SOUTH AUSTRALIAN SUBMISSION ON THE WAGE COST ASSESSMENT PAPER – CGC2015-03S

2016 UPDATE

SOUTH AUSTRALIAN DEPARTMENT OF TREASURY AND FINANCE

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SOUTH AUSTRALIAN SUBMISSION
WAGE COSTS ASSESSMENT – 2016 Update

SUMMARY

- South Australia believes that the interstate wages assessment lacks sufficient conceptual rigour to be continued in its current form.
- Private sector wages do not provide an appropriate nor reliable proxy for movements in public sector wages.
- Wage levels of public sector employees in one jurisdiction are more heavily influenced by developments in job specific labour markets in other jurisdictions, rather than by generic local or regional labour market influences.
- Regression coefficients are substantially affected by omitted variable bias – the analysis does not recognise that the geographic concentration of high remuneration will cause a geographic concentration of highly skilled individuals.
- Should the Commission decide to retain an interstate wages assessment we are still inclined to support an approach based on whole-of-state wages but we withhold our final position on this issue pending consideration of the coverage and quality of the Characteristics of Employees data and the outcomes produced.
- Should the Commission decide to proceed with the assessment and base it on capital city wages, South Australia is inclined to support the Queensland proposal to use the Major Cities classification of the Accessibility/Remoteness Index for Australia (ARIA).
- South Australia will reserve its final position on all aspects of the assessment until after the results of the new Compensation of Employees data has been released and analysed.

CONCEPTUAL CASE

General position

South Australia believes that the interstate wages assessment lacks sufficient conceptual rigour to be continued in its current form. The assessment results in significant redistributions of GST revenue grants but is based on data, assumptions and a methodology that does not reflect how public sector wages are determined and influenced over time.

The Commission's assessment approach is based on an assumption that state and territory governments face underlying private sector wage pressures when delivering services. Whilst there may be some influence, this is not the predominant driver for the majority of public sector employees. With some minor exceptions in highly specialist fields, state and territory governments are not forced to pay private sector wages. Wage outcomes reflect movements in job specific labour markets and fiscal strategies in each jurisdiction.

The Commission has argued that divergences between underlying public sector wage levels between states and territories is influenced by inter-jurisdictional differences in the skills and experience of staff chosen to deliver comparable services (i.e. policy choices).

This has necessitated the need for the Commission to base its assessment on comparable private sector employees as an indicator of the differences in wages that would need to be paid to public sector workers in each state.

This approach is valid so long as there is a strong relationship between public and private sector wages.

The Draft and Final Reports of the 2015 Methodology Review contained time series data on ABS Average Weekly Earnings (AWE) and Survey of Education and Training (SET) data as a way of demonstrating long term relationships between movements in private and public sector wages. These charts were not compelling evidence and did not conclusively demonstrate a relationship strong enough to base a differential assessment on.

In addition, the work of the Queensland Statistician's Office, undertaken to support submissions to the 2015 Methodology Review, highlighted that the line of best fit for relative public sector wages was not statistically different from zero based on the 2009 SET data. This implies that there was no strong relationship between public and private sector wages based on that data. Notwithstanding that a stronger (but not conclusive) relationship was found in prior years, this in itself would be sufficient evidence to question the conceptual underpinning of the entire assessment or heavily moderate its distributional impacts.

National market

The Commission appears to hold the view that public sector wages are predominantly driven by regional labour market influences with national wage pressures being less of a driver.

South Australia accepts regional labour market factors may have some impact on public sector wages but we continue to hold the view that for the majority of public sector employees, the labour market has a predominantly national job-specific character.

Wage levels of public sector employees in one jurisdiction are more heavily influenced by developments in job specific labour markets in other jurisdictions, rather than by generic local or regional labour market influences.

As discussed in previous submissions, in nearly all public sector wage negotiation processes (especially for teaching, nursing and police) relevant unions refer to interstate wages as a key justification for pay rises and changes in working conditions. Unions, like the Australian Education Union, maintain wage comparison charts on their websites to allow their members to observe wage rates and movements in other jurisdictions.

The Commission has provided a comparison of wage levels for nurses, police and teachers and have observed differences for what appear to be the same level of employee. These observed wage differentials are more likely to be the result of differences in responsibilities, differences in employment status (eg tenure), timing differences from when pay adjustments take effect, the impact of non-wage benefits and other policy choice differences.

Underlying wages are more likely to be driven by national factors in each job specific market.

South Australia believes that current assessment approach does not recognise the existence of national influences on public sector wages and this should be additional justification to moderate distributions for this assessment.

Public sector productivity differences

South Australia continues to hold concerns about the true comparability of employees across jurisdictions.

Jurisdictions with larger labour markets can offer greater and more diverse employment opportunities than smaller jurisdictions. This can lead to highly skilled and ambitious individuals leaving smaller jurisdictions and moving to the larger cities.

The result of this is that governments in larger jurisdictions may have access to a labour pool that is relatively more productive than the labour pool available in smaller jurisdictions.

This factor is outside of the control of jurisdictions but it is recognised that this influence is difficult to quantify. Again this is an area where judgement could be exercised by the Commission.

Dominant employer influence

In submissions to the 2015 Methodology Review, South Australia questioned the appropriateness of using private sector wages as a “policy-neutral” proxy for public sector on the basis that for many public sector occupations the public sector is the dominant employer and is driving private sector wages. This brings into question the policy neutrality of private sector wages for occupations like nurses, teachers and police.

South Australia continues to hold this view.

REGRESSION APPROACH

As previously discussed South Australia does not believe that states face a disability in wage setting, however, we make the following observations about the regression approach adopted by the Commission.

In Submissions to the 2015 Methodology Review, South Australia restated its long held view that the residual state regression coefficients are substantially affected by omitted variable bias particularly that obtained for New South Wales (the Sydney factor). We made the point that human capital quality or intensity varies across state labour forces.

Assuming that jurisdictions initially have a uniform distribution of individuals with above average intellectual and productive capacity, the geographic concentration of high remuneration will cause a geographic concentration of highly skilled individuals. At any point in time, the distribution of employment will reflect a migration of highly productive individuals to highly remunerative locations.

As a result, it cannot be concluded that an analysis of truly comparable employees can be achieved by simply controlling for industry and occupation.

CAPITAL CITY AND REGIONAL LOADINGS

Commission staff are proposing to base their wage cost assessment on capital city wages rather than whole-of-state wages. Commission staff hold the view that for most parts of the public sector, wages are determined through state-wide agreements, the outcomes of which are influenced by the need to attract and retain staff in all locations. Usually the highest cost locations will be capital cities, therefore, wage outcomes will be determined with primary reference to capital city wages. Commission staff note that this approach does not hold for states where regional wage costs are generally higher than capital city wage costs (like parts of Western Australia).

Based on their analysis of existing data (SET), Commission staff believe that there are significant differences in private sector wages between capital cities and the rest of the state, with private sector wages higher in capital cities, while public sector wages are more uniform.

The Staff Discussion paper notes that if New South Wales set wages at one per cent above the national average (New South Wales' average difference from the national average) it would not be able to compete for staff in the Sydney labour market where private sector wages are four per cent above the national average. Therefore, private sector capital city wages are a more appropriate measure of interstate wage differences.

Should the Commission decide to retain an interstate wages assessment, South Australia is inclined to support retaining the whole-of-state approach.

We are not aware of any evidence that suggests that public sector wage outcomes are solely based on capital city wage levels. Public sector wage outcomes are influenced by a number of factors including wage levels in other jurisdictions, union involvement and budgetary capacity of respective governments. Given that the conceptual foundations of the wages assessment are already questionable, introducing a major methodological change that is not supported by a solid evidence base, could make the assessment even more unreliable.

Retaining a whole-of-state approach negates the issue of whether wages are higher in capital cities or in regions. A whole-of-state approach uses the state average.

South Australia also holds concerns about the reliability of the regression analysis based on reduced sample sizes if the capital city and regional wages are disaggregated. As the assessment will be based on currently unavailable data this cannot be assessed at this stage.

Although retention of a whole-of-state approach appears more appropriate, South Australia reserves its final position on this issue until the precise coverage and quality of the new data source can be considered.

South Australia does not have a definitive view on how capital city labour market areas should be defined. At this stage we are, however, inclined to support the Queensland proposal that the appropriate benchmark level is the Major Cities classification of the Accessibility/Remoteness Index for Australia (ARIA).

The inclusion of the Gold Coast/Sunshine Coast with Brisbane and Newcastle/Wollongong with Sydney sounds appropriate as these broader geographical areas are likely to comprise a single labour market and be subject to the same wage pressures.

Should the Commission propose a capital city based assessment, South Australia would like to see the impact of adopting the Major Cities classification of the ARIA and impact of adopting the ABS Greater Capital City Statistical Area prior to any final outcome being determined.

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