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2016 Update

Wages Costs Assessment

Tasmania's Response to Staff Discussion Paper CGC 2015-03S

Department of Treasury and Finance

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Introduction

The staff discussion paper states that Commission Staff are particularly interested in State responses to the following dot points:

- Whether Staff have accurately captured the essence of each State's arguments;
- Whether Staff assessment of those arguments adequately addresses them; and
- Any new arguments States wish to present.

Prior to addressing these questions, some general comments on the paper are set out below.

General comments

Tasmania notes that there are numerous economic theories relevant to the Wages Input Costs assessment and that labour economics in particular is a complex and sometimes controversial area of enquiry. The CGC's own information paper on the history of the Wages assessment states: "The inclusion of allowances for interstate differences in wages has been one of the most contentious issues since the very first review of State relativities in 1981".

The contention appears to be due to the difficulty in proving conceptual cases for or against the assessment and the issue of what evidence would falsify a conceptual case. For example, Figure 4 and Figure 3 in the staff discussion paper (that shows how relative public and private sector wages for comparable employees have changed across the four SET surveys) could be interpreted as the Tasmanian Government being sensitive to national average wages to attract and retain suitable staff in the public sector due to national market effects for Tasmania, in the face of consistently low private sector wages. Alternatively, it could be described as Tasmanian Government policy choice in a low wage regional labour market.

For Tasmania, the contentious nature of the assessment also stems from the fact that the Commission's model of underlying public sector policy neutral wages states must pay does not reflect the reality of public sector wage setting for Tasmania where private sector wages in Tasmania are not used as a basis for negotiation.

The staff discussion paper states that some theories may predict that wage levels will eventually equalise but that from the perspective of HFE the CGC are not concerned with long run equilibria, but rather, markets as they operate in given assessment years. The paper states that it should also be noted that the relative importance of the theories in driving relative wage differences is likely to vary across states and over time.

Tasmania considers that this is an important point made by Commission Staff. This effectively means that, should there be a correlation between public and private sector wages for comparable employees, it can be broken and subsequently reappear years later (or potentially never return).

This highlights the importance of regularly reassessing the Wages assessment for its validity. This has been hampered by the lack of new survey data (the current assessment relies on 2009 SET data that showed a considerable weakening in the relationship between public and private state coefficients). According to the ABS the new Compensation of Employees survey will be conducted annually.

The lack of new survey data since the 2009 SET results added to the already contentious nature of the Wages assessment and having an annual survey should improve the debate (assuming the data are reliable).

However, even with annual updated data that are reliable, Tasmania is concerned about the lack of discussion on what evidence would falsify the Commission's conceptual case.

Commission Staff have stated that they consider the correlation between the public and private sector wages can only be used to shed light on the conceptual case regarding the functioning of these labour markets, not prove the validity of the conceptual case. Even when the correlation between public and private sector wages was shown to be not statistically significant, the Commission continued with the assessment citing the potential for lags between public and private wages and that enough data points were in the quadrants consistent with the conceptual case.

With the pending release of a new ABS survey that is to be an annual survey this question needs to be addressed. For example, it is not clear whether another statistically insignificant result for comparable public and private sector employees (similar to the 2009 SET result) would or would not be grounds for ceasing the assessment until clear evidence emerges of regional labour markets.

Should there be moves to more of a national market followed by a move back to regional markets within the duration of a few years there is a method dilemma in that it is not clear when to cease it and then reinstate it. Given that Staff agree that the various impacts on labour markets can come and go across Australia and can have different impacts for different jurisdictions, Tasmania is concerned that the assessment can continue for longer than what is actually appropriate.

Have Commission Staff accurately captured the essence of Tasmania's arguments; does Staff assessment of Tasmania's arguments adequately address them; and any new arguments?

The discussion paper states that Queensland, South Australia and Tasmania have argued that State Government wages are not impacted by regional influences and are instead driven primarily by national market pressures. These States also argue that State public sector wages will therefore converge under these common influences. This view implies that any observed differences reflect either a policy choice of the States or timing differences in wage setting and thus no assessment of disabilities is required.

Staff state that they have not observed evidence that public sector wages are equal across States even in those occupations for which the State government is a major employer. Staff state that regional market influences and national market influences can and do exist together.

Tasmania notes that with a national market at work, wages are never going to be perfectly equal. Secondly, if both influences are working at the same time, for a small jurisdictions like Tasmania with a private sector that is more like a regional area of a large State with very large dense cities, the national effect is the overwhelming factor more so than other states.

The discussion paper states that Tasmania has for many years argued that the private sector is not an appropriate proxy for the wage pressure faced by the Tasmanian Government. It argues that the conditions faced by the Tasmanian private sector are so different from those faced by the public sector that Tasmania must set wages at levels high enough to attract and retain qualified employees from similar occupations interstate. Effectively, Tasmania argues that it operates in a national market for public sector labour, even if other States do not.

Tasmania would argue that it is still the case that the depth and breadth of Tasmania's economic activity, as a whole, is more like a regional area of other states. Nevertheless, Tasmania is a state in the Commonwealth and must provide the necessary public sector staffing and infrastructure to provide the full range of state services.

As the Commission stated in the 2004 Review, the effects of "isolation" on wages is one of the causes of the location effect that the CGC are trying to measure in the Wages assessment. An isolated jurisdiction in a federation may need to offer a premium to attract the necessary staff to provide the full array of state services. A major difference between the public and private sectors in a jurisdiction, in terms of the effects of isolation, could affect the assessment.

For Tasmania, low interstate movement into Tasmania's private sector (low private sector labour mobility), given its regional nature on a national scale, means the private sector wages, which are acting as a proxy for underlying public sector wages, will not show an isolation premium (that the public sector faces).

To the extent that the state government needs to attract interstate employees into the public sector, the CGC's method, which uses private sector wages as a proxy, could understate Tasmania's underlying public sector wage levels.

As a result the CGC set Tasmania's location effect equal to that for the State with the next lowest location effect because it considered that the low mobility of labour in the private sector in Tasmania meant the analysis might understate the wage levels required to attract staff needed to provide State services.

However, the 2009 SET results prompted the CGC to change their approach. The CGC stated that they previously applied the Tasmanian adjustment because relative public sector wages could not fall as low as Tasmania's relative private sector wages, i.e. there are bounds within which public sector wages lie. According to the CGC this assumption is no longer sustainable since relative public sector wages paid in Victoria or South Australia are now comparable with Tasmania's relative private sector wages.

The dilemma with this approach where new, point in time, survey data result in changes to regression output (especially when the surveys are infrequent) is that the output can be explained away as policy choice, or part of a transition to some new steady state consistent with a State's (or the Commission's) conceptual case, or sampling error. For example, is Victoria's result in the 2009 SET showing its relative public sector wages being a fraction lower than Tasmania's relative private sector wages policy choice that is simply a one-off (and is unsustainable as it goes beyond the lower bound that exists and will subsequently have to move closer to the average) or sampling errors in the data. Presumably Tasmania would still have a state-specific discount if the SA and Victorian results were only marginally higher.

In response to the 2009 SET results, the Commission stated that it considers the relationship in individual years could be affected by lags, policy choices and other factors, which would not invalidate the underlying relationship (between public and private). Similarly, Tasmania could argue that the 2009 SET results do not mean Tasmania's private sector results become an appropriate proxy for the underlying pressure on state wages.

The staff discussion paper states that Staff note that reweighting the regression to reflect the public sector education profile lowers Tasmania's relative wages. According to the paper, this indicates that private sector workers with similar levels of qualifications to public servants are paid even lower relative wages and that this does not offer support for the theory that Tasmania is operating in a national labour market for public sector type employees. Tasmania would question the reliability of this result given the small sample size for Tasmania.

Tasmania notes that the consultant has been asked to consider state exemptions or adjustments, which is appropriate. It is also appropriate that this issue be part of the analysis and discussions following the release of the new survey data.

Data from state public service commissions

On 17 September 2015, Staff sent an email to States stating that Staff are trying to determine whether capital city or whole of State private sector wages should be used for the Wages assessment. One part of this question is whether States pay comparable wages for comparable employees in different regions across the State. Commission Staff have identified that most States have public service commissions which produce workforce datasets that contain wage and location data. Such data could offer further insight. States may wish to include analysis of this data in their submissions (either the ones due at the end of this month, or the follow up submissions due in December).

Tasmanian Treasury has made an enquiry with the State Service Management Office as to whether state wages data by location is available for analysis. If data can be obtained, analysis and comments may be provided in the next submission due in December 2015.