widespread and, even in the minority of companies where it does apply, its use is often limited to particular jobs or as an induction rate. Conversely, some firms are still lowering the threshold for paying their adult rates, largely for reasons of equity and to be more competitive in the labour market.

5.41 The introduction of the minimum wage has affected the previous general move away from the use of age-related pay. Where age-related pay exists, it has also resulted in age 22 being increasingly established as the threshold for payment of full adult rates of pay, whereas previously lower ages tended to be used. It is therefore important that the youth Development Rate only applies to those who need its coverage and we consider this issue in the next section.

‘Whilst it is not something that the industry would undertake of its own volition, the evidence clearly shows that future large increases would force retailers to place their 18–21 year old employees on the development rate, utilising this valuable flexibility in coping with NMW increases.’

British Retail Consortium evidence

Role of the Youth Development Rate

5.42 Trade unions and youth organisations continue to argue strongly against a lower rate for 18–21 year olds, and some also urge that the adult rate be paid from the age of 16. They view the youth Development Rate as discriminatory and stress that workers should be paid equally for work of equal value. Several organisations proposed that age rates should gradually be removed from the minimum wage structure and replaced by a Development Rate linked to accredited training.

‘Workers should be paid equally for work of equal value. A lower rate should only apply to those on fully accredited training rather than being justified solely on the grounds of their age.’

Coalition of Youth Organisations evidence

5.43 Employers’ associations remain overwhelmingly supportive of the youth Development Rate. For example, the CBI wrote that the youth Development Rate was an accepted tool to maintain higher levels of employment partly to make up for lower productivity among younger and inexperienced workers. The British Retail Consortium highlighted the flexibility that the youth Development Rate offered retailers and the Association of Licensed Multiple Retailers commented that it provided members with an incentive to embark on training in-house rather than simply recruiting those with existing skills.

5.44 A number of employer organisations remarked that the tight labour market has increased demand for young people and resulted in higher wages to attract staff. Nevertheless unemployment rates for young people not in FTE remain high. In our view the data on lowest decile hourly earnings and unemployment rates for young people not in FTE, combined with international evidence on the impact of minimum wages on youth employment, continue to demonstrate the need to ensure that young people – particularly those with few or no qualifications – are not priced out of the labour market. The arguments for the youth Development Rate would be even stronger in the event of an economic downturn.

Low Pay Commission Research

One hotel commented that they would be more likely to develop staff below 20 years of age internally, but would prefer to buy in skills of people over 20 years of age. The reason for this being that if they were to recruit a young person over 20 years old then they must have experience to warrant their higher wage costs.

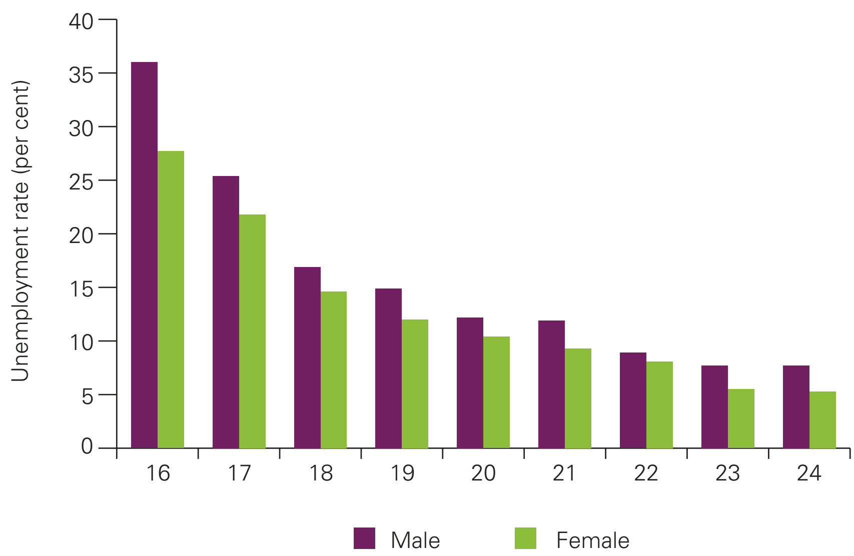
Neathey, Ritchie and Silverman, (2004). *Employment of Young People in Retail and Hospitality*

5.45 The existence of the youth Development Rate also permits a higher level of the adult rate, with the alternative being a single lower rate for all ages. Our previous reports have recognised the argument that the youth Development Rate lacks equity, but in our view a lower rate plays an essential part in assisting young people to gain experience of work, receive coaching and develop workplace skills. We also noted in our fourth report (2003) that the conditions were not in place to enable use of the youth Development Rate to be conditional on accredited training, without creating a risk to youth employment. Employers would be less willing to take on young workers if they had to either provide accredited training or pay the adult rate.

5.46 Some respondents queried whether the youth Development Rate is compatible with the Equal Treatment Directive (2000/78/EC) due to be implemented in the UK from October 2006. The Directive will make age discrimination in employment and vocational training unlawful unless, within the context of national law, it is objectively justified by a legitimate aim (including employment policy) and is an appropriate and necessary means of achieving that aim. The Department of Trade and Industry’s consultation document *Equality and Diversity: Age Matters* (2003) made clear the Government’s view that the National Minimum Wage was objectively justified in the terms of the Directive, and that is also the Commission's point of view. We are strongly convinced there is a need for a youth Development Rate which is lower than the adult rate and that adverse consequences for the employment rate of young people would result if employers were not able to pay some young people below the adult minimum wage level.

5.47 It is, however, important that the youth Development Rate should only apply to those age groups where the dangers of adverse employment effects exist. Figure 5.16 shows that unemployment rates are significantly higher for 18 and 19 year olds compared with 20 year olds and above, and Figure 5.7 showed that the adverse trends in employment between 2001 and 2003 were concentrated among the 18 and 19 year olds. There is therefore a very strong case for a lower youth rate for 18 and 19 year olds. Above that level, the precise optimal cut-off point can be debated. On the basis of the employment and unemployment rate data, arguments could be made for any one of the 20th, 21st or (as now) 22nd birthday.

Figure 5.16
Unemployment Rates of Young People Not in Full-time Education by Age and Gender, Autumn 2003–Summer 2004



Source: LFS, averaged over Autumn–Summer quarters, 2003–2004.

5.48 Our judgement is that the 21st birthday is the most appropriate, and that the employment prospects of 21 year olds do not need to be protected by the youth Development Rate. In April 2004, lowest decile hourly earnings for 21 year olds were at the same level as the adult rate of the minimum wage. Of all the organisations which gave evidence, only the hairdressing sector opposed entitling 21 year olds to the adult rate. Firms' wage-setting behaviour shows that paying the adult rate from the age of 21 would have limited impact on business. Latest ONS data show that in Spring 2004 around 40,000 21 year olds were paid less

'The youth Development Rate is important not just to give employers a chance to train workers in the skills they need, but also to overcome the initial problems young employees may face simply adjusting to the world of work.... The youth Development Rate has continued to be an important tool in companies' employment strategies, and one which may become more important as the adult rate increases.'

CBI evidence

than £4.50 per hour (6.7 per cent of men and 8.8 per cent of women), and some of these are likely to be apprentices or in receipt of accommodation. **We therefore again recommend that 21 year olds should receive the adult rate of the National Minimum Wage.**

Trainees

5.49 In our previous reports we have consistently stressed the importance of training. Our initial reports expressed the hope that the minimum wage would encourage firms to increase their support for training and workforce development. However, in practice we found that the minimum wage plays a limited role compared with the many other factors (particularly Government initiatives to promote workforce development) that determines firms' training strategies. The minimum wage can act as a spur to encourage some firms to train their workers as a way to improve efficiency. And it is also important that the minimum wage does not reduce the provision of training. In this section we look at the impact of two minimum wage rules designed to provide some recognition of the costs of training, namely the older workers' Development Rate and the exemption for apprentices.

5.50 The older workers' Development Rate applies to workers aged 22 and over starting a new job with a new employer and doing accredited training on at least 26 days during the first six months of the employment. Our first report (1998) recommended its creation to provide an incentive for employers to train new staff, but subsequent reports have found that uptake has been low. Evidence suggested there was little awareness of its existence and that the complexity and costs associated with operating accredited training schemes also deterred use. Volume Two of our third report (2001) stated that there might be a case for abolition if low take-up continued, but we needed a longer period before we could provide advice. In the fourth report (2003) we decided, on balance, to advise retention of the older workers' Development Rate for the time being, noting that some firms found it a helpful support to adjust to the minimum wage.

5.51 Use of the older workers' Development Rate remains very low. Our survey found it was employed by only 4 per cent of respondents, with use greatest in the hairdressing (10 per cent of firms) and childcare (5 per cent of firms) sectors. The CBI Employment Trends Survey 2004 found that, among those firms who reported that they would feel an impact from the October 2004 uprating, only 2 per cent were planning to make more use of the older workers' Development Rate. Research commissioned from IDS (2004b) on the impact of the October 2003 uprating stated 'there was no reported use of the adult Development Rate ... which suggests that either employers do not understand the criteria for this, or are unable to meet it'. Cronin and Thewlis (2004) conducted interviews with 53 firms on adjustments to the minimum wage and found only one company using the older workers' Development Rate – a recruitment, travel and training company (with a specific human resource function).

5.52 During consultation only the CBI and the Association of Licensed Multiple Retailers explicitly supported retention of the older workers' Development Rate. The CBI suggested that the older workers' Development Rate provided companies with much-needed flexibility and that use would increase if the minimum wage rose significantly. Other organisations – including employer and training organisations – believe there is little likelihood of greater uptake. It was suggested that employers were reluctant to offer lower rates of pay to mature staff undergoing training and that there were few opportunities to meet the requirements outside of apprenticeships. Representatives from the National Association of Master Bakers, the National Hairdressers Federation and the Hairdressing Employers' Association told us that extending the 12 month apprenticeship exemption to cover those aged 26 and over would provide a greater incentive to train older workers than the older workers' Development Rate. Similar views were expressed by a number of trade associations during our visit to Scotland.

'Some companies would like to make use of the rate but the six-month reference period is too short to allow an employee to become fully trained. Companies may prefer to recruit an apprentice where employees are exempt for the first 12 months.'

CBI evidence

5.53 The second minimum wage provision intended to support the provision of training is the exemption for apprentices. Currently apprentices are exempt from the minimum wage if they are under age 19, or under age 26 and in the first 12 months of their apprenticeship. For the purposes of the minimum wage, apprentices are workers who either have contracts of apprenticeship or are taking part in specified Government training programmes.

5.54 Prior to the introduction of the 16–17 year old rate, apprentices below age 26 were effectively exempt for the first 12 months when the minimum wage would otherwise apply. We recommended in our 2004 report that the exemption from the minimum wage for apprentices aged under 19 should be retained and were pleased that the Government accepted our recommendation. This means that people starting an apprenticeship aged 16–17 can be exempt from the minimum wage for longer than 12 months.

5.55 During consultation we received a range of views regarding the future treatment of apprentices. The National Hairdressers Federation and Hairdressing Employers' Association believe that the current exemption period is too short and recommended that consideration be given to exempting workers (regardless of age) from the minimum wage for the duration of their apprenticeship or accredited training. The Trades Union Congress and the Transport and General Workers Union suggested that we should review the exemptions for apprentices and other forms of accredited training in an interim report next year and consider whether they were still warranted. The Scottish Low Pay Unit and the joint submission from UNISON and YMCA England proposed that the exemptions for apprentices should be abolished, primarily on the basis that the current rules could be abused and that low wages for apprentices contributed to low completion rates.

5.56 In recent years there have been a number of developments relating to apprenticeships. In May 2004 reforms to the apprenticeship system in England were announced. The changes include replacing Foundation Modern Apprenticeships and Advanced Modern Apprenticeships with 'Apprenticeships' (level 2) and 'Advanced Apprenticeships' (level 3) respectively, and planning to open up apprenticeships to adults by removing the arbitrary 25 year old age limit. In March 2004 the Government announced plans for the HM Treasury, the Department for Education and Skills and the Learning and Skills Council to work with employers in England to achieve a minimum level for trainee pay in the range of £70–£80 per week. Subsequently the Learning and Skills Council (2004) recommended to work-based learning providers that employed learners should receive at least £70 a week on starting work-based learning, with incremental rises based on competence, achievement and productivity. From August 2005 it will become a contractual requirement on providers to ensure that all learners receive at least £80 per week. In Scotland and Wales the requirement for starters to be aged under 25 has already been abolished, although funding continues to be prioritised for 16–17 year olds.

5.57 We believe that the current exemption for apprentices is generally working well. We note that some concern has been raised about reported examples of employers classifying their workers as apprentices but not providing any training. In our view such cases should be addressed through enforcement. Many firms use the current exemption and it is clear to us that without it the provision of training would be reduced in some sectors, particularly hairdressing.

5.58 Our 2004 report recommended that apprentices aged under 19 should be exempt from the minimum wage on the basis of current pay arrangements for younger apprentices and the fact that many 16–17 year old apprentices are still working towards level 2 rather than more advanced qualifications. It is too early to assess whether the introduction of the minimum wage for 16–17 year olds (above compulsory school age) has affected training opportunities for this age group, and we therefore believe that the exemption from the minimum wage for apprentices aged below 19 should be retained.

5.59 We understand that the Government believes that the exemption from the minimum wage for apprentices under age 19 is compatible with the Equal Treatment Directive (2000/78/EC). We agree but the same may not be true of the current age 26 cut-off for the 12 months exemption from the minimum wage. The minimum wage was introduced at a time when Government apprenticeship programmes were only available to those below the age of 25. Accordingly, the National Minimum Wage Regulations 1999 provide that the 12 months exemption from the minimum wage only applies to those below the age of 26. The original age limit for undertaking apprenticeships was somewhat arbitrary (driven by EU funding) and has since been abolished in Scotland and Wales. In addition, the Learning and Skills Council has provided for adult apprenticeships to be piloted in England from January 2005 and the upper age limit for apprentices in Northern Ireland is to be reviewed.

5.60 We are unaware of any grounds to justify objectively the retention of the requirement for apprentices to be aged below 26 for the 12 months exemption from the minimum wage to apply. But there continues to be a need to exempt apprentices in their first year of employment from the minimum wage to take account of their lower productivity. We therefore consider that all apprentices aged 19 and over in the first 12 months of employment should be exempt from the minimum wage. This would benefit those seeking to return to the labour market, particularly those wishing to retrain in a new career. Such a change would also further reduce the case for retaining the little used older workers' Development Rate. It would therefore be logical to abolish the older workers' Development Rate at the same time as extending the 12 months exemption from the minimum wage to all apprentices aged 19 and over. However, before taking a final decision it would be appropriate to wait a year and consider the emerging results of the Learning and Skills Council's pilot of adult apprenticeships. **Our provisional conclusion is that the older workers' Development Rate should be abolished**

from October 2006, and that, simultaneously, the 12 months exemption from the minimum wage should be extended to cover all apprentices aged 19 and over. We recommend that the Government invite the Commission to review these provisional conclusions and make firm recommendations on these matters by February 2006.

Conclusion

5.61 The number of jobs held by 18–21 year olds that benefited from the youth Development Rate increased from 70,000 to 120,000 following the October 2004 uprating. In addition, many more young people gained from the uprating of the adult rate. In the year to Summer 2004 there was little change in the employment position of 18–21 year olds, but this followed a two-year period where the labour market position of 18–21 year olds worsened, particularly for those aged 18–19. We found no evidence, however, that the period of declining employment rates could be explained by the minimum wage.

5.62 We have again recommended that 21 year olds should receive the adult rate of the National Minimum Wage. We have also provisionally concluded that the older workers' Development Rate should be abolished from October 2006 and that, simultaneously, the 12 months exemption from the minimum wage should be extended to cover all apprentices aged 19 and over. We wish to make firm recommendations on the training provisions by February 2006.

5.63 Some of the concern relating to the training provisions stems from low awareness of the rules and the fear that the exemption for apprentices can be abused if the rules are not enforced effectively. In the next Chapter we look at compliance and enforcement of the minimum wage and consider the developments that have taken place to increase awareness and tackle areas of non-compliance.

Compliance and Enforcement

Effective enforcement of the National Minimum Wage is crucial to its success. As recognised in our previous reports, the vast majority of employers support and comply with the minimum wage. But we continue to be concerned that a minority of workers are still being underpaid. The Inland Revenue has continued to develop and focus its minimum wage enforcement activities in the light of its experience since the introduction of the minimum wage in 1999. Since our fourth report (2003) the Department of Trade and Industry has taken action to address some legislative anomalies that have arisen and which impeded effective enforcement. We welcome the work that has been done by both Departments, but we believe that more could be done to tackle persistent non-compliant employers and to encourage more workers to report underpayment so that they can receive the pay due to them.

Reviewing the evidence, we are concerned that awareness of the minimum wage remains low in some groups of vulnerable workers. To tackle this, we recommend that the Government review its minimum wage publicity strategy to consider how best to target low-paid workers, with particular emphasis on vulnerable groups of workers.

We also now believe that a more significant deterrent to non-compliance by employers is needed. We therefore recommend that the Government should introduce interest charges payable on arrears arising from minimum wage underpayment and financial penalties for seriously non-compliant employers.

Introduction

6.1 In our fourth report (2003) we concluded that the vast majority of employers were complying with the National Minimum Wage, but we also highlighted our concern that some workers were still being underpaid, particularly, though not exclusively, in the informal economy.

6.2 For this report we have again examined closely how well the minimum wage is being complied with and how effectively it is being enforced. Our work has been informed by an internal evaluation of enforcement powers carried out by the Inland Revenue. We invited organisations and individuals to address compliance and enforcement in their written and oral evidence to us and we have asked about it in our visits. In this Chapter we consider in turn: awareness of the minimum wage, non-compliance, progress in enforcement, employment tribunals, detriment and dismissal related to the minimum wage, the informal sector and the Inland Revenue's evaluation of enforcement powers.

Awareness

6.3 From the outset, we have taken the view that the minimum wage should be self-enforcing as far as possible and to date this approach has largely been effective. Awareness of the minimum wage among all affected groups is therefore essential. In our fourth report (2003), we were encouraged that awareness of the minimum wage continued to be at a high level. However, we noted that awareness among small firms could be improved and that lower awareness persisted among some groups of workers. We recommended that the Government should continue to publicise the minimum wage, including the headline rate and the Helpline, and that publicity should be targeted at different groups. We also recommended that the Small Business Service (SBS) actively promote and disseminate factual information on the minimum wage tailored to small firms.

6.4 In our 2004 report, which largely focused on a minimum wage for 16 and 17 year olds, we recommended that consideration be given to the use of specific channels to promote awareness among young people of both the minimum wage and mechanisms for enforcement.

6.5 In response, the Government has carried out nationwide publicity campaigns for the last two minimum wage upratings, including adverts aimed at specific groups. It also mounted a campaign designed to appeal specifically to 16–17 year olds to coincide with the introduction of the new rate for this age group.

6.6 In 2004 the SBS published an updated version of its guide to employing staff which included the new 2004 rates and sources of further information. Its website also includes a dedicated section on paying staff which includes the new minimum wage rates and gives links to other related sites.

6.7 Other steps the Government has reported taking to heighten awareness of the minimum wage include producing a new guide for output workers and their employers explaining the new fair piece rates legislation; updating the short guides aimed at employers, adult and young workers; updating the detailed guide to the minimum wage; and the inclusion of information about the minimum wage rate changes and the Helpline in the Inland Revenue's employer bulletins (which reach 1.5 million tax-registered employers).

6.8 We welcome the action that the Government has taken to publicise the minimum wage and the Helpline since our fourth report (2003). However, our consultation has highlighted that, although general awareness of the minimum wage is high, awareness of the rates is less so. Moreover, it seems clear that publicity on the 16–17 year old rate has not widely reached its target audience. The coalition of youth organisations' survey in September 2004 found that nearly two-thirds of respondents were unaware of the introduction of a minimum wage for 16–17 year olds in October 2004 and nearly 90 per cent of respondents did not know the rate.

6.9 We are particularly concerned that awareness of the minimum wage is lower within some of the most vulnerable groups of low-paid workers, particularly homeworkers and workers from some minority ethnic groups. The level of awareness needs to be raised further within these groups of workers. **We therefore recommend that the Government undertake a review of its minimum wage publicity strategy to consider how best to target low-paid workers more pro-actively, with particular emphasis on vulnerable groups of workers.**

Low Pay Commission Research

Awareness of the existence of the minimum wage was generally good among a majority of our worker respondents. The most common source of information was through family, friends or neighbours. Even where workers were aware of the existence of the NMW, however, they were not always clear about the detail of the wage nor their eligibility.

Croucher and White, 2004. *Enforcing the Minimum Wage: The Experience of Workers and Employers*

Non-compliance

6.10 The Office for National Statistics estimates that the number of jobs paid below the minimum wage was 272,000 in April 2004. However, this estimate is based on the Annual Survey of Hours and Earnings which is not designed to monitor compliance with the minimum wage. The survey cannot separately identify workers such as apprentices, those undergoing training and those workers eligible for the accommodation offset, all of whom may legally be paid less than the minimum wage. In order to assess the level of non-compliance we have therefore turned to a variety of other information sources, including Inland Revenue statistics, written and oral evidence and our own commissioned research.

6.11 The Government's evidence provides details of the work of the Inland Revenue's minimum wage team. Table 6.1 shows that the number of complaint cases generated from its Helpline remained relatively constant between 2001/02 and 2003/04. The amount of arrears decreased in 2002/03 and 2003/04 from the high of 2001/02, but the variation can be explained by the impact of a small number of large cases. If these large cases are removed, the annual arrears do not differ greatly between the years. Between April and September 2004, there were five large cases with arrears totalling £1 million. The incidence of non-compliance found in investigations arising from complaints continues to be high (40 per cent in 2003/04).

Table 6.1 National Minimum Wage: Enquiries and Complaints to the Inland Revenue and Enforcement Action Taken

	2001/02	2002/03	2003/04	April to September 2004
Enquiries received by the Helpline	79,186	53,676	53,226	26,371
Complaints of underpayment	1,813	1,996	1,969	843
Visits to employers (see note)	4,288	5,363	4,919	2,246
Enforcement notices issued	86	26	45	32
Penalty notices issued	65	6	3	0
Value of underpayments identified	£5.1 million	£3.6 million	£2.5 million	£2.1 million

Source: Department of Trade and Industry, Inland Revenue.
Note: These figures are for the number of cases closed with an inspection having been made.

‘A ‘name and shame’ policy should be adopted towards employers who are found to be in breach of national minimum wage legislation.’

T&G evidence

6.12 In 2003/04 compliance teams completed over 5,500 investigations. The number of investigations arising from information gathered from the Inland Revenue Tax Credit Office has increased since the introduction of tax credits in 2000. In 2003/04 they accounted for 53 per cent of all completed investigations, although the proportion of arrears identified in relation to the total in that year was 36 per cent.

6.13 However, this information presents only part of the picture as we do not know the extent of undetected non-compliance. Evidence given to us suggests that the vast majority of employers are compliant, and that the Inland Revenue is making good progress in tackling those employers not paying the minimum wage. A number of organisations did, however, highlight their concern that to date, no prosecution cases for non-compliance have been brought by the Inland Revenue.

6.14 We commissioned research from Croucher and White (2004) to investigate the experiences and perceptions of workers and employers who had been through the minimum wage enforcement process. The findings suggest that the reasons for non-compliance are numerous. In some cases, employers were clearly not aware of how the rates worked. In others, there was evidence that monitoring systems were inadequate so that when workers crossed age thresholds and became eligible for the adult minimum wage rate, they were not identified. Cases where workers were paid for a fixed number of hours when in fact they worked for longer than those hours was another identifiable reason for non-compliance.

6.15 Although progress in tackling non-compliance has undoubtedly been made, we must not be complacent. A number of organisations have expressed concern that minimum wage underpayment continues to be a problem for many workers and seek a greater level of deterrent to non-compliance. Many reported non-compliance in the 'informal economy' as being a particular problem. We look at the informal economy and deterrents later in this Chapter.

Progress in Enforcement

6.16 Effective enforcement of the minimum wage is in the interests both of workers and of the large majority of employers who are fully compliant. Satisfaction levels with the performance of the Inland Revenue's enforcement team are high, with both employers' and workers' representatives commenting favourably. The T&G thought that the effectiveness of the Inland Revenue compliance teams across the country had been a major factor in the success of the National Minimum Wage. The CBI stated that enforcement was working well in general. However, there were a number of suggestions put forward during our consultation as to how the current enforcement operation could be further improved.

'The Inland Revenue, which acts as the enforcement agents for the DTI have made strenuous efforts to catch underpaying employers....'

TUC evidence

The Effectiveness of Enforcement

6.17 The research project we commissioned on the experiences and perceptions of workers and employers who had been through the minimum wage enforcement process (Croucher and White, 2004), involved telephone and face-to-face interviews with a sample of employers and workers. It found that employers' and workers' views of the process probably related to the outcomes of their case, but, overall, both groups considered that compliance officers had been courteous and helpful. One concern highlighted by both groups was the length of time taken to complete the enforcement process.

6.18 At present the Inland Revenue has a target timescale of 35 working days to visit an employer from the time they receive a minimum wage complaint. There are, however, currently no other target timescales in place for the remainder of the enforcement process. The Inland Revenue advise that the completion time is dependent on the nature of the case and the complexity of the issues involved. But it further advised that as part of a new quality monitoring system, the compliance officer and their manager will review progress of their cases at three key stages in the enquiry process. In addition, new mandatory management checks of every case at set time intervals are being introduced. This will enable progress to be monitored effectively and, where necessary, appropriate interventions made by managers. The Inland Revenue will use the experience gained to identify and address any general issues that result in a delay in completing cases. We welcome this development and believe it should assist in ensuring that any unnecessary delays in progressing cases are addressed promptly.

Low Pay Commission Research

Over half of the employers had pay records that were found to be deficient in some respect. A major benefit of the Inland Revenue visit was seen by some employers as the opportunity to receive advice on their pay records.

Croucher and White, 2004. ***Enforcing the Minimum Wage: The Experience of Workers and Employers***

6.19 Overall, there were three broad conclusions derived from the Croucher and White research.

- The relative complexity of the National Minimum Wage regulations led to employers making 'silly mistakes' on the one hand and workers failing to claim their entitlement on the other.
- There needs to be more attention to the post-enforcement period to ensure that workers receive their full arrears.
- The inspection process can be of real benefit to employers as many found it helpful in improving their overall pay records administration and in meeting their legal obligations.

6.20 We are pleased to note from the research that many workers said they would turn to the Inland Revenue again if they were being underpaid and that some employers had continued to use it as a source of information and advice post-investigation. This would suggest that the Inland Revenue's intervention is relatively effective both at enforcement on behalf of workers and in encouraging future compliance by employers.

Pro-active Enforcement

6.21 In our fourth report (2003) we recommended that there should be further pro-active enforcement, with greater co-ordination between the Inland Revenue and wider Government compliance initiatives, and encouragement of compliance initiatives undertaken by employers and unions. We also recommended that the Government evaluate the use of existing powers, and identify whether any changes in practices or powers were needed to strengthen the deterrent to non-compliance.

6.22 In its evidence, the Government advised that the DTI and the Inland Revenue have been looking at how best to direct enforcement resources. It reported that it was introducing a targeted annual publicity and enforcement campaign commencing in 2005, aimed at tackling a particular low-paying sector or group of workers each year. We very much welcome this approach and believe that such targeting, appropriately directed, could have a significant impact in tackling non-compliance in the sectors where it is most prevalent.

6.23 The Government also advised that it is looking to identify areas where it might be possible for compliance officers to spend less time, in order to free up resources for tackling important breaches in low-paying sectors. In principle we welcome this proposed prioritisation of enforcement work, whereby resources used to pursue minor breaches in the minimum wage regulations are diverted to address more serious breaches. However, considerable care will need to be taken to ensure that genuine issues of non-compliance do not slip through the net. We look forward with interest to receiving details of the Government's proposals.

6.24 The Government stated its commitment to introducing a joint workplace enforcement pilot to explore the potential for sharing intelligence and for closer co-ordinated working between Government Departments to tackle the range of issues relating to illegal working. It is intended that the pilot will commence in Spring 2005. In addition, it has been agreed that any information on illegal workers and their employers that the Inland Revenue comes across during its enforcement activities will be passed, via the DTI, to the Home Office.

6.25 The importance and value of pro-active enforcement was stressed during our consultation, as it has been in previous years. We welcome these developments.

Community Based Activity

6.26 Following a recommendation in our second report (2000), the Government established seven community-based pilot projects with the aim of building workers' confidence in the effectiveness of the enforcement procedures and thereby encouraging greater levels of reporting of minimum wage underpayment. Five of these projects continued into 2003/04 and the Government's evidence described the progress being made.

- The Northern Ireland National Minimum Wage Helpline has been in operation since September 2001. Is is operated by the Northern Ireland Citizens Advice Bureaux, in partnership with the Inland Revenue and the DTI. Since its inception there have been over 6,000 calls to the Helpline with over 300 worker complaints referred to the Belfast compliance team for investigation.

- The Scottish National Minimum Wage Helpline was launched in February 2003. The Scottish Low Pay Unit operates the Helpline, in partnership with the Inland Revenue, the DTI and Citizens Advice Scotland. Since its launch, the Helpline has taken over 1,000 calls generating 50 worker complaints which have been referred to minimum wage compliance teams for investigation.
- In the East Midlands, the partnership with Leicester City Council and Community (formerly the National Union of Knitwear, Footwear and Apparel Trades) has continued to develop. Between April 2003 and March 2004, 31 referrals were generated and £31,000 in arrears identified in 15 completed cases.
- The pilot project with the National Group on Homeworking was aimed at improving awareness of the minimum wage among minority ethnic groups and homeworkers in Bradford and the surrounding area. While raising awareness it proved unsuccessful in generating complaints and it was closed in September 2003, with all parties agreeing to this decision.
- The partnership with the West Midlands Employment and Low Pay Unit initially aimed to raise awareness of the minimum wage across the region, targeting minority ethnic groups. The project was broadly successful in raising awareness but generated few complaints. It closed in October 2004.

6.27 The Government is continuing to monitor and evaluate these projects in order to understand why some appear more successful than others. We are pleased that it is doing so and would be encouraged if further projects were to be established to build on the successes of those currently in place.

The Employment Relations Act 2004

6.28 In its evidence the Government reported on a package of technical measures it had introduced in the recent Employment Relations Act, due to come into effect in April 2005, to assist enforcement of the minimum wage. One key measure relates to the treatment of enforcement notices. At present under the National Minimum Wage Act 1998, compliance officers are unable to withdraw enforcement notices, which set out arrears due to workers, even if new evidence has come to light or an error has been made. The position is the same for penalty notices issued to employers who refuse to comply with enforcement notices. This creates a number of enforcement problems as currently notices can only be rectified through an Employment Tribunal. The amendment to the Act will allow compliance officers to withdraw inaccurate notices and replace them with corrected notices where necessary. This is a positive development and will facilitate more effective use of enforcement and penalty notices.

6.29 Another of the Government's new measures addressed the lack of any specific power to permit compliance officers to disclose information between a worker and an employer to clarify particular issues arising on a case. This hindered investigation as different versions of events could not be cross-checked. The change to the legislation still ensures that information will not be passed on to an employer in a way that would reveal the identity of a complainant, unless authority has been given by the worker to do so. This is crucial as without such confidentiality many workers being paid below the minimum wage would not come forward.

Employment Tribunals

6.30 In our fourth report (2003) we commented that the number of minimum wage applications registered by employment tribunals had fallen sharply between 1999/00 and 2001/02. However, as shown in Table 6.2, there is considerable annual fluctuation in the number of applications. 2002/03 saw a significant increase in National Minimum Wage applications, although this dipped again in 2003/04. The first six months of 2004/05 suggests another increase.

Table 6.2 Applications Registered by Employment Tribunals, Great Britain

	2001/02	2002/03	2003/04	April to September 2004
Number with NMW as Main Jurisdiction	184	173	252	205
Number with NMW as Other Jurisdiction	372	656	361	250
Total NMW applications	556	829	613	455
Total applications under all Jurisdictions	112,227	98,617	115,042	51,031

Source: Employment Tribunals Service.
Note: The Employment Tribunals Service identifies the 'Main' Jurisdiction as the principal type of claim made when first received. A claim may be brought under more than one Jurisdiction or be subsequently amended/clarified in the course of proceedings, but will be counted only once against the Main Jurisdiction.

6.31 In evidence the Leicester Minimum Wage Project (LMWP) expressed the view that, while it supported the existing enforcement arrangements, the Inland Revenue does not, and probably cannot, provide a fully comprehensive enforcement system on its own. They regard the employment tribunal system as an important tool in

‘The LMWP is currently pursuing five employers for non-payment of tribunal awards. One employer has failed to pay an award of £11,000 in minimum wage arrears. Another has been pursued for two years for payment of around £5,000.’

LMWP evidence

enforcing the minimum wage in some circumstances in which the Inland Revenue is unable to act. Other workers’ organisations, including the T&G and Community, supported this view.

6.32 Although there was support for the tribunal system from a number of organisations who gave us evidence, some reported a growing problem in the number of employers failing to pay employment tribunal awards. Tribunal awards were seen as a good enforcement tool, with publicised successes sending an important message to employers. However, there was concern that this could be undermined if no action was taken against employers who failed to pay tribunal awards.

Detriment and Dismissal

6.33 Workers have the right not to be dismissed or victimised because they try to ensure they are paid the minimum wage or because they are, or are going to become, eligible for the minimum wage. Where employers respond to the minimum wage by, for example, reducing workers’ hours or consolidating allowances into the basic wage, these are legal means of coping with the minimum wage if they are taken by agreement with the workers concerned. However, the unilateral introduction of terms and conditions by employers in these circumstances is a contravention of National Minimum Wage legislation.

6.34 Information on the breakdown of minimum wage applications is not collected by the Employment Tribunals Service, therefore, it is not possible to identify how many of the cases shown in Table 6.2 concern minimum wage related detriment and dismissal. We did, however, hear from organisations representing low-paid workers of their concern that workers continue to be dismissed or experience detriment due to the minimum wage. The TUC reported that workers find it very difficult to enforce their rights as redress can only be achieved via an employment tribunal case. The National Group on Homeworking expressed concern that insisting on the right to be paid the minimum wage can often result in the homeworker concerned not receiving any more work. The GMB and TUC called for compliance officers to have more powers to deal with detriment cases.

The Informal Sector

6.35 We have received a significant body of evidence indicating that non-payment of the minimum wage in the informal sector continues to be a problem. Such non-compliance often affects the most vulnerable groups of workers and presents unfair competition to compliant employers.

6.36 The CBI reported that employers in certain sectors feel that they are increasingly undercut by competitors operating in the informal economy, in particular in the hospitality, business services, hairdressing and horticulture sectors. The CBI believes that the higher the minimum wage, the greater the incentive to informal economy activity as the potential gain for unscrupulous employers from tax evasion rises and non-compliance becomes more attractive. It also reported that some employees are willing to accept wages below the statutory minimum from rogue employers (often accompanied by a 'cash in hand' payment) in order to increase their take-home earnings through evasion of income tax and National Insurance Contributions. The CBI suggested that any rises to the minimum wage must be treated cautiously so as not to add to the problem. Other organisations that registered concern about the growth in the informal economy included the T&G and Community.

6.37 We commissioned research from Ram *et al* (2004) to investigate the ways in which small firms in the restaurant and clothing sectors in the informal economy operate in the light of the existence of the minimum wage for five years. The main reasons for non-compliance given by the employers in the study were their alleged inability to pay the full rate and a perceived unlikelihood of detection by the Inland Revenue. Many employers did, however, state that they were fearful of detection by the authorities, although there was uncertainty as to what action would be taken against them and the penalties for non-compliance. Some firms that did comply with the minimum wage were also included in the study to enable comparison. For these firms, a key factor in accounting for their decision to comply was their position in the market. Most sought to grow their business and found that paying below the minimum wage was incompatible with this. In addition, they often supplied larger firms, some of whom exercised influence over internal operations of the firms in the study, and they were more likely to be involved in local business networks.

6.38 The study suggested a high level of minimum wage underpayment in parts of both the clothing and restaurant sectors. In several of the non-compliant firms, the average wages, and in some cases even the highest wages, including those of the owners, were below the minimum wage level. Employers often evaded paying the minimum wage by under-declaring the number of hours worked by employees and in a number of cases workers were complicit in this activity. The study found no evidence that firms visited as part of an earlier study, were moving towards compliance. In fact, operating outside of the

'According to the British Hospitality Association, 41 per cent of companies in this sector believe they are being undercut by black economy firms paying below the NMW.'

CBI evidence

Low Pay Commission Research

'The NMW does not really influence how wage rates are determined. NMW has not had any impact as it is not applied in this trade; employees are just paid a weekly sum, hourly calculations don't really come into the equation'

(Quoting an employer in the restaurant sector.)

Ram *et al.*, 2004. *Informal Employment, Small Firms and the National Minimum Wage*

'We are working with other bodies including DTI, to set-up networks within the supply chain and with retailers to encourage companies out of the informal sector.'

British Apparel and Textile Confederation evidence

Low Pay Commission Research

'Some employees under-declare their hours to get a better family credit rating. They suggested this themselves. They get £150 from me, show £85 and get another £200 from the government.'

(Quoting an employer in the clothing sector)

'We pay people a weekly wage, but we do not declare the whole amount as it is not beneficial for me or the staff as they will not be able to get maximum working tax credit. The lower the wages declared the lower the turnover can be declared by the owners. Accountants who work for restaurant owners know how the system operates and they are basically our point of contact on how to manage the NMW. Everyone in this trade will, if they are honest, give you similar answers, some may be afraid of the consequences.'

(Quoting an employer in the restaurant sector)

Ram *et al.*, 2004. *Informal Employment, Small Firms and the National Minimum Wage*

minimum wage legislation tended to have consequences for firms' tax and other practices, and this may have tightened their position outside the formal sector of the economy.

6.39 We believe that the Government's proposed initiative to develop a programme of targeted enforcement, as referred to earlier in this Chapter, should help to address underpayment of the minimum wage in the informal economy. We will monitor progress with interest and maintain a regular dialogue with the Inland Revenue.

6.40 Some organisations reported that migrant workers were one of the most vulnerable groups of workers in the informal economy as they may be less aware of their employment rights and more open to exploitation. Community told us that workers without English language skills are worst affected. It cited the LMWP as an initiative that was helping migrant workers to gain basic language skills to overcome this problem. Citizens Advice advised us that they were receiving a relatively small but growing number of requests for advice from migrant workers. But they believe those that come forward represent the 'tip of the iceberg'. They are concerned that there may be many more in circumstances that make them too fearful of victimisation even to seek advice.

6.41 Since May 2004, workers from the new EU member states have been entitled to work in the UK, provided they register under the Workers Registration Scheme (WRS). The Government reported in its evidence that the Home Office is sharing information from the WRS database with the Inland Revenue, so that the Inland Revenue can sample a percentage of employers of new EU Member State nationals each month to check compliance with the minimum wage.

6.42 The Government also advised of its actions to assist in informing migrant workers coming to the UK of their employment rights and responsibilities. This included producing employment rights information for nationals from the new EU Member States in the form of bilingual leaflets. The leaflets were launched in Poland and Lithuania in 2004 and were distributed in the respective countries, as well as the UK, with the intention of informing workers of their rights ideally before they set out to travel to the UK. The programme is being rolled out to cover the other new Member States. The Home Office has also provided funding for the translation of a separate document produced by the TUC on workers' rights.

Evaluation of Enforcement Powers

6.43 In our fourth report (2003) we welcomed the work that the Inland Revenue had done to date in enforcing the minimum wage, but felt that it was an appropriate time for a review of its powers and practices. Accordingly, we recommended that the Government evaluate the use of existing powers and identify whether any changes in practices or powers were needed to strengthen the deterrent to non-compliance.

6.44 The Inland Revenue carried out it own review of its use of enforcement powers set out in the minimum wage legislation, following discussion with the DTI and ourselves to identify the key areas to be covered. The Government's evidence noted the main conclusions of the review and these are detailed below.

- The Inland Revenue considered whether to seek confirmation of payment of arrears in all cases but concluded that this would not be resource effective. It will instead seek to identify employers most at risk of not paying arrears and ensure that all such employers are pursued for proof of payment. In addition, all compliance teams will set out clear, unambiguous deadlines for payment of arrears. Workers will be strongly encouraged to advise the Inland Revenue if arrears are not received by the specified date. Early enforcement action will be taken where non-compliance has recurred.
- The Inland Revenue's closed case review programme showed that only 55 per cent of employers visited were keeping adequate records. To tackle this, compliance officers will give advice on record keeping to all employers found to be keeping inadequate records during an enquiry.
- The Inland Revenue will work with the DTI to explore how changes to the legislation in the Employment Relations Act 2004 can enhance the effectiveness of enforcement and penalty notices as a means of bringing enquiries to a satisfactory conclusion.
- The Inland Revenue will build on the experience of a pilot it is running to identify cases where unannounced visits may be appropriate. In future, unannounced visits will be an option that is considered when planning all enquiries.

6.45 The review has clearly provided valuable specific information on areas for improvement. We strongly support the actions that have emerged from it and believe that these go some way to addressing problem areas that have been identified in the evidence provided to us. But if they are to do so, it is essential that they are taken forward in a timely

‘Under the current system there is almost an incentive for employers not to pay the NMW as, if caught, they get no more than a slap on the wrist and need to pay only what they should have paid in the first place. This is not sufficient, particularly when compared with penalties imposed under other regulations. For example, employers producing counterfeit goods face unlimited fines and up to 10 years in prison. IR charges interest to individuals on money owed to them.’

Community evidence

manner, with arrangements put in place to evaluate their effectiveness. We shall monitor developments with interest.

6.46 Although we are encouraged by these proposals, we do not feel that they will do enough to strengthen the deterrent to non-compliance. It is apparent that most employers who do not pay the minimum wage and have enforcement action taken against them are no worse off than if they had paid the minimum wage at the outset. Indeed, in many cases they may even be better off as they are not required to pay interest on underpayment of arrears to the worker. Nor is there any other financial penalty imposed for late payment in itself, except in cases where a penalty notice has been issued (although the financial penalty is not paid to the worker concerned). A worker, however, who is paid below the minimum wage is likely to suffer financial hardship even if arrears are eventually paid, since they do not receive interest to reflect the later payment.

6.47 The lack of an effective deterrent to non-compliance was raised by a number of organisations in their evidence to us. Some suggested that the imposition of a financial penalty on non-compliant employers would act as a deterrent. The TUC stated it was now time that persistent offenders were treated more harshly. It supported the principle of charging interest on the back pay owed to workers by defaulting employers in order to give employers stronger incentives to comply. We also note that interest is payable on any arrears of company or individual tax in order to reflect the time value of money to both taxpayers and to the Government.

6.48 We believe that requiring a defaulting employer to pay interest on minimum wage arrears would send a clear message that non-compliance is not an easy option. It might also encourage more workers to come forward and report underpayment. Imposing a financial penalty on employers guilty of serious non-compliance would strengthen this further. Current legislation does not allow for interest to be paid on arrears owed to a worker or for a financial penalty to be imposed and a change to the legislation would therefore be required. But we believe that the arguments to redress this situation to give workers their fair entitlement are compelling. **We therefore recommend that the Government should introduce interest charges payable on arrears arising from minimum wage underpayment and financial penalties for seriously non-compliant employers.**

Conclusion

6.49 The information we have received indicates that compliance with the National Minimum Wage continues at a high level. However, although we view the overall position as positive, there remain some problem areas where non-compliance is more prevalent. We recognise the positive developments there have been to increase compliance and the steps taken by the Inland Revenue to develop the effectiveness of its enforcement action. We welcome the further improvements planned and believe that the targeted enforcement action announced by the DTI will be a particularly positive step forward. We will monitor progress on this and the other developments referred to above with interest.

6.50 Further, we believe that the recommendations we have made in this Chapter will add impetus to compliance and enforcement of the minimum wage. Awareness of the minimum wage is essential and we have, therefore, recommended that the Government review its minimum wage publicity strategy to target effectively all groups of low-paid workers, with emphasis on the most vulnerable groups. Introducing a requirement for employers to pay interest on minimum wage arrears and a financial penalty will help to ensure that underpaid workers are not disadvantaged and will provide a greater deterrent to non-compliance. We now turn to Chapter 7 in which we review the minimum wage rates.

Setting the Rates

The evidence shows that the minimum wage has been a success. The economy has continued to generate new jobs, including in the main low-paying sectors, without any signs of an emergence of wage inflation. Many low-paid workers have benefited. While some firms continue to report difficulties in adjusting to the successive upratings of the minimum wage, the impact on aggregate and sectoral wage bills has been minimal.

Our formal and informal consultations with employers, however, revealed high levels of concern about the effect of the last two upratings and about the potential impact of further significant increases. And the available macroeconomic data do not yet allow an appraisal of the full effects of the uprating of the minimum wage to £4.85 in October 2004. Our assessment therefore needs to balance the available macro data with the input from consultations.

Most of the interested parties accepted the case for an uprating, but there was no consensus. The range of opinions varied from below to substantially above the predicted growth in average earnings.

Balancing these considerations, we believe that there is a strong case for continuing along the path of uprating the minimum wage outlined in the fourth report (2003), with a further increase relative to average earnings over the next two years. But, in the light of the level of employer concern, we judge it appropriate to proceed with caution. For that reason we are recommending that the increase over two years should be above predicted average earnings, but not substantially so. We also consider that the upratings should be phased so that the increase in the first year is modest, allowing employers further time to adjust to the October 2004 uprating. We recommend that the adult rate of the minimum wage should be increased to £5.05 in October 2005 and further increased to £5.35 in October 2006. We recommend that the 2006 uprating be subject to review, both to check that the macroeconomic conditions continue to

make it appropriate, and in the light of the implementation of age discrimination legislation as outlined below.

The Government has set out its intention of legislating, during the course of the next Parliament, to ensure that the eight bank holidays count as paid leave in addition to the 20 days of paid leave (for a typical full-time worker) which the law currently requires. In the vast majority of cases this change will make no difference, since about 92 per cent of full-time workers already enjoy at least 20 days paid annual holiday excluding the eight bank holidays. And the overall hourly wage bill impact of the change seems unlikely to exceed 0.4 per cent. But those specific companies which currently do not allow paid bank holidays in addition to the 20 days could face hourly wage bill increases of 3.2 per cent and such companies are likely to be concentrated in low-paying sectors.

We do not believe therefore that the proposed change will have an impact sufficiently large or sufficiently widespread as to make further upratings of the minimum wage inappropriate, but we note that the pace of introduction will determine the severity of adjustment difficulties in specific firms. The timing of the implementation is presently uncertain and dependent both upon Government intentions and the Parliamentary schedule. We have based our recommendations on the assumption that the full impact will not occur within the two years covered by this report. We will take the additional costs into account in future years.

While workers in other age groups have seen their position in the labour market improve, the position of young people has remained more or less static. Our ability to increase the adult rate by slightly more than average earnings depends on the continued existence of the youth Development Rate and the 16–17 year old rate. We believe that the application of the adult rate to younger people would damage their employment prospects. And the existence of separate rates for young people is fully consistent with the Equal Treatment Directive.

Our recommendation of a figure of £5.35 for the adult rate in October 2006 therefore depends on the assumption that the forthcoming UK implementation of the Equal Treatment Directive will continue to allow the straightforward use by employers of the lower rates for younger people. The Commission therefore recommends that it should review its recommendation for October 2006 in February 2006 and confirm it if the implementation of the legislation has been designed to achieve this.

The Commission believes, however, that this reinforcement of the principle of lower rates for younger people should be combined with a

change in the upper age limit for the youth Development Rate from the 22nd to the 21st birthday.

We recommend that the youth Development Rate be increased to £4.25 in October 2005 and to £4.45 in October 2006. We recommend an increase slightly lower than the adult rate (and lower than the forecast increase in average earnings) recognising that young people have done less well in the labour market and in the expectation that the Government will recognise the case for extending the adult rate to 21 year olds.

In our fourth report we said that we believed that there was a case for increasing the effective level of the minimum wage. The increase we have recommended over the next two years will again exceed the predicted growth of average earnings. We have, however, kept the adjustment above average earnings small, and concentrated it in the second year to allow business time fully to absorb the impact of the increases.

However, it remains our view that some further increases relative to average earnings will be required in subsequent years to bring the minimum wage to an appropriate long-term level.

We make no recommendations with regard to the 16–17 year old rate. We propose instead that the Government invite us to review the operation of the 16–17 year old rate in 2005 and report in February 2006 with recommendations for any subsequent increase suitably adjusted to take account of the absence of any uprating in 2005.

Introduction

7.1 In arriving at our recommendations we have considered three main factors: our assessment of the impact of the minimum wage so far (set out in detail in Chapters 2 to 5); an assessment of the prospects for the economy over the coming period; and the views expressed by interested parties. This Chapter covers each of these three factors in turn before setting out our recommendations for minimum wage rates for adults and young people for October 2005 and October 2006. It then sets out our assessment of the likely impact of the recommended rates on the number of beneficiaries, the wage bill, and household income. Finally, we reflect on the cycle of our reviews in the light of comments received during consultation.

The Impact of the Minimum Wage So Far

7.2 The economic evidence shows that overall employment levels have continued to strengthen since the introduction of the National Minimum Wage. There has been no evidence of adverse effects on inflation but, inevitably, the minimum wage has created some adjustment difficulties for some firms. As for profits, the macroeconomic data do not support a conclusion that the minimum wage has affected the overall level of profitability in the economy, but equally it is not possible to conclude from the data that there has definitely not been any effect. One study we commissioned did find an impact on the level of profitability of firms that predominantly employ workers paid at or around the minimum wage. But the evidence suggests the impact has been moderate.

7.3 The impact on wage bills remains small. Our latest estimates of the effect of the October 2004 upratings show a range of increases in the overall UK wage bill, depending on the assumptions used, of between 0.06 per cent and 0.08 per cent.

7.4 While the absence of adverse effects is welcome, it is also important that a significant number of workers benefit from the minimum wage. Throughout the life of this Commission, the number of beneficiaries has turned out to be smaller than originally forecast. This issue is explored more fully in Chapter 2. Our latest estimates, based on the provisional Annual Survey of Hours and Earnings (ASHE) April 2004 data, are that about one million adult workers, or 4.4 per cent of the adult workforce, received wage increases between April 2004 and October 2004 as a result of the minimum wage uprating to £4.85 in October 2004. The equivalent estimate for the October 2003 uprating to £4.50, indicates that 0.9 million or 3.8 per cent of the adult workforce were direct beneficiaries in the six months before the uprating. These numbers are similar to those we have observed following previous upratings. As noted in Chapter 2 however, this ‘undershoot’ may largely reflect methodological difficulties in estimating the number of beneficiaries once the minimum wage has been in place for several years.

7.5 The combination of these considerations, however, supports the Commission’s judgements (in our fourth report) that it was appropriate to increase the effective level of the minimum wage over the last two years, and that this increase – bringing benefit to more workers – has been achieved without adverse economic consequences.

7.6 As we saw in Chapter 5, however, labour market data suggest that young people have fared slightly less well. While the employment and activity levels of other groups in the economy have strengthened, participation in the labour market by those aged 18–21 has remained more or less static. There is little evidence to suggest that the minimum wage is responsible for the relative weakness in the labour market of this group of workers, since around 85 per cent of all jobs held by 18–21 year olds pay at or above the adult minimum wage. But, as noted in previous reports, there remain grounds for caution on youth rates.

7.7 Overall, therefore, the evidence so far suggests that the adult rate is not at a level which is causing any undesirable macroeconomic consequences and that it should be uprated at least in line with the forecast growth in average earnings. At the same time, the pace of any adjustment needs to reflect prospects for the economy. In the next section, therefore, we consider recent economic forecasts and trends in prices, earnings, and pay settlements.

The Economy

7.8 The economic outlook partly determines the minimum wage that firms can afford without detrimental impacts on employment prospects or on inflation. Forecasts of price inflation and earnings growth are also used to estimate future wage bill costs and to gauge the likely number of beneficiaries (the 'coverage') of future minimum wage rates. This section therefore examines aggregate forecasts before turning to detailed consideration of how price, earnings and pay settlement trends influence our decisions.

Forecasts

7.9 Economic performance has been strong since our fourth report (2003) – indeed in 2004 the pace of economic growth exceeded the expectations of all but the more optimistic forecasters. The inflation rate has been well contained. And employment levels, as discussed in Chapter 2, have remained at record levels.

7.10 Looking forward, Table 7.1 shows that the consensus of latest forecasts for the UK economy suggests a modest slowdown in Gross Domestic Product (GDP) growth as the economy moves from a period of above trend growth towards trend growth of some 2.5 per cent. At the same time, inflation as measured by the Consumer Price Index (CPI) is predicted to remain below the Bank of England's target of 2.0 per cent, at least until 2007. Average earnings growth is forecast to be some 4.5 per cent, which is compatible with low growth in unit labour costs if productivity grows in line with trend.

Table 7.1 Independent Forecasts of GDP Growth, Inflation and Average Earnings

Average percentage change over a year earlier	2005	2006
GDP growth	2.6	2.5
CPI inflation	1.8	1.9
RPIX inflation	2.3	2.3
Average earnings	4.5	4.5

Source: HM Treasury (2005).

7.11 There are risks in any forecast. But if anything the risks to the macroeconomic outlook look less pronounced in February 2005 than when we produced our fourth report with its recommendations for rises in October 2003 and October 2004.

7.12 Consensus forecasts and assessments of risk therefore suggest that the economy will be able to absorb further increases in the minimum wage at least in line with anticipated growth in average earnings. The one note of caution that must be sounded is that the available data do not yet allow a full appraisal of the impact of the October 2004 increase, which at 7.8 per cent was significant in real terms. While our judgement from available data is that it is probable that the increase has been absorbed without adverse effect, the lack of certainty argues for some caution looking forward.

Prices

7.13 Since its introduction in April 1999, the minimum wage has more than kept up with the cost of living. If the adult minimum wage had been increased in line with the RPIX price index[1] since introduction, its value would have been £4.06 in October 2004, significantly below the actual level of £4.85. But a minimum wage that increased only in line with prices would rapidly lose its value as a wage floor. The lowest paid would not share in the overall rise in earnings and prosperity. While prospects for inflation need to be part of our economic assessment, increasing the minimum wage only in line with prices would be a recipe for making the minimum wage increasingly irrelevant over time.

Earnings

7.14 Increasing the minimum wage in line with average earnings implies an increase above the rate of inflation, and keeps the minimum wage in line with the increase in the general level of prosperity in the country.

[1] RPIX measures price inflation excluding mortgage interest costs.

In the year to December 2004, average earnings as measured by the Average Earnings Index (AEI) increased by 4.3 per cent including bonuses and 4.5 per cent excluding bonuses. The data are consistent with an underlying pace of increase of about 4.5 per cent.

7.15 If the adult minimum wage had, since its introduction, increased in line with average earnings, its value in October 2004 would have been £4.50 as opposed to the £4.85 then introduced. This outcome reflects the fact that over the last two years the growth in the minimum wage has outpaced increases in average earnings. If the minimum wage were to be increased by the same pace as average earnings between October 2004 and October 2006, its value would rise to £5.07 in October 2005 and £5.30 in October 2006.

7.16 Uprating the initial level of the youth Development Rate (£3.00) by average earnings would have led to a rate of £3.75 by October 2004, showing that at its current level of £4.10 the youth Development Rate has increased faster than earnings. Projecting the current rate forward by forecast average earnings would give rise to rates of £4.28 and £4.48 in October 2005 and October 2006 respectively.

7.17 These earnings-uprated projections provide a benchmark against which we can judge how the minimum wage is progressing relative to earnings overall. We concluded, in the light of our analysis of the impact of the minimum wage, that a further modest increase in the effective level of the minimum wage would not do significant harm to the overall economy and would preserve and increase slightly the number of beneficiaries.

Pay Settlements

7.18 The level of pay awards provides an important indicator of general movements in pay. Incomes Data Services (2005b) report that the median pay settlement was 3.1 per cent in the year to October 2004. Other data, such as those from Industrial Relations Services (2005), show a similarly constant pattern around 3 per cent. Pay settlements are stable, display no discernible tendency to accelerate, and therefore do not portend any damaging wage-price spiral. All remain consistently below the growth in average earnings; this is because negotiated settlements generally exclude merit awards, promotion, and other pay drift effects.

7.19 That pay settlement data and growth in average earnings display such a high level of stability has been taken by some to indicate that the labour market is not as tight as it appears. One likely explanation is that

"Having looked at the evidence to date and the outlook for the economy and the labour market as a whole, we believe a further significant increase in the NMW above the expected rise in average earnings is both credible and realistic."

TUC evidence

"Against the backdrop of a continuing deflationary climate in the High Street, companies just cannot continue to live with successive disproportionate increases that have been more than double the prevailing level of pay settlements in the sector. We would strongly urge that there should be no increase in the minimum wage in 2005, in order to give companies time to adjust to previous years' increases."

BATC evidence

the current level of migration provides employers with a ready stream of willing and able workers, which enables employers to fill crucial gaps in their labour forces without being forced to resort to higher wages in order to recruit workers.

7.20 The level of pay settlements is consistent with the overall picture of subdued inflation, with no significant inflationary pressures emanating from the labour market.

The Views of Interested Parties

7.21 All the macroeconomic data referred to above suggest that current economic circumstances are benign and that it is possible to increase the effective level of the minimum wage. However, in reaching our conclusions about the scope for further increases in the minimum wage, we also took careful account of the views of a wide range of those most affected, including employer representatives, trade unions, youth organisations and the not-for-profit sector. These face-to-face meetings sometimes gave us a perspective on an issue that was not readily visible in the available aggregate or macroeconomic data.

7.22 The vast majority of employer organisations accepted that the minimum wage should be uprated, but many preferred future increases to be limited to price inflation. A smaller number proposed a link with average earnings.

7.23 In contrast, trade unions and other workers' organisations argued that further substantial increases in the minimum wage could be achieved with no ill effects on the economy or on employment. Among those we met were some who argued for a significant increase in the value of the minimum wage – with a few suggesting we should adopt the concept of a 'living wage' set at a far higher level.

7.24 In calling for modest future increases, employers drew attention to the two sizeable, above inflation increases in the minimum wage which took effect in October 2003 and 2004 and expressed doubts about the ability of the economy as a whole to withstand further increases on a similar scale. The British Retail Consortium pointed to the growing concern among large retailers about the impact of the minimum wage. They argued that the minimum wage had reached a 'tipping point' with the last two increases and warned of future job losses in the sector as a direct result. A quarter of retailers responding to their survey were already considering reducing jobs as a result of the October 2004 increase to £4.85.

7.25 The CBI argued that the level of corporate profitability appeared to have peaked in the present cycle at a lower percentage of GDP than in previous cycles, and that a squeeze on profits, combined with uncertainty about the economic outlook, was reducing investment in fixed capital and equipment, with potentially harmful consequences for the UK's long-term growth prospects. It was also concerned about increased business costs as a result of new regulation, including the rise in employer National Insurance Contributions. The CBI concluded that, as a result, future increases in the minimum wage would be much less affordable and called for a 'pause year' in 2005.

7.26 The British Chambers of Commerce was concerned that further increases in the minimum wage above average earnings 'could start to have a detrimental impact on staffing levels and competitiveness'. Like a number of employer representatives, the Business Services Association also commented that differentials had been squeezed and the Cleaning and Support Services Association was similarly concerned that this had had a negative impact on recruitment. One of the concerns commonly expressed was that, as the wages of the low-paid rise to the level of those above, it becomes harder for firms to provide incentives to employees to assume positions of greater responsibility.

7.27 Trade unions and other workers' organisations, however, emphasised the success of the minimum wage to date in reducing exploitation and raising the earnings of the lowest-paid workers without any apparent negative effects. They noted that employment had increased to unprecedented levels; inflation was stable and argued for further increases in the minimum wage above average earnings. The Trades Union Congress (TUC) called for a rise to at least £5.35 in October 2005, moving towards £6.00 by October 2006. Some unions wanted more, with the GMB calling for an increase to £6.00 from October 2005 and Unison seeking £6.50 by October 2006. A number of respondents also argued that substantial increases were required to raise the minimum wage from a wages floor to a living wage (reducing dependency on in-work benefits such as the Working Tax Credit) and to tackle the gender pay gap.

7.28 A number of respondents called for the minimum wage to take account of regional differences in the cost of living and of local economic circumstances. The British Apparel and Textiles Confederation (BATC) said that the Commission should consider a regional or sectoral minimum wage and the Federation of Small Businesses believed there was a strong case for a regional minimum wage. The Low Pay Commission's remit, however, is to make recommendations for a

‘In some cases staffing levels have already been affected by the NMW, with 16 per cent of retailers saying they were unable to maintain their staff levels when the NMW was £4.50.… At £4.85, 25 per cent of retailers are unable to maintain their current employee level and this increases to 44 per cent at £5.20.’

British Retail Consortium evidence

‘By reducing the costs of chronic staff turnover, and pushing employers to invest in training and productivity measures, a NMW of £6 an hour will start to address the low pay, low skills, low productivity vicious circle which traps [low-paying] sectors.’

GMB evidence

‘The CBI accepts that the National Minimum Wage should increase as economic circumstances allow so that it does not wither on the vine. However, if negative effects of the NMW are to be avoided, any uprating must take account of the competitiveness of the overall UK economy and that of individual firms.’

CBI evidence

National Minimum Wage only, not a wage that varies from region to region. Nor are we mandated to recommend a ‘living wage’. Rather our aim is to set a minimum wage that establishes an important floor. Moreover, alongside other government policies, it makes a significant difference to low incomes, but does so in ways that do not cause economic harm. The total combined impact of the minimum wage and the benefits system is considered below in the section The Impact on Low Incomes.

7.29 Submissions from the trade unions and workers’ organisations consistently argued that the adult rate of the minimum wage should apply from the age of 18 and that a lower youth rate was discriminatory. Youth organisations feared that young people were being exploited in the workplace and that too low a rate could force those in education to work longer hours to support their studies. A smaller number of respondents proposed a flat rate from 16, but there was generally an agreement that a lower rate for 16–17 year olds was necessary.

7.30 Employer representatives were broadly supportive of maintaining the current differential between the adult rate and the youth Development Rate, although the British Hospitality Association urged caution to avoid pricing the 18–21 age group out of the market place. Business representatives also tended to agree that the 16–17 year old rate should not increase, or that any increase should be small in 2005, until the impact of the £3.00 rate introduced in October 2004 could be fully assessed.

7.31 A common theme expressed by many business representatives and by some unions was the need for greater predictability of future rates. However opinion was divided on the question of whether an automatic indexing process should determine future minimum wage upratings, or whether flexibility was required to respond to changing economic circumstances.

The Recommended Rates

7.32 Our recommendations have taken account of both quantitative and qualitative sources of data, covering both economic and sectoral effects. Our aim is to have a minimum wage that helps as many low-paid employees as possible without any significant adverse impacts on inflation or employment.

7.33 Quantitative analysis of the impact of the minimum wage so far shows that it has not had significant inflationary effects nor has it destroyed jobs at either the overall or sectoral level. Its wage bill impact has been low, lower than originally anticipated, and well below levels which might create the danger of an inflationary spiral. This suggests that, notwithstanding the significant real increase over the past two years, there is scope for a further increase in the effective level of the minimum wage over the next two years.

7.34 Economic forecasts suggest that such an increase would take place against the backdrop of economic growth close to trend, and an inflation rate below the Bank of England's target of 2 per cent. And the risks to this outlook seem less severe than when we last made recommendations for the adult rate in February 2003.

7.35 However, we note business concerns about the impact on differentials. We have therefore recommended an uprating for October 2005 slightly below the projected growth in average earnings. At the same time, given that there is a general desire among employers to move away from alternating small and large adjustments, we have deliberately not proposed an award too heavily skewed towards one year or the other.

7.36 **We recommend that the adult rate of the minimum wage should be increased to £5.05 in October 2005 and that it should be further increased to £5.35 in October 2006. We recommend that the 2006 uprating be subject to review in February 2006, both to check that the macroeconomic conditions continue to make it appropriate, and in the light of the implementation of age discrimination legislation as outlined below.**

7.37 Our recommendations envisage increases in the minimum wage in October 2005 and October 2006 which, taken together, imply an increase in the minimum wage above the projected increase in average earnings. In the first year, the recommended increase in the adult rate of 4.1 per cent is slightly below the projected growth in average earnings, but taken together the two increases amount to 10.3 per cent, 1.1 percentage points greater than the projected 9.2 per cent compound increase in average earnings.

7.38 For the youth Development Rate we recommend slightly lower increases than those proposed for the adult minimum wage, with a 3.7 per cent increase in October 2005 and a total of 8.5 per cent over two years. This reflects the need for some caution in the light of mildly adverse trends in youth labour markets. **We recommend the Youth Development Rate should be £4.25 in October 2005 and £4.45 in**

'An equal minimum wage would make a difference to many more young people's lives; protecting all our most vulnerable workers and giving them a fair, equal and legitimate position in the workplace.... An equal minimum wage would also help relieve the increasing financial pressures for younger people....'

Coalition of Youth Organisations' evidence

October 2006. This latter recommendation is however strongly tied to our firmly held conviction that 21 year olds should receive the adult rate. Should 21 year olds continue to be paid the youth rate we would probably recommend that the youth Development Rate be increased proportionately in line with the increase in the adult rate.

7.39 Our ability to increase the adult rate by slightly more than average earnings depends on the continued existence of lower rates for younger people (i.e. the youth Development Rate and the 16–17 year old rate). Evidence suggests that the application of the adult rate to younger people would have adverse employment consequences, given the distinctive features of the labour market for young people. Separate rates for young people are also fully consistent with the Equal Treatment Directive (2000/78/EC), which specifies that different remuneration rates for young people on grounds of age shall not constitute discrimination if, within the context of national law, they are objectively and reasonably justified by a legitimate aim (including employment policy).

7.40 Our recommendation of a figure of £5.35 for the adult rate in October 2006 therefore depends on the assumption that the implementation of this anti-age discrimination legislation will continue to allow the straightforward use by employers of the flexibility which the existence of the lower rates for younger people is intended to allow. The Commission therefore recommends that it should review its recommendation for October 2006 in February 2006 and confirm it if the implementation of the legislation has been designed to achieve this.

7.41 As the minimum hourly rate for 16–17 year olds was introduced for the first time in October 2004, the evidence on which to base a judgement is not yet available. Accordingly, we make no recommendations at this time with regard to the 16–17 year old rate. **We recommend instead that the Government invite us to review the operation of the 16–17 rate in 2005 and report in February 2006 with recommendations suitably adjusted to take account of the absence of any uprating in 2005.**

The Impact of Our Recommendations

Coverage – the Number of Beneficiaries

7.42 Since the recommended adult rates for October 2006 will represent an increase from October 2004 slightly above average earnings, this two-year uprating is likely to produce an increase in coverage.

7.43 To estimate coverage figures we need to assume how the wages of the lowest paid would increase in the absence of the minimum wage. Our preferred calculations are based on the assumption that the wages of the low paid would have increased in line with average earnings.

7.44 Assuming that, from October 2005, 21 year olds would be entitled to the adult minimum wage and if low wages were to increase in line with average earnings, we estimate that at the new rate of £5.35 in 2006, the number of adult beneficiaries (aged 21 and above) would be about 1.2 million or 5.3 per cent of the labour force. If we assume instead that the wages of the low paid would merely have matched price inflation, a greater number of workers would turn out to be beneficiaries – about 2 million or 8.5 per cent of the adult workforce. We believe that the average earnings assumption is the most credible. On this basis we estimate that the new rate for the minimum wage will achieve slightly higher coverage levels than those achieved by the £4.85 uprating in October 2004.

7.45 Given the less certain position of young workers in the labour market, we have opted to increase the youth Development Rate by a smaller percentage than the adult minimum wage, by 3.7 per cent in October 2005, and an increase over the two years of 8.5 per cent to October 2006. On the basis of the assumption that young people's wages would otherwise rise with average earnings, we estimate that about 100,000 young workers (aged 18–20) would be beneficiaries of the new youth Development Rate in October 2005; this equals about 7.7 per cent of young workers.

7.46 We should also remember that roughly 85 per cent of young workers are paid at least the adult minimum wage. Many of these will therefore be beneficiaries of the proposed uprating of the adult minimum wage, which is larger in percentage terms than the increase in the youth Development Rate as well as the projected growth in average earnings.

7.47 Taking the increase through to October 2006, and assuming again that, in the absence of an increase in the minimum wage, the increase in youth wages would have matched the growth in average earnings, we calculate that there would be a similar number of beneficiaries to the October 2005 uprating.

7.48 Overall, we estimate, based on the proposed new rates for October 2006, that the total number of beneficiaries would be about 1.3 million if wages of the low paid were to increase by the forecasted growth in average earnings over the two years, or around 2.1 million if, instead of increasing in line with average earnings, the low paid would otherwise have received increases in line with prices.

Position Relative to Average Earnings

7.49 In previous reports we have commented on the relationship between the minimum wage and average earnings as a way of measuring the 'bite' of the minimum wage. ONS has recently replaced the mean with the median as its headline measure of average earnings, and this is the measure that we use here. It is preferred over the mean for earnings data as it is less influenced by extreme values, which occur at the upper end of the distribution. We considered the relationship of the minimum wage to median earnings in our fourth report (2003).

7.50 In April 2004, according to ASHE, the median gross hourly earnings (excluding overtime) of all employees (full-time and part-time) were £9.21. Uprating that figure by the growth in average earnings actual and predicted (including bonuses) yields a basis for comparison with the minimum wage. The figure arrived at in this fashion is £10.28 for October 2006. The new recommended adult rate of the minimum wage will thus be about 52 per cent of forecast median earnings, or slightly more than half median earnings. If instead of looking at the median earnings of all workers, we looked at those of full-time workers alone and compared the minimum wage with median full-time hourly earnings excluding overtime, the corresponding proportion would be 46 per cent.

7.51 Comparing this UK ratio for full-time employees with that of other countries we find the UK placed squarely in the middle of the existing range for the twelve OECD countries used as a basis of comparison – see Table A4.2 in Appendix 4. The new ratio would place the UK joint seventh in relation to other countries, behind Australia, France, New Zealand, Ireland, Belgium, and Greece, but substantially ahead of Spain, the United States, Japan and Canada. The position in the UK is roughly on a par with that in Holland.

Wage Bills

7.52 Assuming that wages would increase in line with the predicted rise in average earnings regardless of our proposals, the impact of our recommendations on the overall wage bill will be small. Over the two-year period, we recommend that the adult minimum wage should increase by 10.3 per cent compared with a predicted increase in average earnings of around 9 per cent. The impact will be smaller in the first year when, if our recommendation is accepted, the adult minimum wage will rise by 4.1 per cent – lower than the expected

4.5 per cent increase in average earnings. In October 2006, if the Government agrees, the adult minimum wage will increase by a further 5.9 per cent, compared with the forecast average earnings growth of 4.5 per cent.

7.53 There are two additional factors to take into account. As discussed in Chapter 2, some people are paid below the minimum wage. Assuming that all those earning less than the minimum wage receive increases that take them up to the recommended minimum wage in 2005 and 2006 would add a little more to the impact on the wage bill. Moreover, we are recommending that 21 year olds should be entitled to the adult minimum wage and this would lead to an increase in wages of more than 10.3 per cent for those affected. However, as around 92 per cent of working 21 year olds are already paid at least the adult rate, the impact will not be significant. Overall, we conclude that the direct impact of our recommended upratings on aggregate wage bills will be modest. Taking all of the above into account and using the earnings assumption we calculate that, compared with October 2005, the direct wage bill in October 2006 would increase by about 0.02 per cent as a result of the 2006 upratings. If differential impacts were included, the increase would be 0.04 per cent. Using the prices assumption, the increases are estimated to be 0.07 per cent and 0.09 per cent respectively.

7.54 The impact of the recommended upratings in 2005 and 2006 would not be even across the economy. As discussed in Chapter 2, the impact falls more heavily on small firms and the low-paying sectors. This will again be the case for the 2005 and 2006 upratings.

Bank Holidays

7.55 The Government asked us to consider the impact of legislating to ensure that bank holidays are not counted as part of a worker's annual statutory leave entitlement. At present, the Working Time Regulations 1998 (SI 1998/1833) provide that 'a worker is entitled to four weeks' annual leave in each leave year'. In general, employees work a five-day week, and thus would be entitled to 20 days annual paid leave. Part-time workers have a pro rata entitlement based on the number of hours worked. These regulations do not explicitly state that bank holidays are to be in addition to this entitlement, and some employers have counted them as forming part of the 20 day entitlement (or its pro rata part-time equivalent).

7.56 If no-one was presently entitled to paid leave on bank holidays, there would be an additional eight days of annual leave for which all employers would need to pay. Assuming that employees typically work a five-day week, this would be equivalent to a 3.2 per cent increase in their annual earnings. Thus the maximum possible increase to the wage bills of the total economy would be 3.2 per cent. However, most employees already enjoy this entitlement.

7.57 Table 7.2 below, drawing on information from the Labour Force Survey (LFS), shows that in Autumn 2003 around 83 per cent of the workforce were already receiving 20 days or more paid leave (not counting the eight bank holidays). Fewer than eight per cent of full-time employees were not receiving at least 20 days. Even half of all part-time workers got 20 days or more paid leave.

Table 7.2 Paid Leave Entitlement (Excluding Bank Holidays) for Working Age Employees by Hours, Autumn 2003

Paid leave entitlement (per cent)	Part-time	Full-time	All
Fewer than 10 days	23.4	1.7	6.3
10 to fewer than 12 days	4.7	0.8	1.6
12 to fewer than 20 days	23.1	5.3	9.1
20 days or more	48.8	92.2	82.9

Source: LFS, September–November 2003.
Note: Figures may not sum to 100 due to rounding.

7.58 Due to the lack of adequate data, there are difficulties in determining the pro rata entitlement for part-time employees, but three-quarters of part-time workers received at least 10 days paid leave excluding bank holidays.

7.59 We estimate that, at most, the new entitlement would add 0.25 per cent to the total wage bill for full-time employees and 0.75 per cent to the total wage bill for part-time employees. We arrive at this figure by multiplying the maximum 3.2 per cent increase which applies to full-time workers benefiting by estimates of how many are affected and by how much. Overall, the impact would amount to, at most, an additional 0.4 per cent on aggregate wage bills.

7.60 Most full-time employees along with many part-timers are already getting this entitlement. The implication is that for the vast majority of employers the proposed legislation will have little or no impact. Conversely however, for a few employers the impact may be considerable.

7.61 Our main concern is the potential impact on low-paying sectors. Table 7.3 shows paid leave entitlement for those employees earning £4.50 or less an hour[1]. In Autumn 2003 out of a total of around 950,000 full-time employees earning £4.50 and below, around a quarter (about 230,000) did not get 20 days paid holiday. However, around 90,000 of these had been with their employer for less than a year and so would only have been entitled to a lesser number.

Table 7.3 Paid Leave Entitlement (Excluding Bank Holidays) for Low-paid Working Age Employees by Hours, Autumn 2003

Paid leave entitlement (per cent)	Part-time	Full-time	All
Fewer than 10	41.1	6.8	24.4
10 to fewer than 12 days	4.2	3.4	3.8
12 to fewer than 20 days	18.2	14.0	16.1
20 days or more	36.6	75.8	55.7

Source: LFS, Autumn 2003.
Notes:
1. Those earning £4.50 or less in Autumn 2003, when the adult minimum wage was £4.20 in September 2003 and £4.50 in October 2003.
2. Figures may not sum to 100 due to rounding.

7.62 Further, there were about one million part-time employees paid £4.50 or less in Autumn 2003. Of these part-time employees, about 41 per cent (410,000) received fewer than ten days paid leave. However, nearly half (195,000) had been with their employer for less than a year.

7.63 Overall, this suggests that no more than 230,000 low-paid full-time employees received less than their full paid leave entitlement and maybe 400,000 low-paid part-timers received fewer than 10 days paid leave.

7.64 On these figures, the annual cost of total compliance to employers of low-paid employees could add up to 1.1 per cent to their annual total wage bill. However, the impact would not be spread evenly; it would be nil for some employers, but higher (potentially up to 3.2 per cent) for others.

7.65 We do not believe, therefore, that the proposed change will have an impact so large or so widespread as to make further upratings of the minimum wage inappropriate, but we note that the pace of introduction will determine the severity of adjustment difficulties in specific firms.

1 The income data in the LFS are self-reported and many responses are proxy responses from other household members. Thus, care should be taken in interpreting estimates of the number of those working in low-paid jobs derived from the LFS. It should be noted that the adult minimum wage was uprated from £4.20 to £4.50 in October 2003. We use £4.50 or below as the measure of low pay in this analysis. According to the LFS, using the derived hourly wage variable, around one million full-time employees were paid £4.50 or below in Autumn 2003.

The timing of the implementation is presently uncertain and dependent both upon Government intentions and the Parliamentary schedule. We have based our recommendations on the assumption that the full impact will not occur within the two years covered by this report. We will take the additional costs into account in future years.

Public Sector

7.66 As we have noted in previous reports, agreements for public sector wage rates tend to be reached at levels above the minimum wage. Accordingly, the estimated effect of the new recommended rates on public sector wage bills is small.

7.67 We asked the Government to provide estimates of the impact on public expenditure of hypothetical 10 pence and 30 pence increases in the adult rate of the minimum wage. The estimated full-year savings for the Exchequer are shown in Table 7.4 below.

Table 7.4 Government Savings from an Increase in the Adult National Minimum Wage, £ million, 2005/06

	Savings from a 10 pence increase	Savings from a 30 pence increase
Income Tax	51	141
National Insurance Contributions	25	66
Working Tax Credit	21	69
Child Tax Credit	5	14
Pension Credit	1	3
Income Support/Job Seeker's Allowance	3	6
Housing Benefit	9	24
Council Tax Benefit	3	10
Total of above	118	333

Source: Department for Work and Pensions estimates based on 2002/03 Family Resources Survey data, uprated to 2005/06 and Inland Revenue estimates based on 2002/03 Family Resources Survey data, uprated to 2005/06.

7.68 Increasing the minimum wage in line with our recommendation for 2005 is therefore estimated to save around £225 million in a year. This figure is indicative only. The estimate assumes no behavioural response on the part of workers or employers and does not take into account the impact on corporation tax. It also excludes the cost to public sector wages and any higher prices for purchasing goods and services resulting from the minimum wage uprating, e.g. the price of contract cleaning may rise.

The Impact on Low Incomes

7.69 The National Minimum Wage is part of a wider Government strategy to make work pay and to improve the financial incentive for people to go out to work. It complements the tax and benefits system. For many of those earning the minimum wage, their overall household income will be substantially supplemented by tax credits and benefits.

7.70 In April 2003 the Government reformed the tax and benefits system, introducing the Working Tax Credit (WTC) and the Child Tax Credit. The WTC builds on the old Working Families Tax Credit and provides financial support on top of earnings, to improve incentives for households moving into work at low earnings. The 2004 Pre-Budget Report (HM Treasury, 2004c) provided details of minimum income guarantees for April 2005 as a result of the WTC and the £4.85 per hour adult rate of the minimum wage. These were:

- £258 a week for a family with one child and one earner working for 35 hours on the adult rate of the minimum wage;
- £198 a week for a single earner couple without children or a disability, aged 25 or over and working for 35 hours on the adult rate of the minimum wage.

7.71 In the first example shown, the £4.85 per hour adult rate of the minimum wage would thus be topped up to £7.37 per hour take-home pay once tax credits and benefits are taken into account. The second example equates to an hourly rate of £5.66.

7.72 Our recommendations for future rates of the minimum wage will further improve incentives to move into work. An important feature of the new tax credits is that any increase of less than £2,500 on the previous year's family income does not affect that year's tax credit assessment. This means that recipients do not see their tax credits reduced as soon as their income rises and therefore workers on the minimum wage will receive the full benefit of the increase until the end of the tax year, when their tax credit will be reassessed.

Future Reviews

7.73 We noted earlier in this Chapter that some business representatives would favour a form of indexation to make future upratings more predictable. Other employers called for more notice of upratings and a few, particularly in the retail sector, suggested that they take effect in April each year. At present the Low Pay Commission conducts biennial reviews (normally published in March) for implementation in October of

'The six months' notice (March to October) in year one is insufficient for many businesses which budget on, for example, a January to December basis.'

British Hospitality Association evidence

the same year and October of the following year. The British Retail Consortium (BRC) saw this as out of step with the financial year used by many companies, obliging them to adjust pay budgets (set at the start of the financial year) by means of a second pay review in October designed to ensure compliance with the minimum wage.

7.74 The BRC was also concerned that minimum wage upratings should be 'sensitive to changes in economic conditions' and take account of evidence on the impact of the most recent upratings, even if this reduced the time between the announcement of changes and their implementation. In contrast, the British Chambers of Commerce and the British Hospitality Association called for longer notice of upratings. The CBI commented that some firms would prefer announcements to be made in April for implementation in October the following year, thus giving 18 months notice. BUPA Care Services suggested that the Commission make recommendations for the next three years and the Independent Care Organisations Network recommended a rolling review programme. However, the Hairdressing Employers Association and the National Hairdressers' Federation were concerned that small firms found it difficult to keep abreast of new rules and regulations and called for 'no change to the architecture of the National Minimum Wage for a period of at least two years'.

7.75 These comments highlight some of the difficulties in determining the most appropriate timetable for the review cycle. While on the one hand some firms would like more notice of future upratings, there is also a need to make recommendations based on timely information on economic conditions. The current timetable for submitting our reports to Government is largely determined by the availability of data from ASHE, which, like its long-running predecessor the New Earnings Survey, is collected by the Office for National Statistics (ONS) in April each year. Although the ONS has been able to push forward publication of the data to October to assist the Commission, we are unable to obtain the data any earlier and this means there is little scope to change our timetable for reporting to Government.

7.76 If minimum wage upratings were implemented in April each year, this would address one of the BRC's concerns, since the full impact of the most recent upratings should be captured in the April ASHE data. However, the notice period would be significantly reduced, perhaps to as little as one month, and employer organisations have indicated previously that a notice period of less than six months would be difficult to manage. October was originally selected as the best time of year for implementing changes to the minimum wage as it was a relatively quiet period for pay settlements (reducing the impact of upratings on pay increases throughout the economy). Furthermore, firms and individuals are now aware that minimum wage upratings take effect from October and many firms have adjusted their pay settlement dates to take account of the minimum wage.

7.77 A further option which the Commission considered as a means to give employers more certainty was a rolling two-year review programme. This would mean that we would submit reports to the Government each February, reviewing our recommendations for the coming October (which were first made a year earlier) in the light of more recent economic data, and making recommendations for October of the following year. In practice this would mean that we would undertake annual reviews, an option we rejected in Volume Two of our third report (2001) for a number of reasons, including the burden this would place on those responding to our consultations. We were concerned that an annual process would not allow adequate time to carry out a comprehensive review or to properly consider how the minimum wage operates in practice.

7.78 While we recognise that there are some disadvantages associated with the timing of our reviews and the effective date for minimum wage upratings, the other options which we considered present difficulties as well. We have found no ideal solution which would address all the points raised by the different interest groups. Given that the present system is increasingly familiar to those affected by the minimum wage, and that we believe it is working reasonably well, we do not propose any changes. Nevertheless, we will keep the issue under review.

Conclusion

7.79 At the time of the fourth report (2003) we stated a medium-term objective (para 6.39):

> 'We believe that there is a case for increasing the effective level of the minimum wage, implying a series of increases for a number of years above average earnings, and increasing gradually the number of people benefiting. We are also however, conscious of the need for caution in economic conditions which could prove difficult. We have therefore decided not to recommend the full adjustment to a new level in two years, but to take a partial step towards that end….'

Since we set out that objective, economic conditions have improved. Economic growth has turned out to be stronger than the consensus expected, while inflation has been well contained within the Bank of England's target. Employment has continued to be robust, and our research has not identified any significant adverse consequences resulting from the minimum wage. The effect of the October 2004 uprating has not yet been fully captured in the published data. Even so, the overall economic situation remains sufficiently robust that we feel confident in recommending a further uprating of the minimum wage that, taken over the next two years, achieves a modest uprating relative to average earnings.

7.80 But we have also noted some concerns. Many employers and their representative organisations have expressed serious misgivings about the recent pace of minimum wage increases. The last two increases, amounting to 15.5 per cent over two years, have caused problems with existing reward structures in large companies as well as small. The 7.8 per cent uprating of the adult minimum hourly rate in October 2004 came too late to be fully reflected in the data we were able to analyse.

7.81 Our recommendations strike a balance between these different considerations and concerns. They continue the increase in the level of the minimum wage relative to average earnings which we proposed in our fourth report (2003) but at a gradual pace and with a smaller increase in the first year to allow business the chance to absorb fully the impact of the 2004 upratings.

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

Association of Convenience Stores

British Apparel & Textile Confederation

British Beer & Pub Association

British Hospitality Association

British Retail Consortium

Business in Sport and Leisure

Business Services Association

CBI

Community

Cleaning and Support Services Association

GMB

Hairdressing Employers Association

Independent Care Organisations Network

National Farmers' Union

National Hairdressers' Federation

Trades Union Congress

Transport and General Workers' Union

Union of Shop, Distributive and Allied Workers

UNISON

Written Evidence to the Commission

Article 12 (joint submission with British Youth Council, Children's Rights Alliance for England, Child Poverty Action Group, National Children's Bureau, NCH Children's Charity, UK Youth Parliament)

Association of Charity Shops

Association of Chartered Certified Accountants

Association of Convenience Stores

Association of Licensed Multiple Retailers

Association of London Government

British Apparel & Textile Confederation

British Association of Removers

British Beer & Pub Association

British Chambers of Commerce

British Hospitality Association

British Retail Consortium

British Shops and Stores Association

British Youth Council (joint submission with Article 12, Children's Rights Alliance for England, National Children's Bureau, NCH Children's Charity, Child Poverty Action Group, UK Youth Parliament)

BUPA Care Services

Burfield & Co. (Gloves) Ltd

Business in Sport and Leisure

Business Services Association

CBI

Central Council of Physical Recreation

Centrepoint

Cheshire County Council

Child Poverty Action Group (joint submission with Article 12, British Youth Council, Children's Rights Alliance for England, National Children's Bureau, NCH Children's Charity, UK Youth Parliament)

Children's Rights Alliance for England (joint submission with Article 12, British Youth Council, Child Poverty Action Group, National Children's Bureau, NCH Children's Charity, UK Youth Parliament)

Citizens Advice

Cleaning and Support Services Association

Communication Workers Union

Community

Disability Rights Commission

Dyfed Cleaning Services Limited

East Riding and Hull Care Association

EEF The manufacturers' organisation

Employers' Organisation for Local Government

English Community Care Association

Equal Opportunities Commission

Equity

Federation of Licensed Victuallers Associations

Federation of Small Businesses

Food and Drink Federation

GMB

Her Majesty's Government

Institute for Employment Studies

Kenmar Products Ltd

Landwell

Leicester City Council

Leonard Cheshire

Lincolnshire Association of Registered Care Homes

Local Authority Caterers Association

Manchester Metropolitan University Business School, Centre for Hospitality and Employment Research

MCCH Society Ltd

Michelsons Limited

National Association of Master Bakers

National Children's Bureau (joint submission with Article 12, British Youth Council, Children's Rights Alliance for England, Child Poverty Action Group, NCH Children's Charity, UK Youth Parliament)

National Council for One Parent Families

National Farmers' Union

National Federation of SubPostmasters

National Hairdressers' Federation

NCH Children's Charity (joint submission with Article 12, British Youth Council, Children's Rights Alliance for England, Child Poverty Action Group, National Children's Bureau, UK Youth Parliament)

Northern Ireland Amusement Caterers' Trade Association

Nottinghamshire County Council

Professional Association of Teachers

Scottish Food and Drink Federation

Scottish Licensed Trade Association

Scottish Low Pay Unit

Scottish Trades Union Congress

Tenant Farmers Association

The Bingo Association

The Cinema Exhibitors' Association

The Directory Distribution Company

Trades Union Congress

Transport and General Workers Union

UK Youth Parliament (joint submission with Article 12, British Youth Council, Children's Rights Alliance for England, Child Poverty Action Group, National Children's Bureau, NCH Children's Charity)

Union of Shop, Distributive and Allied Workers

UNISON (joint submission with YMCA England)

United Kingdom Care Home Association Limited

Unquoted Companies Group

Welsh Assembly Government

White Horse Child Care Limited

Working Men's Club & Institute Union Limited

YHA (England and Wales) Ltd

YMCA England (joint submission with UNISON)

Young People's Rights Network

Zacchaeus 2000 Trust

Visits and Meetings

England

Agricultural Wages Board for England and Wales

ASDA

Association of Convenience Stores

Association of Licensed Multiple Retailers

British Apparel & Textile Confederation

British Beer & Pub Association

British Chambers of Commerce

British Hospitality Association

British Retail Consortium

British Shops & Stores Association

British Youth Council

Business Services Association

Business in Sport and Leisure

CBI

Central Council of Physical Recreation

Centrepoint

Children's Rights Alliance for England

Citizens Advice

Citizens Advice Maidstone

Cleaning and Support Services Association

Commission for Racial Equality

Disability Rights Commission

EEF The manufacturers' organisation

Equal Opportunities Commission

Ethical Trading Initiative

Federation of Small Businesses

Hairdressing Employers Association

Holly House Farm

Independent Care Organisations Network

Independent Retailers Confederation

Institute of Directors

Judy Scott Consultancy

MCCH Society Ltd

MITIE Group

National Association of Master Bakers

National Day Nurseries Association

National Farmers' Union

National Hairdressers' Federation

National Group on Homeworking

Rose & Crown Hotel

Rural Shop Alliance

Sector Skills Development Agency

Skillsmart

Sodexho UK

Sunclose Farm

Sure Start Unit

The Coventry Partnership

The East London Citizens Organisation (TELCO)

Trades Union Congress

Transport and General Workers Union

UNISON

Union of Shop, Distributive and Allied Workers

Women and Work Commission

YMCA England

Northern Ireland

CBI Northern Ireland

Fermanagh Homecare Services

Fitzwilliam International Hotel

Northern Ireland Textiles and Apparel Association

Quality Speed Cleaners

Robinsons Cleaning and Support Services Ltd

Sperrin Caring Services

UNISON Northern Ireland

Scotland

Edinburgh and District Trade Council

Edinburgh Voluntary Organisations' Council

National Federation of Retail Newsagents Scotland

Poverty Alliance

Scottish Association of Master Bakers

Scottish Building Employers Federation

Scottish Executive

Scottish Federation of Meat Traders Associations

Scottish Grocers' Federation

Scottish Licensed Trade Association

Scottish Low Pay Unit

Scottish Retail Consortium

Scottish Trades Union Congress

Transport and General Workers' Union Scotland

Wales

Coray and Co Ltd

MITIE Cleaning South Wales Ltd

Simon Constantinou Hair Salon

Toy Box Day Nursery

Welsh Assembly Government

Low Pay Commission Research Projects

Overview

1 We commissioned thirteen research projects to expand our knowledge of the impact of the minimum wage. This section provides an overview of the main findings. Further information on the projects is included in Table A2.1.

2 Evidence is accumulating that the minimum wage is now having a widespread influence in the labour market. Incomes Data Services (IDS) (2004b and 2004c) examined the impact of the 2003 and 2004 upratings and found that, in addition to setting the pay agenda for the main low-paying sectors, the minimum wage also exerted an important influence in parts of the economy where most pay rates were well above the minimum wage. An increasing number of companies had moved their pay review dates to October and the minimum wage now functioned as the key rate for many low-paying firms, as well as a benchmark for higher-paying firms to rise above.

3 Despite the expanded influence of the minimum wage in the labour market, there are few signs that employment or hours worked have been adversely affected. Galindo-Rueda and Pereira (2004) found evidence 'of employment growth being significantly lower in the 1998–1999 period for service sector firms which are expected to be more affected by the NMW as a result of them being part of a given industry sector and region'. As an indication of the magnitudes involved, the authors reported that employment growth in firms belonging to a sector and region with a share of 10 per cent of workers in 1998 paid below the 1999 minimum wage level, was 0.12 per cent lower than for firms with 9 per cent of workers paid below the 1999 minimum wage. No significant effects were found in the manufacturing sector.

4 Stewart and Swaffield (2004) also found some adverse effects. They attempted to gauge whether hours worked by the low-paid had changed in response to the introduction and subsequent upratings of the minimum wage. They found that while the initial effects were insignificant, the longer-term adjustments were slightly more significant. Taking lagged-effects into account, the evidence suggested that the introduction of the minimum wage had resulted in a reduction of between one and two hours per week in basic working hours for both men and women. They were unable, however, to determine whether this reduction was a result of employee choice or imposed by employers.

5 If the minimum wage boosts take-home pay then individuals may no longer need to have more than one job in order to maintain income levels. Conversely, if hours worked decline in response to upratings of the minimum wage, then individuals may take second jobs in order to earn enough money. Robinson and Wadsworth (2004) considered this issue but statistical analysis revealed no discernible influence of the minimum wage on the probability of individuals holding second jobs.

6 Dickens and Draca (2005) examined whether there were any employment effects arising from the 2003 minimum wage upratings. They found no statistically significant effects (either positive or negative) on employment, although they found that the 2003 upratings affected fewer workers than previously and the lower coverage reduced the probability of observing significant disemployment effects.

7 Research by Ram, Edwards and Jones (2004) suggested a less benign interpretation of the data showing a reduction in working hours: some firms lowered *reported* hours worked in order to appear compliant with the minimum wage. The authors examined the experiences of small firms in two sectors noted for low pay and informal working: catering and clothing. In some instances even the highest paid members of staff, and sometimes the owners, were earning less than the minimum wage. For the majority of the firms in the study, the reasons given for non-compliance were disadvantageous business conditions and a perception that the business could not afford to pay the minimum wage.

8 Croucher and White (2004) studied the enforcement process and found it was working reasonably well, with both employers and workers generally satisfied with the process and the role of the Inland Revenue's compliance officers. There were, however, some important caveats. There was some criticism about the length of time taken to complete investigations and, in a few cases, the complainant had

concerns about the confidentiality of the process. The research also highlighted a need for greater attention to be paid to the post-investigation period to ensure that the worker received the correct amount owed promptly and in full.

9 Machin, Draca and Van Reenen (2005) examined the impact of changes in the minimum wage on profits and prices. They noted that if employment effects were small '… this does beg the question as to how firms are able to sustain the higher wage costs induced by minimum wages. It is evident that, if employment effects are small, then something else has to give. One possibility is that the minimum wage eats into profit margins, or raises prices.' They did find some support for the hypothesis that profit margins were squeezed in firms that were more affected by the introduction of the minimum wage, although it was hard to find evidence that a significant proportion of these low-wage firms were forced out of business. Furthermore, they were unable to detect significant price effects.

10 The impact of minimum wage upratings on small, formal sector firms was also investigated. Cronin and Thewlis (2004) found concern about the current level of the minimum wage, with some employers claiming that the latest increases had been 'arbitrary'. Adjustments made by firms in response to the upratings included reducing hours by sending staff home during quiet times and consolidating bonuses into hourly rates. Firms operating in consumer markets could partly offset their costs by raising prices, but those serving other businesses felt they lacked the pricing power to enable them to follow suit. Cronin and Thewlis also reported the tendency of those in the hairdressing sector to take on fewer young staff, trainees and inexperienced staff.

11 Indeed the position of young people in the labour market has been a special focus of attention for the Low Pay Commission . Neathey, Ritchie and Silverman (2004) focused on the position of young people in the two largest low-paying sectors of the economy, namely retail and hospitality. In general, employers exhibited a preference for workers slightly older than 16–17, and the range of opportunities available to workers increased as they reached 18 and above. But employment of young people was generally based on pragmatic considerations, such as the availability of labour.

12 IDS (2005) investigated the changing use of age-related pay for 18–21 year olds since the introduction of the minimum wage. Age-related pay was not widespread, particularly for those aged 18 and above. There were two trends, in opposing directions. First, a move to increase the

age at which adult rates were paid to 22 in order to offset the cost of the minimum wage and second, a longer-term trend to reduce the age at which adult rates were paid down to age 18. There was no significant evidence of an overall increase in the number of employers using age-related pay.

13 Bryan and Taylor (2004) studied the characteristics of households containing at least one minimum wage worker. They found that the minimum wage recipient tended to be the spouse of the head of the household or another adult member of the household, rather than the head of the household. Moreover, some young workers earning the minimum wage still live in the family home. Minimum wage households were not the poorest households (these consisted mainly of pension and benefit recipient households) but were concentrated in the bottom 30 per cent of the income distribution of *working-age* households.

14 Whether beneficiaries of the minimum wage remain in low-paid work, or whether it is a temporary staging post from which they quickly move up the earnings distribution is a matter of some interest. Sloane, Murphy, Jones and Jones (2004) examined this issue and found that minimum wage employment was indeed characterised by high levels of ‘churning’, with 40 per cent moving into higher-paid employment a year later, 4 per cent exiting into unemployment and 12 per cent becoming economically inactive.

Table A2.1 Low Pay Commission Research Projects

Contractor	Aims and Objectives	Methodology	Results
M. Bryan and M. Taylor (Institute for Social and Economic Research, University of Essex)	To analyse household characteristics of minimum wage recipients across the household income distribution.	The British Household Panel Survey (BHPS) (wave 12) was used to: assess the characteristics of minimum wage households (single/multi-earner, marital status, number and age of children, housing tenure and head of household's personal characteristics); examine the position of minimum wage households in the overall household income distribution; and project hourly wages and wage profiles in order to estimate the predicted gains from the October 2003 uprating.	Looking at the income distribution of all households, the researchers found that minimum wage households were not concentrated at the bottom (those at the bottom consisted mainly of pension and benefit recipient households). Minimum wage households were, however, concentrated at the bottom of the income distribution of working-age households, and of working-age households in which at least one individual was in work. Equal proportions of minimum wage households, all working households and all households had female heads of household. Heads of minimum wage households were, however, more likely to be older and less educated than heads of other working households. Minimum wage households were more likely to contain children, although these children tended to be older than those in other working households. Minimum wage households typically contained multiple earners and were far more likely than other working households to contain three or more earners. The spouse of the head of household, or other adult members of the household, were most likely to receive the minimum wage. Estimated wage growth profiles suggested that, on average, minimum wage households gained £6.23 per week from the 2003 uprating.

Table A2.1 Low Pay Commission Research Projects

Contractor	Aims and Objectives	Methodology	Results
E. Cronin and M. Thewlis (IRS Research)	To investigate firms' adjustments to the National Minimum Wage, including the effect on pricing decisions, profitability, employment, productivity and training.	The project consisted of three stages: face-to-face discussions with four employer trade associations and the Trades Union Congress to identify key issues to explore during the research; postal survey of 4,000 small businesses seeking their views on the minimum wage and information on its impact on their business; and 53 interviews with firms across the UK, of which 50 employed fewer than 100 employees. The sectors covered by this study were: cleaning and facilities management; catering and food processing; security; packing and distribution; hospitality; hairdressing; retail; and small office based companies.	Employers were generally positive about the introduction of the National Minimum Wage but the October 2003 and 2004 upratings were causing concern. Employers found it difficult to isolate the impact of the minimum wage from other employment legislation but, among the 265 respondents to the questionnaire, nearly three-fifths reported that the minimum wage had affected pay levels and over a half reported an effect on profits. Results from the interviews indicated that the nature of the businesses made it difficult for employers to substitute labour with machinery or to make changes to working practices to improve productivity. Instead, among interviewed firms, one-tenth of employers made changes to their pay scales and structures as a coping mechanism for the minimum wage. Just under two-fifths of employers reported reducing staff hours and a similar proportion had reduced staffing levels. In the hairdressing sector, employers were either reluctant to hire young staff or trainees, or had cut down on the number of trainees employed in recent years. Overall, businesses operating in consumer markets (cafes, hotels etc.) were able to increase their prices but those operating in business-to-business markets (e.g. packing, cleaning and security) were unable to do so. Employers reported that where they were able to raise prices, this did not cover the full costs of increases caused by the minimum wage and other legislation.

Table A2.1 Low Pay Commission Research Projects

Contractor	Aims and Objectives	Methodology	Results
R. Croucher (Cranfield University) and G. White (University of Greenwich)	Research on the enforcement of the National Minimum Wage.	The Inland Revenue contacted over 1,000 people involved in National Minimum Wage investigations inviting them to take part in the research. This resulted in a total of 70 semi-structured telephone interviews (43 with employers and 27 with workers and ex-workers) and 12 follow-up face-to-face interviews. None of the employers in the sample had had an enforcement notice issued against them.	The enforcement process was working reasonably well but there were specific areas of concern. Overall, both employers and workers found the approach taken by the Inland Revenue's compliance officers to be courteous and helpful. Many employers claimed to be unclear about the detail of the minimum wage and hence had underpaid through ignorance rather than intent. For most employers the Inland Revenue's visit had come as a surprise and most seemed unaware of the penalties involved in non-payment of the minimum wage. Over half the employers had pay records that were deficient in some way and a major benefit of the process was seen as the advice given by the Inland Revenue in improving these. Most employers claimed not to have experienced any difficulty in meeting the arrears owed but a minority had. Awareness of the existence of the National Minimum Wage was generally good among workers but many were not clear, before the enforcement process, if it applied to them. Their most common source of information was through family and friends. Both workers and employers felt that there needed to be greater publicity given to the detail of the minimum wage due to the complexity of the regulations. Over half the workers had approached their employer prior to a complaint but had received a negative response. Some had decided to resign before making a complaint. All but one worker had received arrears payments following enforcement action, but it was not always clear that they had received their full entitlement. In some cases, employers had pressurised workers into accepting less than the amount owed. A key criticism of the process by both employers and workers was the length of time taken to complete an investigation. Some workers also had concerns about the confidentiality of the process.

Table A2.1 Low Pay Commission Research Projects

R. Dickens (Queen Mary, University of London and Centre for Economic Performance, London School of Economics) and M. Draca (Centre for Economic Performance, London School of Economics)	To estimate employment effects of the 2003 National Minimum Wage uprating.	The researchers used Quarterly Labour Force Survey (QLFS) data (October 2002–March 2004) to provide revised estimates of the coverage of the 2003 uprating. They used a difference-in-difference analysis of employment transitions out of employment among affected low-paid workers (the treatment group) and their counterparts further up the distribution (the control group). They also analysed transitions into low-pay employment.	The hourpay variable (weekly earnings divided by weekly hours) in the LFS continues to be highly ineffective in measuring the incidence of minimum wage affected workers. Revised estimates of the incidence of affected workers indicated that the 2003 uprating affected fewer workers than the initial introduction of the minimum wage or the 2001 uprating. The analysis revealed insignificant negative effects on the employment retention rates of all adults and, most notably, male workers. And analysis of employment inflows uncovered insignificant negative effects for females and some potential 'noise' in the estimates for males (due to lower sample numbers). But the results were not statistically significant from zero. Arguably the lower coverage of the 2003 uprating reduced the probability of observing significant disemployment effects.
F. Galindo-Rueda (Centre for Economic Performance, London School of Economics) and S. Pereira (Yale University and University College London)	To assess the impact of the minimum wage on productivity and unit labour costs in low-paying sectors.	The researchers used data from the New Earnings Survey (NES) (to assess workers' exposure to the minimum wage) and the Annual Business Inquiry (ABI)/Annual Respondents Database (ARD) (for business level information). Information from firms in the ABI was linked to individual workers in the NES to calculate a measure of the firm's exposure to the minimum wage. Firm-level exposure by industry and region was also considered. Firm entry and exit was analysed using information from the Inter-departmental Business Register (from which the ABI is drawn). They used difference-in-difference methodology for their analyses.	Using a matched employer-employee data set, the results showed that wages and labour productivity were slightly positively affected in service sector firms more exposed to the introduction of the minimum wage, but there was no evidence of employment or total factor productivity effects. No effects were found in the manufacturing sector. Evidence was found of employment growth being significantly lower in the 1998–1999 period for service sector firms in industry sectors and regions expected to be more affected by the minimum wage. Employment did not decline, but grew at a lower rate. This lower employment growth was paralleled by faster growth in unit labour costs, implying a labour demand elasticity of about –0.5. Positive, but barely significant, effects of minimum wage exposure on labour productivity and capital/labour ratios were also found. The researchers showed that for most low-paying sectors, employment and business creation was slower in areas of the country where wages needed to adjust most due to the introduction of the minimum wage, suggesting that growth was slower than it would have been in the absence of the minimum wage. The analysis suggested that firms thought to be most affected by the introduction of the minimum wage responded by reducing the speed at which they hired new workers. This appeared to have led to some modest, but not entirely robust, productivity gains. It also suggests that the minimum wage might have a slight disemployment effect that could go unnoticed (in absolute terms) when the level of the minimum wage was low and economic conditions benign.

Table A2.1 Low Pay Commission Research Projects

Incomes Data Services Ltd	To monitor the impact of the 2003 and 2004 upratings of the minimum wage in a number of low-paying sectors.	Detailed surveys of private nurseries and the hotels, leisure, pubs and restaurants and retail sectors.	The minimum wage was increasingly the key determinant of pay rates across low-paying sectors. A higher proportion of firms needed to increase their wage levels to meet the October 2003 upratings, and even more will have needed to make moves to meet the October 2004 upratings. In addition some companies were operating explicit policies to keep their lowest pay rates above the minimum wage. The minimum wage upratings have, however, only had a limited impact on the skill mix or on employment levels in companies. Companies remained divided over the need to increase pay rates further up pay structures to maintain differentials with the lowest grades. In some cases narrowed pay differentials had led to major changes in pay structures. The October 2003 upratings also closed pay differentials in companies with location-based pay systems. There was evidence that the minimum wage had led to an increasing number of nurseries and pubs and restaurants using age-related pay. In the retail sector, however, companies were moving in different directions.
S. Machin (University College, London and Centre for Economic Performance, London School of Economics), M. Draca and J. Van Reenen (Centre for Economic Performance, London School of Economics)	To research the impact of the National Minimum Wage on profits and prices.	FAME (Financial Analysis Made Easy) data were used to investigate the impact of the minimum wage on profitability. Industry-level variables were drawn from the LFS and information on consumer prices from retail price index (RPI) data. Used difference–in-difference estimation to investigate the evolution of wages and profit margins before and after the introduction (and subsequent upratings) of the minimum wage at the sector and business level. Used industry and sector data to analyse price impacts.	The research showed that profitability fell in firms that were most affected by the introduction of the minimum wage. However, low wage firms were not forced out of business by the higher wage costs resulting from the minimum wage. Absence of data on firm level prices meant that the researchers had to rely solely on an industry or product level analysis. The researchers were unable to detect evidence of higher wage costs being passed on in terms of higher prices. The researchers found that being a low wage firm, rather than being located in a low wage industry, mattered for the wage impact of the minimum wage.

Table A2.1 Low Pay Commission Research Projects

F. Neathey, H. Ritchie and M. Silverman (Institute for Employment Studies)	To research the employment of young people in the retail and hospitality sectors.	The project consisted of two stages: a postal survey and case studies. A postal survey was distributed to a random sample of 2,000 employers in the retail and hospitality sectors and 216 replies were received providing basic employment and wage data. From the respondents to the postal survey 15 case studies were selected (5 in retail and 10 in hospitality), comprising firms of various sizes and employing a mixture of young workers such as students and work-based trainees. Interviews were held with the individual responsible for the employment and pay of young people in the establishment and also with some young workers in all but one of the establishments.	There was little evidence of a link between the minimum wage and decisions to employ young workers of various ages. Case study findings indicated that the employment of young workers was often based on pragmatic considerations, such as the availability of labour. Some employers, however, showed a preference for slightly older workers compared with those in the lowest age group (16–17) and were often seeking to increase the proportion of slightly older workers in their workforce. The range of job roles available to young people seemed to increase with age. This was partly a result of legal restrictions in respect of the employment of workers under 18 in certain areas, but also due to employer perceptions of the skills and attributes of particular age groups. The majority of case study establishments and about three-fifths of respondents to the survey operated some form of age-related pay system. But this was often limited to workers aged under 18. Concentration in particular low-paying occupations was an important factor in the low pay rates received by the youngest workers. Trainee status also affected the pay rates of young people, but in most cases employers were not paying these workers below minimum wage rates.

Table A2.1 Low Pay Commission Research Projects

M. Ram (de Montfort University), P. Edwards (University of Warwick) and T. Jones (de Montford University)	Research on the relationship between the minimum wage and the informal economy.	Detailed interviews with 17 small firms in the clothing and catering sectors where 'informality' is common. Evidence from employers and employees was collected. Four firms that were minimum wage compliant were included to enable comparisons with those that did not comply. Five firms had taken part in earlier studies and provided an insight into the experiences of small firms in the 'informal' economy in the light of the existence of the National Minimum Wage for five years.	Market conditions were different in the two sectors, with intense competition between firms characterising restaurants and overseas competition being key in clothing. Since the introduction of the minimum wage little had changed in terms of the firms' attitudes to compliance. Low pay was still common and pay setting informal, with no clear process of firms moving towards compliance with the minimum wage as a result of experience. Market conditions and 'ability to pay' were key factors in determining whether the firms complied with the minimum wage. Changes to the minimum wage did not directly affect firms' pay practices. The minimum wage acted more as a broad benchmark. Operating outside the minimum wage had consequences for firms' tax and other practices, and this connected set of practices may have tightened their position outside the formal sector of the economy. Changes in labour market opportunity, rather than the minimum wage specifically, affected recruitment and retention. However, at the same time new groups of workers, notably recent immigrants, filled the gap. There were various specific reasons leading compliant firms to pay at National Minimum Wage levels or higher. Underpinning this was market conditions that allowed them to do so. For most, non-compliance was incompatible with their desire to grow their business. Firms recognised the consequential benefits of paying the minimum wage or above, for example, the ability to attract more skilled and committed workers. Although the majority of employers in the research were non-compliant with the minimum wage, many were concerned about the consequences if detected. Alleged inability to pay and the perceived remote likelihood of detection were important factors in explaining non-compliance. Under-reporting hours worked and keeping false records were common.
H. Robinson (Cardiff Business School, Cardiff University) and J. Wadsworth (Centre for Economic Performance, London School of Economics)	To research the impact of the minimum wage on the incidence of second job holding.	The researchers used difference-in-differences estimation on a panel of individuals matched against successive LFS to estimate the impact of the minimum wage on the incidence of second job holding.	The researchers found that the lower paid were more likely to hold second jobs. There was little evidence of any reduction in second job holding resulting from the introduction of the minimum wage, although many second job holders received a relatively large increase in their hourly and weekly wages. Furthermore there was little evidence that hours worked in either the first or second jobs had changed in the immediate period after the introduction of the minimum wage.

Table A2.1 Low Pay Commission Research Projects

P. Sloane, P. Murphy, M. Jones and R. Jones (University of Wales, Swansea)	To analyse flows into and out of the National Minimum Wage.	The researchers use the LFS (1999–2003) and BHPS (1999–2002) to model transitions between different market states. Looking at four starting positions (employed at minimum wage, employed above minimum wage, unemployed or economically inactive) and using LFS data, the researchers estimated the probability of being in each of those four states after five quarters, for the youth Development Rate and adult rate respectively. The LFS and BHPS were also used to assess an individual's propensity to be on the minimum wage depending on certain characteristics (such as age and gender) and estimate average duration on the minimum wage.	The researchers found that about 44 per cent of those at or below the minimum wage remained in that state after twelve months, with 40 per cent moving into higher paying jobs, 12 per cent becoming inactive and 4 per cent exiting to unemployment. Movements into employment paid at or below the minimum wage from other labour market positions were small in relative terms. There was some state dependence (i.e. the individual's labour market position in the current period depended in part on their position in the previous period). Those most at risk of being paid at or below the minimum wage included women, the less qualified, non-whites, those with shorter job tenures, part-timers, non-unionists, the less skilled and those living in Wales, Scotland and the West Midlands. It was also found that those with qualifications, mortgages, permanent contracts or employed in certain industries (in particular distribution, hotels and restaurants) were more likely to move out of minimum wage employment into higher paid jobs. The reverse was found for those with a disability, part-timers or private sector workers (particularly in small firms). The exit probability from the minimum wage was estimated at 0.68 and it was calculated that the average duration on minimum wage jobs was about 1.5 years.
M. Stewart (University of Warwick) and J. Swaffield (University of York)	To research the impact of the minimum wage on working hours for low-paid employees.	The researchers used difference-in-difference estimation on a panel of individuals matched against successive NES and LFS data to estimate the impact of the introduction of the minimum wage and subsequent upratings on the working hours for low-paid employees.	The researchers found that the 'lagged' impact of the minimum wage on working hours was more important than the 'initial' effect. Initial effects were generally small and insignificant in most cases. The evidence suggests that the introduction of the minimum wage led to a reduction in the paid hours of both male and female low-wage workers. The NES total effect (initial plus lagged) estimates indicated a reduction of between one and two basic hours per week for both men and women. Paid overtime hours for women were also reduced but there was a negligible effect on paid overtime hours for men. Estimates using the LFS were typically less significant. The LFS estimated total effects on basic hours were greater for men and lower for women than the corresponding NES estimates.

Low Pay Commission Survey of Employers

The Survey

1 For previous reports we have conducted surveys of employers in low paying sectors to provide information on how businesses have responded to and coped with the National Minimum Wage. For this report we have carried out a further survey of employers to examine the impact of the October 2003 upratings of the minimum wage and to complement the information we obtained from our research programme, written and oral evidence, and official statistics. We consider here the key findings of the survey, including the impact of the upratings on wage bills and differentials, benefits, productivity, prices and profits. In line with our last survey, we also asked additional questions of the social care and textiles sectors. The survey questionnaire can be found at the end of this Appendix.

2 As with our earlier surveys, we have targeted the sectors that were most likely to be affected by the minimum wage. Our analysis of the New Earnings Survey data indicated that hospitality, retail, social care, the manufacture of clothing, textiles and footwear, hairdressing, cleaning, security and leisure continue to be the main low-paying sectors. We adopted a similar approach to that taken for our fourth report (2003). In so doing, we aimed to maintain a level of consistency to enable comparison with the impact of the 2001 upratings. However, we developed the survey questionnaire to capitalise on the aspects from which we had previously obtained the most useful data.

3 We commissioned NOP World to undertake the administration of the survey on our behalf. A sample of firms in the low-paying sectors was selected from the Dunn and Bradstreet business database. NOP World distributed questionnaires to 32,306 employers, with an emphasis on small firms in the Summer of 2004. We are very grateful to the firms that completed and returned the questionnaires. We received 3130 replies – a response rate of 10 per cent. The response rate was 3 percentage points lower than the response rate achieved in our 2002

survey. However, the level of response has been sufficient to enable us to obtain very useful information from the survey.

4 Table A3.1 gives the response rates by sector and shows that the highest rate of response was from the social care and childcare sectors, as was the case in our 2002 survey.

Table A3.1 Responses to the Survey by Sector

	Hospitality (SIC 55)	Social care (SIC 85.31)	Textiles (SIC 17,18, 19.3)	Hairdressing (SIC 93.02)	Retail (SIC 52)	Childcare (85.32)	Security (SIC 74.6)	Cleaning (SIC 74.7)	Leisure (SIC 92.6, 92.7)	Total
Number of responses	610	699	226	222	459	473	112	102	227	3130
Response rate (per cent)	7	15	7	6	13	17	8	7	8	10

5 The respondents to the survey are not a random sample of firms in the sectors. Respondents are more likely to be affected by the minimum wage than non-respondents.

6 Table A3.2 shows that respondent firms employed nearly a quarter of a million people. This is fewer than in the 2002 survey and reflects the lower response rate to this survey. Eighty per cent of responses came from firms with fewer than 50 employees, as shown in Table A3.3.

Table A3.2 Number of Employees by Sector in the Sample

	Total number of employees	Median number of employees in each firm
Hospitality	37,308	14
Social care	34,833	23
Textiles and clothing	8,198	15
Hairdressing	1,488	5
Retail	92,092	33
Childcare	8,074	12
Security	5,357	22
Cleaning	29,714	78
Leisure	18,101	14
Total	235,165	16

Base: All firms that provided employee numbers.

Table A3.3 Size Distribution of Firms by Sector

Per cent	1 to 49 employees	50 to 249 employees	250+ employees
Hospitality	79	18	4
Social care	83	14	3
Textiles and clothing	84	14	2
Hairdressing	98	2	0
Retail	62	27	11
Childcare	94	6	0
Security	68	29	3
Cleaning	42	37	21
Leisure	82	12	6
Total	80	16	5

Base: All firms that provided employee numbers.

Impact

7 Table A3.4 shows that half of the respondents to the survey stated that their business had been affected by the October 2003 upratings of the minimum wage. The highest proportion of respondents affected were in the cleaning, childcare, retail and hospitality sectors. The most significant impact was in the cleaning sector with nearly double the proportion of respondents saying they were affected by the 2003 upratings compared with the 2001 upratings. The proportion of firms affected in the hospitality and retail sectors increased by 7 and 15 percentage points respectively.

8 According to the results of the survey, the impact of the 2003 upratings was greater on large firms with 63 per cent being affected, a 16 percentage points increase when compared with those affected by the 2001 upratings. Medium-sized and small firms also said that they had observed a greater impact from the 2003 upratings, although not so marked. Sixty-one per cent of medium-sized firms and 46 per cent of small firms said they had been affected, an increase of 8 and 2 percentage points respectively on the previous survey. Firms in the North of England were proportionately most affected at 66 per cent, with firms in Greater London being least affected at 31 per cent.

Table A3.4 Percentage of Firms Affected by the October 2003 Increases in the National Minimum Wage in Any Way

	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
Per cent	55	46	34	47	55	57	44	65	34	50

Base: All firms.

9 It is important to note that the responses to our questionnaire are likely to overstate the impact that the National Minimum Wage has had on businesses for two main reasons. First, the survey specifically targeted those low-paying sectors that were most likely to have been affected. Second, even within these sectors, those who responded were more likely to have been significantly affected than non-respondents. We tested the hypothesis of an upward bias in our fourth report (2003) through a telephone survey of a random sample of non-respondents. This confirmed that the proportion of those affected was considerably lower than in the postal survey. Those in the telephone survey had also experienced a smaller impact on their wage bill. Given these factors, the survey responses should not be taken as indicative of the overall impact on business, even in low-paying sectors. The survey does, however, provide valuable information about how those affected by the

increases in the minimum wage have coped with it and enables comparison between sectors and size of business.

Total Wage Bill

10 Table A3.5 shows that nearly three-quarters of respondents affected by the 2003 upratings had reported an increase in their wage bill of 5 per cent or more, with just over half reporting a wage bill increase of between 5 to 10 per cent. Approximately a quarter of respondents from the social care and childcare sectors reported a 10 per cent or greater increase on their pay bill. We found that significantly fewer large firms saw their wage bills rise by 10 per cent or more (6 per cent) compared with small firms (21 per cent) and medium-sized firms (17 per cent).

Table A3.5 Impact on Total Pay Bill for Those Affected by the October 2003 Increases in the National Minimum Wage

Per cent	No significant change	Increased by less than 5 per cent	Increased by 5 per cent to 10 per cent	Increased by more than 10 per cent
Hospitality	6	22	54	18
Social care	3	14	56	27
Textiles	16	27	45	11
Hairdressing	6	15	65	15
Retail	9	24	53	14
Childcare	6	15	52	27
Security	11	15	53	21
Cleaning	5	18	62	15
Leisure	9	31	45	15
Total	7	19	54	20

Base: All firms affected by the October 2003 increases in the National Minimum Wage in any way. (Fifty three per cent of firms did not answer this question.)

Differentials

11 Table A3.6 shows that almost half of those affected by the October 2003 upratings in the minimum wage had increased their lowest rate of pay in order to maintain pay differentials above the minimum wage rate. The childcare and social care sectors were again most affected. Across the sectors 35 per cent of small firms, 38 per cent of medium-size firms and 48 per cent of large firms said they had increased pay rates to maintain differentials for experienced or higher-grade staff.

Table A3.6 Impact on Pay Rates for Those Affected by the October 2003 Increases in the National Minimum Wage

Per cent	To comply with new NMW rates	To maintain pay differentials above the lowest pay rate	To maintain pay differentials for more experienced staff	To maintain pay differentials for higher grade staff (e.g. supervisors)
Hospitality	63	47	47	32
Social care	59	58	59	44
Textiles	74	38	30	21
Hairdressing	72	33	48	18
Retail	73	44	45	29
Childcare	71	48	67	58
Security	73	35	31	29
Cleaning	77	52	38	29
Leisure	75	31	47	26
Total	68	47	51	37

Base: All firms affected by the October 2003 increases in the National Minimum Wage in any way.

12 Table A3.7 shows the distribution of the highest hourly rate increased as a result of the 2003 upratings. The median for the highest hourly rate which firms reported increasing was around £5.25 per hour. For about a third of respondents affected by the increase in the minimum wage, the highest rate they had to increase was below £5.00 per hour and for less than a quarter the highest rate increased exceeded £6.49 per hour. The data suggest that the effect on the higher rates of pay was most significant in the childcare, cleaning and social care sectors, and in businesses employing more than 50 workers.

Table A3.7 Distribution of Highest Hourly Rate Increased

Per cent	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
£4.10 to £4.49	0	1	0	1	0	1	0	0	1	0
£4.50 to £4.99	34	23	38	28	40	20	35	21	31	30
£5.00 to £5.49	15	18	13	11	12	13	18	18	14	15
£5.50 to £5.99	11	13	12	12	6	11	12	18	8	11
£6.00 to £6.49	8	10	3	6	8	13	6	6	4	9
£6.50 +	19	25	18	13	20	30	18	29	18	22
No increase for higher grade staff	12	9	16	17	11	11	8	8	21	12
Mean rate increased (£)	5.79	6.16	5.58	5.35	5.63	6.12	5.34	6.10	5.60	5.85
Median rate increased (£)	5.00	5.50	5.17	5.00	5.00	5.78	5.20	5.50	5.00	5.25

Base: All firms affected by the October 2003 increases in the National Minimum Wage in any way.

Benefits

13 We asked firms affected by the 2003 increases in the minimum wage whether it had led to any benefits to their business. The results are given in Table A3.8. The greatest level of benefit noted was in staff motivation with an average of 15 per cent of firms claiming to have noticed an improvement in motivation amongst their workforces. A quarter of firms in the security sector reported an increase in motivation. Firms in the security and cleaning sectors were most likely to have experienced lower staff turnover and faster filling of vacancies. Only a small percentage of firms across the low-paying sectors said they had obtained any significant benefit from the 2003 increases, although 7 per cent of hairdressing firms reported experiencing a significant decrease in staff turnover.

14 A higher percentage of respondents from Northern Ireland (26 per cent) reported obtaining benefit from the 2003 minimum wage increases, compared with the English regions, Wales and Scotland, where approximately a tenth of firms said there had been benefits.

Table A3.8 Benefits to Business from the October 2003 Increases in the National Minimum Wage

Per cent	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
Lower staff turnover										
Significant	3	2	4	7	1	2	2	3	4	3
Slight	9	11	6	10	10	10	19	21	9	11
Higher staff motivation										
Significant	2	2	1	2	1	1	2	3	0	2
Slight	12	14	9	13	11	16	23	12	15	13
Faster filling of vacancies										
Significant	1	0	1	1	1	1	4	3	0	1
Slight	6	7	6	7	5	7	10	13	7	7

Base: All firms affected by the October 2003 increases in the National Minimum Wage in any way.

Staffing

15 Around half of the firms affected by the October 2003 increases in the minimum wage reported making a wide range of adjustments to staffing in response. Table A3.9 shows that the most significant response by businesses to the 2003 increases in the minimum wage across all the sectors was to reduce overall staffing levels, reported by 37 per cent of firms. The results show that the retail, textiles, hospitality and hairdressing sectors have been most affected in terms of staffing levels. The changes made by firms showed little variation irrespective of their location.

16 We also analysed the interaction of increased wage bill costs with the impact on staffing. This revealed that firms reporting increases in the wage bill of 5 per cent or more were most likely to have made a range of changes to their business as a result. In particular they were more likely to have decreased staffing levels and hours worked. Forty-two per cent of those with an increase in their pay bill of 5 per cent or more reported a decrease in overall staffing levels, compared with 27 per cent of those whose wage bill increased by less than 5 per cent. This is consistent with the response by firms following the 2001 minimum wage upratings.

Table A3.9 Changes Made by Firms as a Result of the October 2003 Increases in the National Minimum Wage

Per cent	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
Overall staffing levels										
Decrease	47	22	49	47	51	24	29	27	40	37
Increase	4	5	1	6	2	3	10	8	3	4
Basic hours										
Decrease	45	16	22	38	45	23	21	17	40	31
Increase	3	4	3	7	2	2	6	3	3	3
Overtime hours										
Decrease	37	19	33	17	37	23	24	19	32	28
Increase	2	5	4	6	2	3	2	3	5	3
Overtime rates etc										
Decrease	19	12	17	20	19	14	13	11	15	16
Increase	5	10	3	8	5	4	4	13	3	6
Non-wage benefits										
Decrease	16	7	4	5	11	11	6	3	7	10
Increase	2	4	0	1	0	3	2	0	0	2

Base: All firms affected by the October 2003 increases in the National Minimum Wage in any way.
Note: The remaining respondents noted 'no change'. A small percentage of firms did not answer all questions in this section and these have also been assumed to indicate 'no change'.

Productivity, Prices and Profits

17 Table A3.10 shows the range of adjustments made by firms following the October 2003 upratings. About eight out of ten firms affected experienced a decrease in profits, by far the most common change reported by firms. An increase in prices was reported by nearly two-thirds of those affected and was the key adjustment made by firms in the childcare and cleaning sectors. Other measures taken by firms differed by sector. For example, 22 per cent of hairdressing firms reported introducing new products and services, whereas in the cleaning sector only 2 per cent said they had done so. Eighteen per cent of firms in the childcare sector said that they had increased their use of unskilled or unqualified labour due to the 2003 increases in the minimum wage, compared with an average of 11 per cent across the other sectors. Firms in the hospitality sector were most likely to take measures to control non-labour costs. Over a quarter of respondents from the security sector said they had increased the quality of their goods and services, closely following by just over a fifth of respondents from the hairdressing sector.

Table A3.10 Changes in Firms as a Result of the October 2003 Increases in the National Minimum Wage

Per cent	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
Profits										
Increase	3	4	3	4	2	3	6	8	3	3
Decrease	79	88	85	77	83	77	86	75	69	81
Prices										
Increase	69	55	30	73	47	83	76	81	40	63
Decrease	1	6	6	3	4	2	2	6	4	3
Measures taken to control labour costs										
Increase	37	30	26	28	29	24	29	35	32	30
Decrease	10	6	3	12	8	6	10	5	9	8
Measures taken to control non-labour costs										
Increase	44	35	27	38	38	30	33	27	35	36
Decrease	6	9	9	8	8	12	8	11	8	9
Use of new technology/processes										
Increase	19	10	18	15	19	9	19	16	21	15
Decrease	3	5	0	7	2	6	8	7	3	4
Quality of goods and services										
Increase	13	10	9	21	8	7	27	6	15	11
Decrease	10	8	7	10	8	8	8	15	3	8
Introduction of new products and services										
Increase	18	7	15	22	18	7	17	2	21	13
Decrease	5	9	5	10	8	7	8	6	2	7
Use of unskilled/unqualified labour										
Increase	15	8	7	9	7	18	9	15	13	11
Decrease	3	3	6	10	5	5	7	2	8	4

Base: All firms affected by the October 2003 increases in the National Minimum Wage in any way.

Note: The remaining respondents noted ‘no change’. A small percentage of firms did not answer all questions in this section and these have also been assumed to indicate ‘no change’.

18 As in our 2002 survey, small firms were generally more likely than larger firms to report 'no change' when asked about the impact of the minimum wage on a range of factors in their business. Micro firms were least likely to make changes to their business as a result of the 2003 upratings. Eighty-two per cent of firms with between 6 and 200 employees reported a decrease in profits, compared with 70 per cent of firms with 201+ employees and 75 per cent of firms with 1 to 5 employees. Firms with more than 200 employees were most likely to make use of new technology and processes and to take measures to control labour and non-labour costs. There was little difference in the responses by firms based on their location. Firms in Greater London were, however, less likely to have experienced a decrease in profits or an increase in prices as a result of the 2003 upratings.

19 In the survey we asked additional questions of firms in the textiles sector. We knew from previous surveys and consultation that this sector made particular use of incentive pay schemes, so we asked about the impact of the increases in the minimum wage on incentive schemes and productivity. A quarter of all textiles firms reported that they had an incentive pay system; this rose to half amongst textile firms with 50 or more employees. Fifty-two per cent of those with incentive schemes said they had been affected by the 2003 increases in the minimum wage compared with 26 per cent of those without such a scheme. We asked whether firms had experienced any of the effects outlined in Table A3.11. Thirty-one per cent of firms in the sector reported increased costs as a result of the 2003 upratings. However, around 80 per cent of respondents reported no impact for the other four possible effects.

Table A3.11 Impact of the National Minimum Wage on Incentive Systems in the Textiles Sector

Per cent	Significant	Slight	None
Reduced differentials	9	9	82
Reduced competitiveness	11	10	79
Reduced motivation	9	12	79
Reduced productivity	6	8	86
Increased costs	16	15	70

Base: All firms in the textiles sector with an incentive scheme.

20 In previous reports we have commented on the reliance of the social care sector on local authority fees. In this survey, as in the one undertaken in 2002, we sought information on the extent to which businesses in this sector had been able to renegotiate the conditions of public service contracts following the increases in the minimum wage.

Ninety per cent of those affected by the October 2003 increases in the minimum wage in the social care sector had public sector contracts. A third tried to renegotiate their contracts to take account of increased minimum wage costs, but only 11 per cent of those that had done so had been successful, with a further 29 per cent being able to recoup part of the increase.

Pay Structures

21 Table A3.12 shows that 20 per cent of firms responding to the survey said they use age-related pay structures, although they are more common in the hospitality and retail sectors, at 31 and 30 per cent respectively, and in the hairdressing sector at 28 per cent. Security and cleaning firms were least likely to have such structures. Age-related pay structures are more likely to be used by medium-sized and large firms. Firms with age-related pay structures were asked about their minimum hourly rates but we do not know how many of their employees were paid these rates. Figure A3.1 gives the distribution of minimum pay rates for those firms in the sample with age-related pay structures and employees in the specific age group. It shows that average minimum hourly rates rise steadily with age. Around half of the firms using age-related pay paid at least the then adult minimum hourly wage rate of £4.50 for 18 year olds. This increases considerably for 21 year olds with three quarters of firms surveyed paying at least the adult minimum wage to workers aged 21. Nearly half of firms with age-related pay structures had minimum hourly pay rates below £3.80 for those aged under 18.

Table A3.12 Firms with Age-related Pay Structures

Per cent	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
Total with age-related pay	31	11	10	28	30	18	5	8	15	20

Base: All firms responding to the survey.

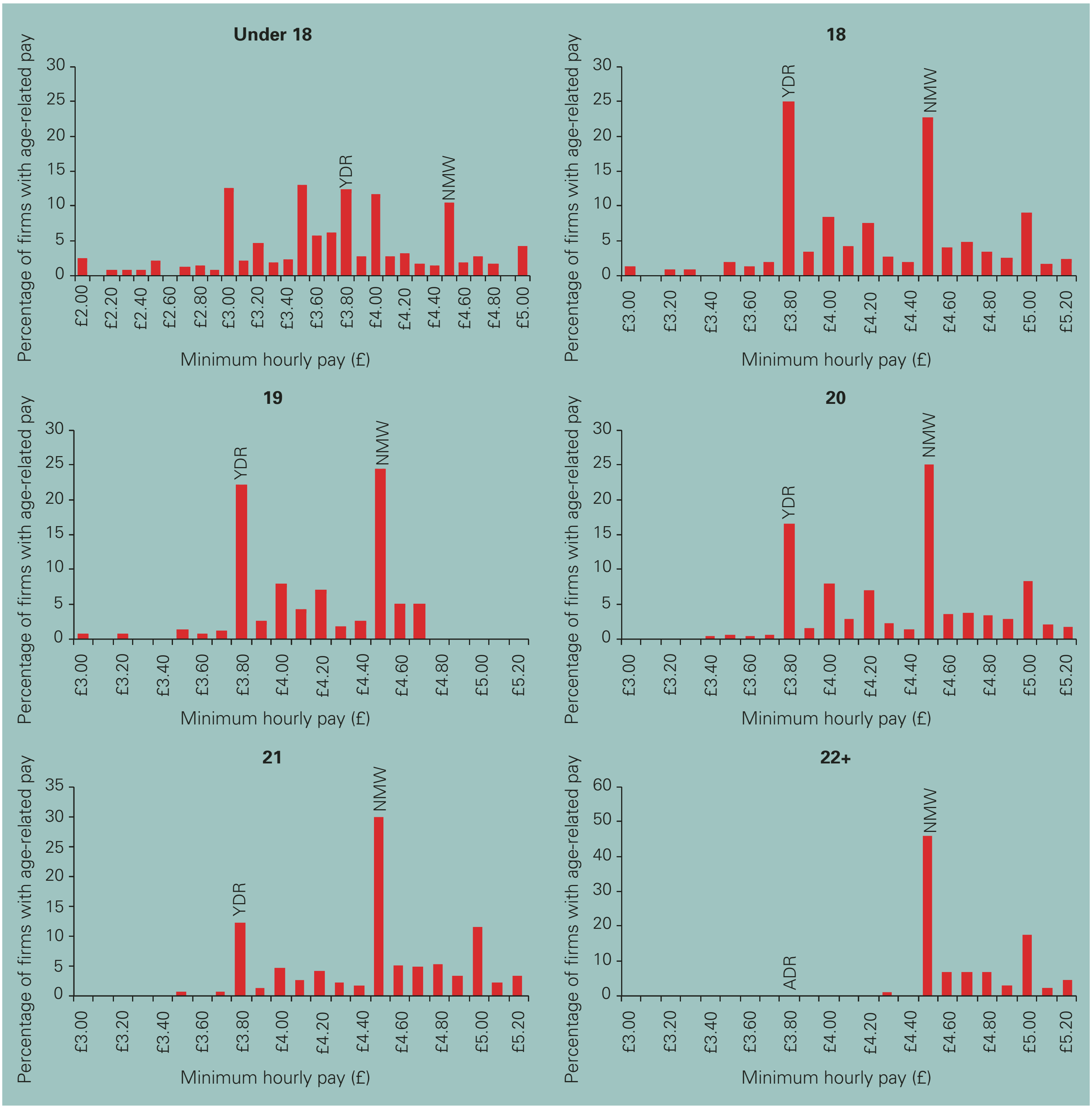
22 We asked all respondents to the survey to state the age from which they pay their full adult hourly rate of pay. Eighty per cent of all respondents provided this information. Table A3.13 shows the age groups at which respondents said they pay their lowest adult wage rate. Of these, over half pay their adult rate to employees aged 18 or under, with 78 per cent paying their adult rate to those aged 21 and under. The age at which the adult rate of pay applied differed considerably by sector. The cleaning and social care sectors were most likely to pay their adult rate to employees aged 18 or under (79 and 69 per cent respectively), whereas only 26 per cent of hairdressing firms reported doing so.

Table A3.13 The Starting Age at Which Firms Pay Employees the Adult Rate of the Minimum Wage

Per cent	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
16–17	8	11	6	1	5	9	5	26	8	8
18	45	58	49	25	33	48	39	53	51	46
19	2	1	1	4	3	1	1	0	2	2
20	2	1	2	4	3	2	5	4	1	2
21	20	17	24	28	27	14	24	7	18	20
22+	23	11	18	39	28	27	26	11	21	22

Base: All firms stating the age at which full adult rate payable (80 per cent of all firms responding to the survey).

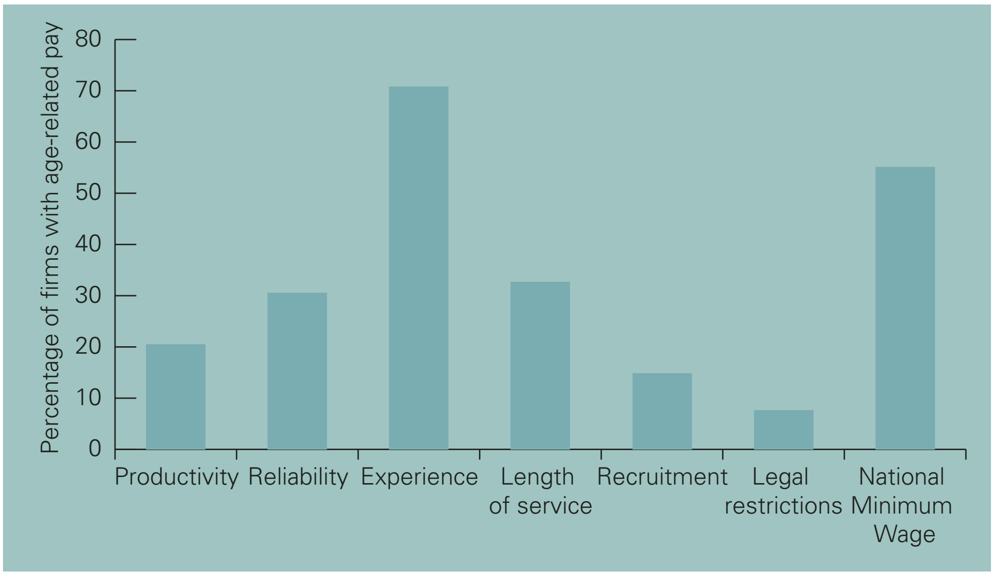
Figure A3.1 Distribution of Minimum Hourly Pay Rates by Age



Note: NMW label shows the adult NMW rate. YDR label shows the youth Development Rate. ADR label shows the older workers' Development Rate. In each case, the rate was that in place at the time the survey was conducted.

23 There were two principle reasons given by firms for using age-related pay structures (see Figure A3.2). The most common reason, cited by 71 per cent of firms, was to take account of employees' level of experience. The National Minimum Wage was the second most common reason, cited by 55 per cent of firms.

Figure A3.2 Reasons for Age-related Pay



24 For firms that do not have age-related pay structures, the two most significant factors accounting for differences in workers' pay are responsibilities, particularly in the cleaning (88 per cent), security (86 per cent) and leisure (85 per cent) sectors, and experience, particularly in hairdressing (84 per cent). Qualifications and skills came closely behind.

Development Rate

25 Only 4 per cent of respondents said they used the Development Rate for employees aged 22 or over, the same level as in our last survey. Table A3.14 shows that 11 per cent of employers in the hairdressing sector said they used the Development Rate, followed by employers in the childcare sector at 6 per cent.

Table A3.14 Percentage of Firms Using the Development Rate for Employees Aged 22 and Over

Age	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
22 +	3	3	1	11	4	6	2	0	3	4

Base: All firms.

26 We asked firms that do not currently use the Development Rate, whether they were more likely to use it when the adult minimum wage increases to £4.85 in October 2004. Twenty-two per cent of

respondents stated that they would, which is a significant increase on those currently using the Development Rate (4 per cent). Respondents most likely to use the Development Rate due to the October 2004 increases were in the hairdressing (36 per cent) and childcare (33 per cent) sectors. Some caution should, however, be taken in interpreting these results as the wording in this questionnaire may have been interpreted to include the youth Development Rate.

Substitution of Workers

27 We asked firms affected by the October 2003 increases in the minimum wage whether it made them more or less likely to employ workers in different age groups. Overall the increase has had little impact on the employment of younger workers. Table A3.15 shows that 85 per cent of respondents said it had not made a difference to their employment of 16 to 21 year olds and 88 per cent said it had not made a difference to their employment of workers aged 22 or over. More firms overall reported that they would not substitute different age groups of workers as a result of the 2003 upratings, compared with the 2001 minimum wage upratings (an increase of 13 percentage points). Eight per cent of firms with an increase in their wage bill of 5 per cent or more reported that they were less likely to employ staff aged 22 or over, compared with 4 per cent of those who experienced a smaller pay bill impact.

Table A3.15 Have the 2003 Increases in the National Minimum Wage Made You More or Less Likely to Employ Workers in Different Age Groups?

Per cent	Total
Workers aged 16–17	
More likely	6
Less likely	9
No change	85
Workers aged 18–21	
More likely	7
Less likely	8
No change	85
Workers aged 22 or over	
More likely	5
Less likely	7
No change	88

Base: All firms.

28 We also asked respondents whether the introduction of a National Minimum Wage of £3.00 for 16 and 17 year olds in October 2004 would make them more or less likely to employ workers in different age groups. The results are given in Table A3.16. The most notable outcome from responses given by firms was from the hairdressing sector. Thirty-eight per cent of hairdressing firms said that they would

be less likely to employ 16 and 17 year olds, 22 per cent less likely to employ 18 to 21 year olds, and 11 per cent less likely to employ 22 year olds or over (firms may have been unaware of the exemption for apprentices aged below 19).

Table A3.16 Will the Introduction of a National Minimum Wage of £3.00 for 16 and 17 Year Olds in October 2004 Make You More or Less Likely to Employ Workers in Different Age Groups?

Per cent	Total
Workers aged 16–17	
More likely	4
Less likely	11
No change	85
Workers aged 18–21	
More likely	4
Less likely	6
No change	90
Workers aged 22 or over	
More likely	4
Less likely	4
No change	93

Base: All firms responding to the survey.

Apprentices

29 Overall, 7 per cent of respondents employed apprentices under a Government apprenticeship scheme and 4 per cent under a contract of apprenticeship, as shown at Table A3.17. Hairdressing and childcare were by far the most significant sectors employing apprentices.

Table A3.17 Firms Employing Apprentices

Per cent	Hospitality	Social care	Textiles	Hairdressing	Retail	Childcare	Security	Cleaning	Leisure	Total
Government scheme	3	3	2	25	5	16	4	2	4	7
Contract of Apprenticeship	17	4	1	18	5	7	1	1	5	4

Base: All firms responding to the survey.

30 Table A3.18 shows that 77 per cent of all apprentices were aged 19 or under. Twelve per cent of firms employed four or more apprentices, while 43 per cent employed only one. We asked firms with apprentices to give their lowest hourly rate of pay. The average hourly rate for first year apprentices was £3.40, rising to £3.74 in year two and £4.43 in year three. The lowest rates of pay for apprentices were most likely to be found in the hairdressing sector.

Table A3.18 Percentage of Apprentices by Age Group

	16 to 17	18	19	20	21	22+
Percentage of Apprentices	34	25	18	9	7	7

Base: All firms employing apprentices.

Conclusion

31 Our survey has provided very useful information about the impact of the 2003 upratings on those sectors that are most affected by the minimum wage. The results complemented the view of the minimum wage we had obtained from our other research projects, written consultation, visits and economic analysis.

32 Half of all respondents to the survey said that their business had been affected by the October 2003 increases in the minimum wage. Three-quarters of firms affected (just over a third of all respondents) reported that their wage bill had increased by at least 5 per cent. The results suggest that the October 2003 increases have led to some compression of pay differentials, a finding which is consistent with our other sources of evidence.

33 Firms have taken a range of actions to cope with the impact of the minimum wage. Reducing staffing levels and increasing prices were the main responses, as we have seen in previous years, and some firms took more innovative measures, such as introducing new technology or products and services. However, some firms, especially in the social care sector, have found it more difficult to recoup increased costs.

34 The survey highlighted that there is still limited use of age-related pay structures, in particular beyond the age of 21. Twenty per cent of firms in the sample used age-related pay structures, which is in line with the results of the survey we carried out in 2002. Seventy-eight per cent of all responding firms paid their adult rate from age 21 or younger.

NATIONAL MINIMUM WAGE SURVEY

1. How many workers in total does your business currently employ? How many are men? And how many women? (Please include all workers - full-time, part-time, and casual staff) *(Please insert numbers)*

Total [ ] Men [ ] Women [ ]

2. How many workers in your business are aged...? *(Please insert numbers)*

16 to 17 [ ] 18 to 21 [ ] 22 or over [ ]

3. Has the October 2003 increase in the National Minimum Wage affected your business in any way?

Yes *(go to Q4)* [ ] No *(go to Q10)* [ ]

4. What has happened to your TOTAL pay bill (Including any extra payments needed to maintain differentials) as a result of the October 2003 increase in 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% [ ]

5. If you have increased the pay rates of staff as a result of the October 2003 increase in the National Minimum Wage, was the increase due to any of the following reasons?

a) To comply with the new NMW rates (i.e. £4.50 for 22+ and £3.80 for 18–21s) [ ]

b) To maintain pay differentials above the NMW of lowest pay rate [ ]

c) To maintain pay differentials for more experienced staff [ ]

d) To maintain pay differentials for higher-grade staff (e.g. supervisors) [ ]

e) Other reasons Please specify ....

6. Please specify the highest hourly pay rate you had to increase as a result of the October 2003 increase in the National Minimum Wage. *(Please write in pounds and pence)*

From £ [ ] To £ [ ]

7. Has the October 2003 increase in 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	[ ]	[ ]	[ ]
b) Higher staff motivation	[ ]	[ ]	[ ]
c) Faster filling of vacancies	[ ]	[ ]	[ ]

8. As a result of the October 2003 increase in the National Minimum Wage, have you changed any of the following in your business?
(Please tick one box for each potential change)

	Significant Increase	*Slight Increase*	*Slight Decrease*	*Significant Decrease*	*No Change*
a) Overall staffing levels	☐	☐	☐	☐	☐
b) Basic hours	☐	☐	☐	☐	☐
c) Overtime hours	☐	☐	☐	☐	☐
d) Overtime rates/incentive payments/ bonuses/commission/ tips etc	☐	☐	☐	☐	☐
e) Non-wage benefits (e.g. meal vouchers, paid breaks etc)	☐	☐	☐	☐	☐

9. Has the October 2003 increase in the National Minimum Wage led to changes in any of the following in your business? *(Please tick one box for each potential change)*

	Significant Increase	*Slight Increase*	*Slight Decrease*	*Significant Decrease*	*No Change*
a) Profits	☐	☐	☐	☐	☐
b) Prices	☐	☐	☐	☐	☐
c) Measures taken to control labour costs (e.g. treatment of absence, paid breaks, staff meals, overtime rates)	☐	☐	☐	☐	☐
d) Measures taken to control non-labour costs (e.g. costs of supplies, distribution and marketing costs, improved stock control)	☐	☐	☐	☐	☐
e) Use of new technology/processes	☐	☐	☐	☐	☐
f) Quality of goods and services you provide	☐	☐	☐	☐	☐
g) Introduction of new products or services	☐	☐	☐	☐	☐
h) Use of unskilled/unqualified labour	☐	☐	☐	☐	☐
i) Other	Please specify				

10. At what age is a worker entitled to your full adult rate? ☐

11. Do you have age-related pay structures? Yes *(go to Q12)* ☐ No *(go to Q14)* ☐

12. 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. *(Please write in pounds and pence)*

16/17 £ ☐ 18 £ ☐ 19 £ ☐ 20 £ ☐

21 £ ☐ 22 + £ ☐

13. There could be a number of reasons why employers have age-related pay structures. Some of these are listed below. *(Please tick all that apply)*

Productivity ☐ Reliability ☐ Experience ☐

Length of service ☐ Recruitment ☐ Legal restrictions ☐

National Minimum Wage ☐ Previous Wage Council practice ☐

Other ☐ Please specify ……………………………………………… *(Go to Q15)*

14. If you have no age-related pay structures, what other factors account for differences in your workers' hourly pay?
(Please tick all that apply)

Experience ☐ Qualifications/skills ☐ Responsibilities ☐

Length of service ☐ Output work ☐ Performance Assessment/appraisal ☐

Other ☐ Please specify ………………..

15. Has the 2003 increase in the National Minimum Wage made you more or less likely to employ workers in different age groups?
(Please tick one box for each age group)

	More likely	*Less likely*	*No change*
Workers aged 16–17	☐	☐	☐
Workers aged 18–21	☐	☐	☐
Workers aged 22 or over	☐	☐	☐

16. If you employ any apprentices, how many do you employ?
(Please insert numbers)

a) under a Government apprenticeship scheme, or ☐

b) under a contract of apprenticeship ☐

17. How many of your apprentices are aged...? *(Please insert numbers)*

16 to 17 ☐ 18 ☐ 19 ☐ 20 ☐ 21 ☐ 22+ ☐

18. What is your lowest hourly pay rate for apprentices?
(Please write in pounds and pence)

Year 1 apprentices ☐ Year 2 apprentices ☐ Year 3 apprentices ☐

19. Do you currently make use of the Development Rate for workers aged 22 or over (i.e. pay less than £4.50 but at least £3.80)? *(This Development Rate is for workers receiving accredited training in their first six months with a new employer.)* Yes ☐ No ☐

20. If you don't currently use the Development Rate, will you be more likely to use it when the adult minimum wage rate increases to £4.85 October 2004? Yes ☐ No ☐

21. Will the introduction of a National Minimum Wage of £3 for 16 and 17 year olds in October 2004 make you more or less likely to employ workers in different age groups? *(Please tick one box for each age group)*

	More likely	*Less likely*	*No change*
Workers aged 16–17	☐	☐	☐
Workers aged 18–21	☐	☐	☐
Workers aged 22 or over	☐	☐	☐

22. We would find helpful any other comments that you might have about your experience of the National Minimum Wage. Please continue on a separate sheet if necessary. All your comments will be read.

....
....
....

Additional Questions for the Social Care Sector

23. Does your business provide services to the *public sector?* Yes ☐ No ☐

24. Did you seek to renegotiate the conditions of your public sector contract as a result of the October 2003 increase in the National Minimum Wage? Yes ☐ No ☐

25. Were you successful in renegotiating the contract? Yes ☐ No ☐ In part ☐

26. What percentage of the increase in your pay bill due to the October 2003 increase in the National Minimum Wage were you able to recoup through negotiation?

None ☐	1 to 24% ☐	25 to 49% ☐
50 to 74% ☐	75 to 99% ☐	100% ☐

Additional Questions for the Textiles Sector

27. Do you have an incentive pay system (e.g. piece rate or payment by results)? Yes ☐ No ☐

28. Do you determine or control the hours worked by your piece rate workers? Yes ☐ No ☐

29. What impact has the October 2003 increase in the National Minimum Wage had on your incentive system?

	Significant	*Slight*	*None*
a) Reduced differentials	☐	☐	☐
b) Reduced competitiveness	☐	☐	☐
c) Reduced ability to motivate employees	☐	☐	☐
d) Reduced productivity	☐	☐	☐
e) Increased costs	☐	☐	☐

Minimum Wage Systems in Other Countries

An Overview

1 This appendix presents updated information on minimum wage systems in the other countries we examined in our previous reports. We report on the introduction of a minimum wage in Jersey, the different minimum wage rates currently in place in France and on recent debate about a possible national minimum wage in Germany. Changes to the uprating of the minimum wage in Spain and new rules on the treatment of workers with reduced working capacity in Portugal are also described.

2 Ten countries joined the European Union (EU) on 1 May 2004, and according to Eurostat (2004), nine have a minimum wage in place (Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia). However data from Eurostat indicate that, with the exception of Malta, their minimum wages are lower than those within the established membership of the EU, ranging from €121 per month in Latvia to €471 per month in Slovenia. The highest monthly rate among the new members is in Malta at €543 per month, slightly higher than rates in Portugal and Spain[1]. When the relative purchasing power of these countries is considered, the new EU members remain at the lower end of the scale among the 18 EU members which have a minimum wage in place, again with the exception of Malta. As lessons for the UK from the new EU members are likely to be limited, we have continued to concentrate on the group of twelve Organisation for Economic Co-operation and Development (OECD) member countries we examined in previous reports, many of which are also members of the EU.

3 We are grateful to the OECD, the German Embassy in London, the Jersey Government and a number of British Embassies and High Commissions for their assistance with our research.

[1] Rates per month on 1 January 2004.

4 Table A4.1 compares minimum wage levels across countries and Table A4.2 describes adult minimum wages as a percentage of full-time median earnings. As noted in previous reports we need to be cautious about direct comparisons: there are differences between countries in the definitions of what counts towards the minimum wage, the definitions of earnings used, the age coverage and the sectors covered. In addition minimum wage rates are set at different dates from country to country.

5 In previous reports we highlighted the approaches adopted across countries for uprating their minimum wages and enforcing the provisions. This information has been updated in Tables A4.3 and A4.4 respectively. We have also updated information on age variations provided in previous reports in Tables A4.5 and A4.6.

Specific Country Updates

France

6 Although the hourly statutory national minimum wage rate is currently €7.61 (equivalent to €1,154.18 per month based on a 35 hour week), a number of guaranteed monthly salary rates are also in place to reflect the staggered implementation of the 35 hour working week. This was designed to ensure that when employers switched to the 35 hour working week, employees' salaries were not cut by the same proportion as their statutory working time. The guaranteed monthly rates range from €1,178.54 to €1,197.37. These will gradually be brought into line with the highest rate, resulting in a single minimum wage by 1 July 2005.

Germany

7 Currently there is no national minimum wage in Germany, although a large number of bargaining agreements are in place which vary by sector and region. But with the exception of the agreement for construction, the bargaining agreements are only binding on those employers who belong to the relevant employer associations.

8 There is now considerable political debate within Germany, however, about whether there should be a national minimum wage. The issue has become more prominent as a result of proposed revisions to the benefits system, which would require people who had been unemployed for more than 12 months to accept any offer of a legal job; in the absence of a minimum wage, a jobseeker might be required to accept a job offering very low rates of pay. However, we understand

that in general most trade unions and industry are opposed to a national minimum wage and it seems unlikely that the Government will proceed in the near future.

Jersey

9 The States of Jersey (the Jersey Government) has approved the introduction of a minimum wage which is due to come into force on 1 April 2005. The rates from that date will be £5.08 per hour for all employees over school leaving age (16 years old) and £3.82 per hour for an employee of any age undertaking accredited training for up to one year, in a new job with a new employer. In addition, employers may deduct an offset of up to £55.65 per week for accommodation and up to £74.20 per week where accommodation and meals (defined as three adequate meals per day) are provided. Enforcement of the new minimum wage will be the responsibility of Compliance Officers from the Employment and Social Security Department and complaints will be handled by an Employment Tribunal.

Portugal

10 The Government brought in new legislation effective from August 2004, which introduced a new flexibility in determining pay for workers with reduced working capacity (such as those with physical disabilities). A reduction may be applied which corresponds to the difference (in percentage terms) between the worker’s actual ability and full working ability and may be applied where that difference exceeds 10 per cent. The maximum reduction is 50 per cent.

Spain

11 A number of changes to the way in which the minimum salary is uprated took effect from 1 July 2004, together with a 6.6 per cent uprating to make up for lower than inflation increases between 1996–2004. The Government has removed the existing automatic links between increases in the minimum salary and a range of benefits. Welfare payments, which will be set annually at the time of the budget, are now tied to a new indicator (indicator público de rentas de efectos multiples (IPREM), which roughly translates as the public index of various goods). This means that increases in public expenditure (specifically benefits) are no longer tied to increases in the minimum wage and it should enable the Government to meet its manifesto pledge of an increase in the minimum salary to €600 per month by 2008 (currently €490 per month).

Comparison of Minimum Wage Systems

Table A4.1 Comparison of Level of Minimum Wages[(a)] Across Countries, end 2004

	In national currency expressed as hourly rate[(b)]		In UK £, using: Exchange rates[(c)]	PPPs[(d)]	Date of last uprating	Age full minimum wage usually applies[(e)]
Australia[(f)]	Aus $11.69	($467.40/week)	4.57	5.37	May 2004	21
Belgium[(g)]	€6.98	(€1210/month)	4.67	4.92	October 2004	21
Canada[(h)]	Can $7.08		2.96	3.66	[(i)]	16
France[(j)]	€7.61		5.10	5.20	July 2004	18
Greece[(k) (l)]	€3.13	(€25.01/day)	2.09	2.62	September 2004	15
Ireland	€7.00		4.69	4.15	February 2004	20
Japan[(m)]	Yen 665		3.31	2.71	October 2004	–
Netherlands	€7.30[(n)]	(€291.90/week)	4.89	5.04	July 2003[(o)]	23
New Zealand	NZ $9.00		3.24	4.01	April 2004	18
Portugal[(k)]	€2.11	(€365.6/month)	1.41	1.99	2004	16
Spain[(k)]	€2.83	(€490.8/month)	1.90	2.34	July 2004	16
United Kingdom	£4.85		4.85	4.85	October 2004	22
United States	$5.15[(p)]		2.83	3.37	1997	20

Sources: OECD Minimum Wage Database. British Embassies and High Commissions. For PPPs, OECD, *Main Economic Indicators*. For exchange rates, Bank of England monthly average spot exchange rate.

Notes:

(a) In all cases, the minimum wage refers to the basic rate for adults.

(b) For countries where the minimum wage is not expressed as an hourly rate, the rate has been converted to an hourly basis assuming a working time of 8 hours per day, 40 hours per week and 173.3 hours per month.

(c) August 2004.

(d) Purchasing Power Parities (PPP) for private consumption, August 2004.

(e) Exemptions and special rules apply in many cases. For example, in France and the United States the full adult rate applies to young workers with a tenure of more than 6 and more than 3 months respectively. See Table A4.5 for further details.

(f) Federal minimum wage.

(g) For white collar workers. Blue collar workers receive a minimum hourly rate of €7.35.

(h) Weighted average of provincial rates.

(i) Date of last uprating varies between provinces. For example the rate was last increased on 1 October 1999 in Alberta and 1 February 2004 in Ontario.

(j) Rate applies to workers who are not covered by the garanties mensuelle de remunération, or monthly guaranteed salary.

(k) Not including annual supplementary pay of two additional months of salary for full-time workers.

(l) For blue collar workers.

(m) Weighted average of prefectural rates.

(n) Excludes 8 per cent supplement for holiday pay.

(o) Rate last reviewed July 2004.

(p) Federal minimum wage. Tipped employees receive a special minimum wage of $2.13 per hour in direct wages.

Table A4.2 Adult Minimum Wages Relative to Full-time Median Earnings, Mid-2004[a]

Country	Percentage	
Australia[b]		
-LFS	58.8	
-ES	55.1	
France	56.6	
New Zealand	53.6	
Ireland	51.7	
Belgium	48.5	
Greece[c]	47.9	(55.9)
Netherlands[d]	46.4	(50.1)
United Kingdom[e]	43.2	
Canada	39.5	
Portugal[c]	38.0	(44.4)
Japan	33.7	
United States	32.2	
Spain[c]	30.0	(35.0)

Sources: (Except UK) Minimum wages and mean and median earnings for full-time workers: OECD estimates and OECD Earnings Structure Database.

Notes:

(a) In all cases, the minimum wage refers to the basic rate for adults. In some cases, the median earnings data for full-time workers for mid-2004 are estimates based on extrapolating data for earlier years in line with other indicators of average earnings growth. All earnings data are gross of employee social security contributions.

(b) Two estimates of median earnings are available based on the Labour Force Survey (LFS) and an enterprise survey (ES). In each case, the data refer to weekly earnings. The minimum wage refers to the Federal Minimum Wage.

(c) The ratio including annual supplementary pay of two additional months of salary is given in parentheses.

(d) The ratio including 8 per cent supplement for holiday pay is given in parentheses.

(e) LPC calculation using Annual Survey of Hours and Earnings (including supplementary information), applying the adult rate of £4.50 (applicable in mid-2004). On the basis of the minimum wage of £4.85, the figure would be 46.6 per cent.

Table A4.3 Uprating of Minimum Wages

Country	Method of uprating
Australia	An independent body (the Australian Industrial Relations Commission) is responsible for setting minimum 'safety net' rates for awards and the Federal Minimum Wage. Reviews are triggered by the Australian Council of Trade Unions and usually, but not necessarily, take place each year. Reviews consider economic factors and the needs of the low paid.
Belgium	The minimum monthly average guaranteed income is set for the private sector by a collective employment agreement reached at the National Labour Council (social partners).
Canada	Uprating is generally based on recommendations from provincial Labour Ministries from time to time, taking into account the cost of living and views of employers and employees. The recommendations are reviewed and voted on by the provincial Parliament. In Quebec the rate is reviewed annually based on eleven indicators, including the ratio between the minimum wage and the average hourly wage.
France	The minimum wage is reassessed each year on 1 July. The uprating must be at least half that of the increase in purchasing power of the average hourly wage. During the course of the year if the price index increases by over two per cent, the minimum wage is increased automatically by the same amount. The Government can also increase the minimum wage at any time.
Greece	Minimum wages are increased every six months or every year, depending on the provisions of the two-year National General Collective Labour Agreements. They are the result of negotiations between the social partners and upratings take account of the anticipated level of inflation and other factors, including the national level of productivity.

Uprating of Minimum Wages – *Continued*

Country	Method of uprating
Ireland	The National Minimum Wage can only be increased following a recommendation in a national agreement. Where there is no national agreement, any organisation which the Labour Court is satisfied is substantially representative of employees or employers can ask the Labour Court to examine the national minimum hourly rate of pay, not earlier than 12 months after the Minister last declared a national minimum hourly rate of pay. The Labour Court can then make a recommendation to the Minister. To date, all increases to the National Minimum Wage have been as recommended by the social partners in national agreements.
Japan	The system operates regionally. The minimum wage is reviewed and amended each Autumn. Regional Minimum Wage Councils, comprising representatives of labour unions, employees and public agencies, make a proposal based on their consideration of the cost of living, salary of workers in similar industries, and the financial capability of employers. The final decision is made by the Director of the Regional Labour Standard Agency. In addition, if specific industries believe it is necessary to set a higher rate than the regional minimum wage, they can set their own rate by industry within the prefecture. The labour and management representatives of the industry must submit the rate to the Regional Minimum Wage Council.
Netherlands	The Ministry of Social Affairs normally uprates twice yearly (1 January and 1 July) taking account of the 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 (including unemployment benefit and pensions) and the number of people working exceeds 82.6 per cent, the Government may decide not to link the wage to the average contractual wage increase (as it did decide between 1993 and 1996). If the ratio is lower than 82.6 per cent the minimum wage must be linked to wage growth. The minimum wage system is evaluated every four years, mainly to consider whether the level is too high or too low compared with average earned wages and labour market circumstances. In October 2003, the Government and the social partners agreed a wage freeze for 2004 and 2005 in line with the Government's general policy of restoring Dutch competitiveness.
New Zealand	The Minister of Labour conducts annual reviews in accordance with the Minimum Wage Act. The review considers the effectiveness of the minimum wage in meeting its objectives and there are set criteria for reviewing changes to the minimum wage. The Minister invites submissions from the New Zealand Council of Trade Unions and Business New Zealand, as well as other organisations. The Minister makes recommendations to the Governor General on the basis of these submissions and analysis undertaken by a number of Government departments.
Portugal	An Inter-Ministerial annual review considers the social and economic effects of the minimum wage. This includes the expected inflation rate and productivity levels. Following consultation with the social partners, the wage is usually uprated annually and implemented from January of each year.
Spain	The Government uprates annually following consultation with the social partners. The Government is obliged to take account of inflation, average national productivity, participation levels and general economic conditions.
UK	The Government considers recommendations from an independent Commission, which reports following wide-ranging consultation and consideration of the effects on the economy as well as on specific sectors and groups of workers. Since the minimum wage was introduced in 1999 there have been annual upratings.
US	Changes to the Federal minimum wage are voted on by Congress intermittently. Most States have their own minimum wage rates. Where Federal and State laws stipulate different rates, the higher rate applies.

Source: British Embassies and High Commissions.

Table A4.4 Enforcement of Minimum Wages

Country	Method of enforcement
Australia	In the Federal jurisdiction complaints are lodged with the Department of Employment and Workplace Relations and are investigated by inspectors. Employees can also refer claims to a Small Claims Court. Similar processes apply in State jurisdictions.
Belgium	Labour inspectorate.
Canada	Labour inspectorate. Usually the employee contacts the Labour Board and files a claim for lost wages, and the problem is investigated. The inspectorate can perform random investigations.
France	Labour inspectorate (which is also responsible for general conditions of work, health and safety). Inspectors carry out random checks and investigate complaints from trade unions and individual employees.
Greece	Labour inspectorate. Employers can be sued by employees, who have to pay their own costs, or by inspectors.
Ireland	The National Minimum Wage is enforced by Labour Inspectors in the Department of Enterprise, Trade and Employment, who conduct both routine inspections and investigate complaints. Disputes can be referred to the Rights Commissioner Service of the Labour Relations Commission.
Japan	Labour inspectorate.
Netherlands	Labour inspectorate periodically reports on the application of the minimum wage in practice. Employers are informed of pay salaries below the minimum wage but the Labour inspectorate is not able to take employers to court; the employee must do this.
New Zealand	Labour inspectorate may take action in the Employment Relations Authority or the Employment Court to recover wages owing, plus penalties. Alternatively Labour Inspectors may issue a demand notice requiring that the employer pay monies to an employee, as assessed by the Labour Inspector. Complaints received from a person other than the employee are proactively investigated.
Portugal	Labour inspectorate.
Spain	Labour inspectorate (which also has the power to enforce a wide range of labour issues, including collectively-bargained rates). It can fine employers, or the employee can take the case to tribunal to obtain back pay. The system is both reactive and proactive. There are around 600 inspectors and 800 assistants, stationed on a provincial basis.
UK	Inland Revenue is the enforcement agency. It conducts both proactive, targeted enforcement and investigation of complaints. Employees also have the right to take their case to an Employment Tribunal.
US	Wage and Hour Division in Department of Labor. It both pursues complaints and investigates likely areas of non-compliance. There is a team of approximately 950 inspectors, spread over 54 offices.

Source: British Embassies and High Commissions.

Table A4.5 Age Variations Under Minimum Wage Systems

Country	Treatment by age
Australia	Full minimum wage at 21 in most sectoral awards. Below 21 a sliding scale applies from age 16 (40–50 per cent of the minimum wage) through age 18 (65–80 per cent) to age 20 (85–100 per cent). The remainder of awards provide the full minimum at 18, 19 or 20, or provide the full minimum to all ages.
Belgium	Full minimum wage applies at age 21. An additional premium is payable to workers aged 21½ who have been employed for at least 6 months and to workers aged 22 who have been employed for at least 12 months. There is a 6 per cent deduction from the minimum wage for each year below age 21, with those aged 16 or under receiving 70 per cent of the full rate.
Canada	Full minimum wage at all ages except in Ontario, which has retained youth rates. Both British Columbia and Nova Scotia have introduced a first job/entry-level wage rate for workers new to the paid labour market.
France	Full minimum wage at 18. Certain categories of young people receive a reduced rate, provided they have worked less than six months (80 per cent for those aged 16 and 90 per cent for those aged 17).
Greece	Full minimum wage at 15 (but variation depending on length of their employment).
Ireland	Full minimum wage applies to an experienced adult employee, which is an employee who has had any employment whatsoever in any two years over the age of 18, unless undergoing structured training or study. Employees in the first year after the date of first employment over age 18 receive 80 per cent of the full minimum rate and they receive 90 per cent in the second year. All employees under age 18 are entitled to 70 per cent of the full adult rate.
Japan	It is prohibited to vary regional minimum wages by age except in the case where specific industries have set a higher regional minimum wage. They would be permitted to set a lower sectoral rate for under 18s or over 65s.
Netherlands	Full minimum wage at 23. Youth rates are 30 per cent at 15, 34.5 per cent at 16, 39.5 per cent at 17, 45.5 per cent at 18, 52.5 per cent at 19, 61.5 per cent at 20, 72.5 per cent at 21 and 85 per cent at 22.
New Zealand	Full minimum wage at 18. 16–17 year olds receive 80 per cent of the main rate. Although trainees aged 16 and over may be paid below the minimum wage, a Bill was passed in 2003 which empowers the minimum training wage to be equivalent to the youth minimum wage rate.
Portugal	Full minimum wage at all ages. Exceptions are apprentices and trainees in qualified or highly qualified jobs, who can receive 80 per cent for up to a year, or 6 months if the course is technical/professional.
Spain	Full minimum wage at 16. Young people who were unemployed but join various training schemes to help them to enter the labour market receive 80 per cent of the new index (the IPREM or 'public index of various goods').
UK	Full minimum wage at 22. Separate rates exist for 16–17 and 18–21 year olds (currently 62 and 85 per cent respectively of the adult rate).
US	Full minimum wage at all ages, except below 20 where lower rate of $4.25 can apply (approximately 80 per cent of full minimum wage) for the first 90 days in any job. Also full-time students can be paid 85 per cent of the minimum wage. Additionally, student-learners (those aged 16 and over who are enrolled in vocational education) can be paid 75 per cent of the minimum wage while on the vocational education programme.

Source: British Embassies and High Commissions.

Table A4.6 Youth Minimum Wages as Percentage of Adult Minimum Rates, end 2004

Country	Percentage at age 16	Percentage at age 17	Average percentage at ages 18/19
Australia[a]	50	60	75
Belgium	70	76	86
Canada	100[b]	100[b]	100
France[c]	80	90	100
Greece	100	100	100
Ireland	70	70	85
Japan[d]	100	100	100
Netherlands	34.5	39.5	49
New Zealand	80	80	100
Portugal	100	100	100
Spain	100	100	100
UK	62	62	84
US[c]	82	82	82

Sources: OECD Minimum Wage Database. British Embassies and High Commissions.

Notes:

(a) As prescribed in the NSW Shop Employees Award. These rates are broadly representative of the reduced rates for younger workers prescribed in other awards.

(b) All provinces except Ontario.

(c) For France and the United States, the reduced rates apply to young workers with a tenure of less than 6 months and less than 3 months, respectively.

(d) Some variation in specific industries in certain prefectures (see Table A4.5).

Sectoral Employment and Earnings Data

Table A5.1 Trends in Employee Jobs in Low-paying Sectors, Thousands, 1998–2004

	Sept 1998	Sept 2000	Sept 2002	Sept 2003	Sept 2004
Retail					
Full-time	–	1,102	1,159	1,151	1,156
Part-time	–	1,514	1,611	1,628	1,644
Total	2,554	2,616	2,769	2,779	2,800
Hospitality					
Full-time	–	656	766	738	752
Part-time	–	974	953	1,017	1,016
Total	1,566	1,630	1,719	1,755	1,768
Cleaning					
Full-time	–	169	123	138	169
Part-time	–	269	299	276	253
Total	464	437	422	414	422
Security					
Full-time	–	107	106	124	132
Part-time	–	24	41	30	25
Total	128	131	147	154	157
Nursery nurses					
Full-time	–	85	86	100	97
Part-time	–	45	48	50	66
Total	114	131	135	149	163
Residential social care					
Full-time	–	193	195	199	206
Part-time	–	249	241	245	244
Total	423	442	437	445	450
Agriculture					
Full-time	–	233	171	175	179
Part-time	–	54	47	47	46
Total	304	288	218	222	225
Textiles, clothing and footwear					
Full-time	–	217	161	136	121
Part-time	–	30	21	20	19
Total	331	247	183	156	140
Hairdressing					
Full-time	–	59	56	55	58
Part-time	–	45	44	50	45
Total	92	104	100	105	103

Source: ONS employee jobs series 1998–2004. Labour Force Survey (LFS), 1998–2004 for nursery nurses.

Table A5.2 Hourly Earnings for Employees Aged 18 and Over by Low-paying Sector, 2002–2004

	Years				Annual percentage change	
	2004a	**2004**	**2003**	**2002**	**2003/04**	**2002/03**
Retail						
Lowest decile	£4.55	£4.57	£4.38	£4.20	4.3	4.4
Lowest quartile	£4.88	£4.89	£4.77	£4.55	2.5	4.8
Median	£5.64	£5.65	£5.55	£5.19	1.8	7.0
Mean	£7.33	£7.35	£7.16	£6.72	2.6	6.6
Mode	£4.50	£4.50	£4.20	£4.10	7.1	2.4
Hospitality						
Lowest decile	£4.44	£4.42	£4.20	£4.04	5.2	4.0
Lowest quartile	£4.53	£4.51	£4.40	£4.10	2.5	7.3
Median	£5.20	£5.20	£5.14	£4.77	1.2	7.7
Mean	£6.53	£6.50	£6.48	£6.00	0.4	8.0
Mode	£4.50	£4.50	£4.20	£4.10	7.1	2.4
Cleaning						
Lowest decile	£4.50	£4.50	£4.20	£4.10	7.1	2.4
Lowest quartile	£4.80	£4.84	£4.50	£4.25	7.6	5.9
Median	£5.48	£5.50	£5.23	£5.00	5.2	4.6
Mean	£6.91	£7.07	£6.57	£6.03	7.6	8.9
Mode	£4.50	£4.50	£4.20	£4.10	7.1	2.4
Security						
Lowest decile	£4.75	£4.75	£4.40	£4.38	8.0	0.5
Lowest quartile	£5.49	£5.50	£5.12	£5.21	7.4	-1.7
Median	£6.50	£6.50	£6.22	£6.10	4.5	2.0
Mean	£7.46	£7.50	£7.24	£7.37	3.6	-1.7
Mode	£4.50	£4.50	£4.20	£4.10	7.1	2.4
Nursery nurses						
Lowest decile	£4.50	£4.50	£4.24	£4.10	5.8	3.4
Lowest quartile	£5.00	£5.02	£4.77	£4.60	5.2	3.7
Median	£6.35	£6.50	£6.38	£6.12	1.9	4.2
Mean	£6.75	£6.80	£6.58	£6.33	3.3	3.9
Mode	£8.18	£8.19	£8.19	£7.61	0.0	7.6
Residential social care						
Lowest decile	£4.77	£4.80	£4.40	£4.21	9.1	4.6
Lowest quartile	£5.39	£5.41	£5.00	£4.66	8.2	7.4
Median	£6.60	£6.68	£6.20	£5.73	7.8	8.1
Mean	£7.83	£7.94	£7.42	£6.90	7.0	7.5
Mode	£4.50	£4.50	£4.20	£4.10	7.1	2.4
Agriculture						
Lowest decile	£4.93	£5.00	£4.67	£4.55	7.1	2.6
Lowest quartile	£5.36	£5.50	£5.25	£5.04	4.8	4.1
Median	£6.29	£6.38	£6.13	£5.96	4.1	2.8
Mean	£7.53	£7.69	£7.28	£7.05	5.7	3.2
Mode	£5.00	£5.00	£5.79	£5.49	-13.6	5.5
Textiles, clothing and footwear						
Lowest decile	£4.63	£4.65	£4.50	£4.30	3.3	4.6
Lowest quartile	£5.32	£5.37	£5.13	£4.99	4.8	2.7
Median	£6.62	£6.63	£6.50	£6.28	1.9	3.6
Mean	£8.55	£8.58	£8.28	£7.95	3.6	4.2
Mode	£4.50	£4.50	£4.20	£4.10	7.1	2.4
Hairdressing						
Lowest decile	£4.20	£4.27	£4.00	£4.00	6.8	0.0
Lowest quartile	£4.79	£4.76	£4.36	£4.20	9.1	3.8
Median	£5.63	£5.70	£5.37	£5.00	6.1	7.5
Mean	£6.42	£6.49	£6.22	£5.83	4.4	6.6
Mode	£4.50	£4.50	£4.20	£4.10	7.1	2.4

Source: ASHE, 2002–2004 without supplementary information, 2004a with supplementary information.
LFS, 2002–2004 for nursery nurses.

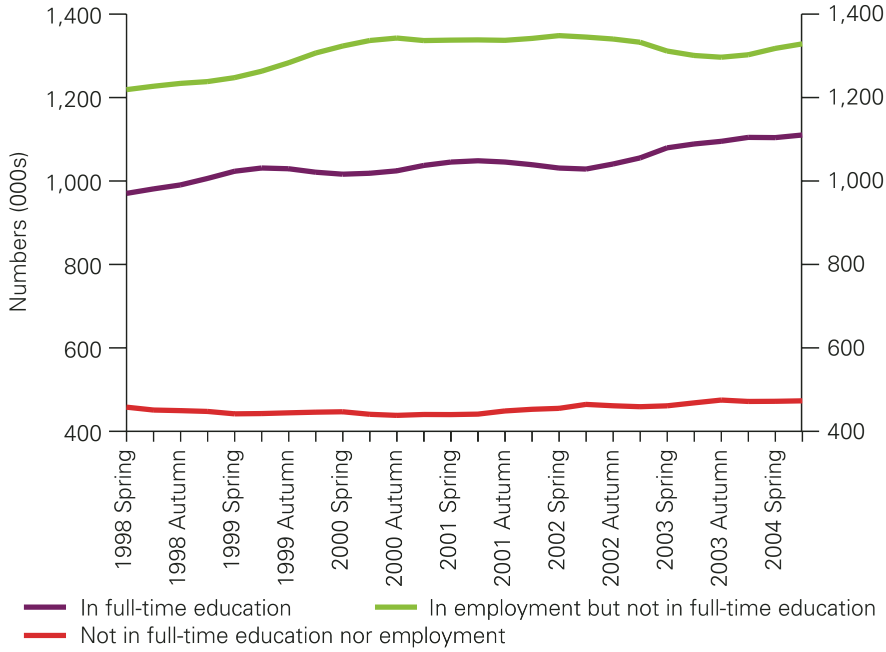
The Labour Market Position of 18–21 Year Olds

1 In Chapter 5 we found that there have been slight increases in employment rates for 18–21 year olds and a fall in unemployment rates since the introduction of the minimum wage. However, in the period Summer 2001–Autumn 2003 there was a significant worsening in their labour market position (particularly for those aged 18–19), but the decline appears to have halted since the October 2003 upratings. This Appendix provides additional information on the labour market position of 18–21 year olds.

2 According to the Labour Force Survey (LFS), the population of 18–21 year olds has been steadily rising, from 2.65 million in Spring 1998 to 2.91 million in Summer 2004 (using four quarter moving averages). This represents an increase of 10 per cent (11.2 per cent for men and 8.8 per cent for women). Figure A6.1 shows that the number of 18–21 year olds in full-time education (FTE) has risen by 14 per cent over this period (12.7 per cent for men and 16.1 per cent for women), with a noticeable increase since Summer 2002. Figure A6.2 shows that the fall in the proportion of employed 18–21 year olds not in FTE since Summer 2002 mirrors the increased participation in FTE.

Figure A6.1

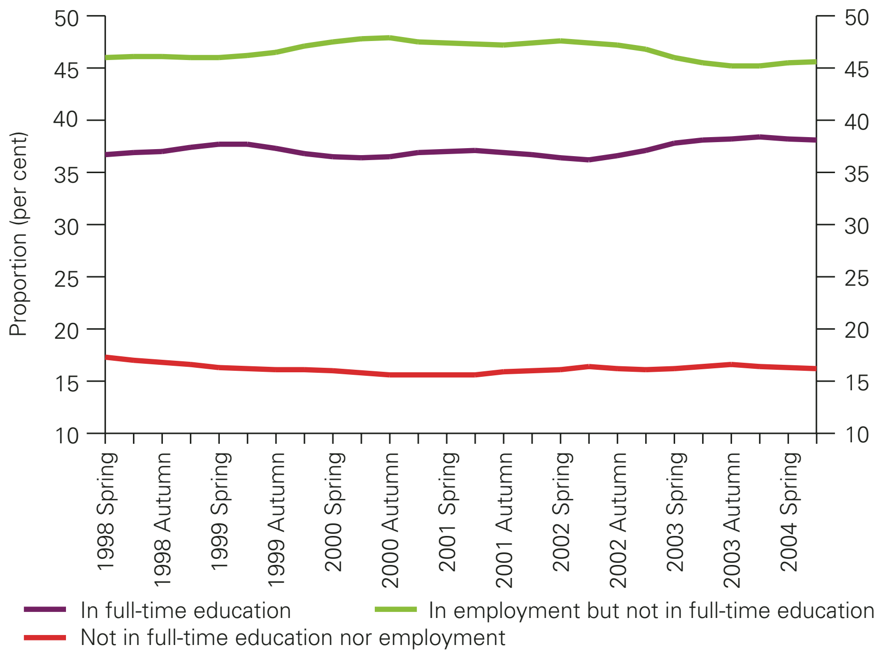
Number of 18–21 Year Olds by Education and Labour Market Status, Thousands, 1998–2004



Source: LFS, four quarter moving average, 1998–2004.

Figure A6.2

Proportion of 18–21 Year Olds by Education and Labour Market Status, 1998–2004

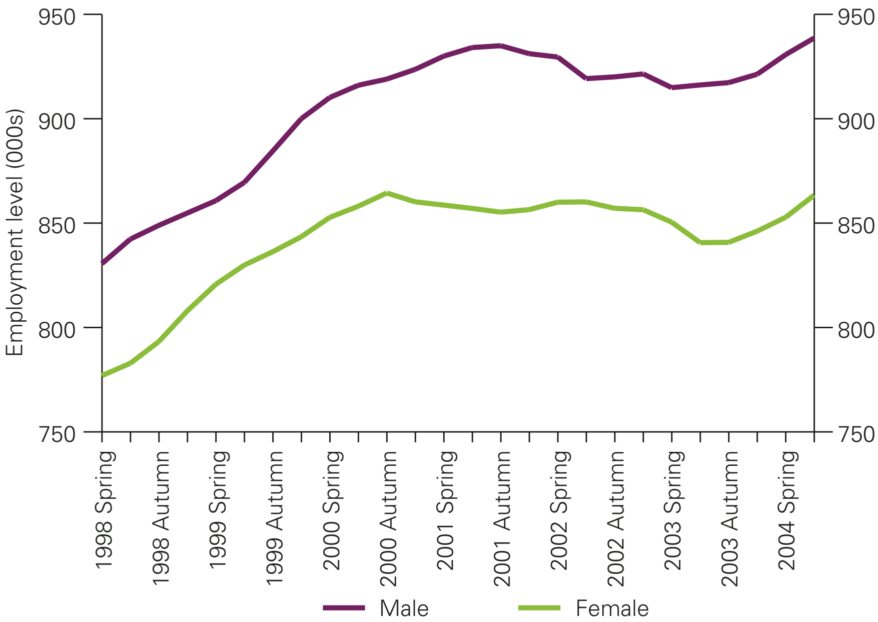


Source: LFS, four quarter moving average, 1998–2004.

3 In Summer 2004 employment levels for 18–21 year olds were at their highest level (four quarter moving average) since the introduction of the minimum wage. Since Spring 1998 they have risen by around 110,000 for men (about two-thirds were not in FTE) and 85,000 for women (over two-fifths were not in FTE). This is demonstrated in Figure A6.3. In the year to Summer 2004 employment levels increased by 22,000 for men (12,000 for those not in FTE) and 23,000 for women (16,000 for those not in FTE).

Figure A6.3

Employment Levels for 18–21 Year Olds by Gender, Thousands, 1998–2004



Source: LFS, four quarter moving average, 1998–2004.

4 In Chapter 5 we showed that employment rates for 18–21 year olds not in FTE had fallen for men between 2001–2002 and then stabilised, while the rate for women fell from 2002–2003 and then stabilised (see Figure 5.5). Unemployment rates for 18–21 year olds not in FTE have largely mirrored the employment rates, as illustrated in Figure A6.4. For men the unemployment rate increased between 2001–2002 before falling, while for women the unemployment rate increased in 2002–2003 before falling slightly.

Figure A6.4

Unemployment Rates for 18–21 Year Olds Not in Full-time Education, 1998–2004

Source: LFS, four quarter moving average, 1998–2004.

Office for National Statistics Low Pay Methodology

1 Prior to 2004, due to the limitations of the surveys available, the Office for National Statistics (ONS) used a central estimate methodology to produce its low pay statistics. Under this methodology the findings of the New Earnings Survey (NES) and the Labour Force Survey (LFS) were averaged to produce the low pay estimates (the central estimate). The NES, although providing reliable information from employer records, was likely to under-sample those on low pay, especially if they earned less than the Pay As You Earn (PAYE) threshold. The LFS, on the other hand, would cover such workers, but it was self-reported and contained many proxy responses – both factors making for an element of uncertainty.

2 The NES was replaced by a new annual earnings survey, the Annual Survey of Hours and Earnings (ASHE) in April 2004. ASHE, like NES, is based on a one per cent sample of employees. Information on earnings and hours is obtained in confidence from employers. The survey does not cover the self-employed. In 2004 information collected on earnings and hours related to the pay period which included 21 April 2004. The earnings information relates to gross pay before tax, national insurance or other deductions, and excludes payments in kind. It is restricted to earnings relating to the survey period and so excludes payments of arrears from another period made during the survey period. Any payments due as a result of a pay settlement but not yet paid at the time of the survey will also be excluded.

3 There are four main differences between ASHE and NES.

- First, ASHE results are weighted to the number of jobs given by the LFS, which itself is weighted by the Census and mid-year population estimates. This weight differs slightly from that previously used for the low pay statistics. NES, being a random one per cent sample, was unweighted for the main earnings statistics.
- Second, unlike NES, ASHE imputes for item non-response.

- Third, the median replaces the mean as the headline statistic. The median is the value below which 50 per cent of employees fall. It is preferred over the mean for earnings data as it is less influenced by extreme values and because of the skewed distribution of earnings data.

- Last, and perhaps most importantly for the low pay statistics, the coverage of employees for ASHE extends that of the NES.

4 The sample has been boosted in order to improve the coverage of those at the lower end of the earnings distribution. A supplementary survey now collects information on those businesses which are registered for Value Added Tax (VAT) but not registered for PAYE. In addition, follow-up surveys have been introduced for those changing jobs, or new entrants starting jobs, between ONS conducting the initial PAYE sample in January and the survey reference period in April.

5 People working for small firms and those who move jobs frequently are more likely to be low paid than others and these additional samples therefore improve coverage of the low end of the pay distribution. The improved quality and coverage of the ASHE data has enabled ONS, from April 2004, to replace the former central estimate methodology for its low pay statistics with data drawn from ASHE alone.

6 The NES data has been revised from 1998 to 2003 to take account of the imputation and weighting used in ASHE. Unfortunately, the extended coverage is not available for NES. The revised imputed and weighted NES is now known as ASHE without supplementary information. The ONS has therefore revised its low pay estimates for 1998–2003 using a central estimate of LFS and ASHE without supplementary information. ASHE with the extended coverage (as well as the imputation and weighting) available from 2004 is known as ASHE with supplementary information.

7 Overall, ONS concludes that there is little difference between the old central estimates calculated using the old methodology and the results gained using the new ASHE methodology. This may be true overall, but we have found that the new ASHE survey brings significant improvements to calculations relating to the low paid.

8 The results of the new methodology are shown in Table A7.1. This shows the number of jobs that ONS now estimates to have been paid below the minimum wage between 1998 and 2003.

Table A7.1 ONS Revised Estimates of Employee Jobs Paid Below the National Minimum Wage for Those Aged 18 and Over, 1998–2003

	Youth Development Rate (£)	Jobs held by people aged 18–21		Adult minimum wage (£)	Jobs held by people aged 22 and over		All jobs	
		Thousands	Per cent		Thousands	Per cent	Thousands	Per cent
Spring 1998	3.00	110	7.2	3.60	1,170	5.4	1,280	5.6
Spring 1999	3.00	40	2.4	3.60	460	2.1	490	2.1
Spring 2000	3.00	30	2.2	3.60	190	0.9	230	1.0
Spring 2001	3.20	40	2.1	3.70	210	0.9	240	1.0
Spring 2002	3.50	50	2.7	4.10	290	1.3	340	1.4
Spring 2003	3.60	50	2.9	4.20	200	0.9	250	1.0

Source: ONS estimates based on a central estimate of the LFS and ASHE without supplementary information, Spring 1998–2003.
Note: Figures for Spring 1998, before the National Minimum Wage was introduced, are for the number of jobs paid at less than £3.00 per hour (aged 18–21) or £3.60 per hour (aged 22 and over).

9 We can see how these new estimates differ from the old methodology in Table A7.2. This shows the latest estimates of those paid below the minimum wage using the LFS, NES, the central estimate and ASHE. The Table demonstrates that the estimates have become much closer over time. The ASHE estimates in 1998 are much lower than the LFS, NES and central estimates.

Table A7.2 Comparison of Old and New ONS Methodology for Estimates of Employee Jobs Paid Below the National Minimum Wage for Those Aged 18 and Over, 1998–2003

Year	LFS		NES		Central estimate		ASHE	
	Thousands	Per cent	Thousands	Per cent	Thousands	Per cent	Thousands	Per cent
1998	1380	6.0	1400	6.1	1390	6.0	1210	5.2
1999	520	2.2	500	2.1	510	2.2	470	2.0
2000	240	1.0	230	0.9	230	1.0	230	0.9
2001	270	1.1	220	0.9	240	1.0	230	0.9
2002	360	1.5	300	1.2	330	1.4	320	1.3
2003	250	1.0	260	1.1	250	1.1	250	1.0

Source: ONS estimates based on LFS, NES, central estimate and ASHE, Spring 1998–2003.
Notes:
1. LFS using revised weights consistent with the population estimates published in Spring 2003.
2. NES using annual revisions and Spring 2003 population weights.
3. Central estimate is the average of LFS and NES.
4. Using the new ASHE methodology with weights for low pay data.

10 Further details of the new low pay estimates for 1998–2004 can be found in Labour Market Trends (Bird (2004), Daffin (2004), Milton (2004)) and on the National Statistics website at:

http://www.statistics.gov.uk/downloads/theme_labour/2004_jobs_below.xls
and at:
http://www.statistics.gov.uk/downloads/theme_labour/2004_10pbands.xls

For comparison, estimates are also given for the old low pay methodology using a central estimate of the NES and LFS at:

http://www.statistics.gov.uk/downloads/theme_labour/jobs_paid_below_minimum_wage_rates.xls
and at:
http://www.statistics.gov.uk/downloads/theme_labour/10pbands.xls

The new low pay methodology is explained in more detail at:
http://www.statistics.gov.uk/cci/article.asp?ID=992

and the new ASHE methodology at:

http://www.statistics.gov.uk/CCI/article.asp?ID=992&Pos=&ColRank=2&Rank=224.

Abbreviations

ABI	Annual Business Inquiry
ADR	Adult/Older Workers' Development Rate
AEI	Average Earnings Index
ARD	Annual Respondents Database
ASHE	Annual Survey of Hours and Earnings
AWB	Agricultural Wages Board
BHA	British Hospitality Association
BATC	British Apparel and Textile Confederation
BHPS	British Household Panel Survey
BRC	British Retail Consortium
BSA	Business Services Association
CBI	Confederation of British Industry
CCPR	Central Council of Physical Recreation
CIPD	Chartered Institute of Personnel Development
CPI	Consumer Price Index
CSSA	Cleaning and Support Services Association
Defra	Department for Environment, Food and Rural Affairs
DfES	Department for Education and Skills
DRC	Disability Rights Commission
DTI	Department of Trade and Industry
ES	Enterprise Survey
EU	European Union
FAME	Financial Analysis Made Easy
FSB	Federation of Small Businesses
FTE	Full-time Education

GB	Great Britain
GCSE	General Certificate of Secondary Education
GDP	Gross Domestic Product
GMLPU	Greater Manchester Low Pay Unit
HEA	Hairdressing Employers Association
ICON	Independent Care Organisations Network
IDS	Incomes Data Services Ltd
ILO	International Labour Organisation
IPREM	Indicator Público de Rentas de Efectos Multiples (or public index of various goods)
IR	Inland Revenue
KFAT	National Union of Knitwear, Footwear and Apparel Trades
LFS	Labour Force Survey
LMWP	Leicester Minimum Wage Project
LPC	Low Pay Commission
NES	New Earnings Survey
NFU	National Farmers' Union
NGH	National Group on Homeworking
NHF	National Hairdressers' Federation
NHS	National Health Service
NICs	National Insurance Contributions
NMW	National Minimum Wage
OECD	Organisation for Economic Co-operation and Development
ONS	Office for National Statistics
PAYE	Pay As You Earn
PPP	Purchasing Power Parity
QLFS	Quarterly Labour Force Survey
RPI	Retail Price Index
RPIX	Retail Price Index excluding mortgage interest payments
SBS	Small Business Service
SIC	Standard Industrial Classification
SME	Small and Medium-sized Enterprise
SOC	Standard Occupational Classification

T&G	Transport and General Workers Union
TUC	Trades Union Congress
UK	United Kingdom
UKHCA	United Kingdom Home Care Association
US	United States
Usdaw	Union of Shop, Distributive and Allied Workers
VAT	Value Added Tax
WRS	Workers Registration Scheme
WTC	Working Tax Credit
YDR	Youth Development Rate

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