Wages Policy and the 1991 National Wage Case: An Economic Perspective

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Abstract

The National Wage Case decision of April 1991 has provided a crisis for the implementation of wages policy in Australia. Since 1983 wages policy has been implemented under a process which requires consistency between the principles under which the Industrial Relations Commission determines National Wage Case adjustments, and the elements of successive Commonwealth Government/ACTU Accords. The 1991 decision represents a rejection by the IRC of the thrust of the Government's wages policy as presented in Accord V1. It is argued here that it is the shift in the primary goal of wages policy, from control of inflation to the promotion of allocative and operational efficiency, which has provoked the crisis. Unlike the Government, the IRC was not prepared to abandon control over the aggregate wage outcome in the pursuit of the uncertain productivity benefits of enterprise bargaining.

1. Introduction

The National Wage Case decision of April 1991 appears to have brought to an end the process by which Wages Policy has been implemented in Australia since 1983. This process has been based on the Accord (a negot-

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iated agreement between the Commonwealth Government and the ACTU on the parameters for union pay claims), and the determination by the IRC, in regular National Wage Cases, of the principles under which it will make awards and ratify wage settlements.

Of course the demise of the Accord-based system has been confidently predicted on other occasions. The system has managed to survive by making sufficient adjustments in response to both changing economic circumstances, and to the strains of the various competing (and often conflicting) goals for Wages Policy.

It is argued here that it is the changing nature and priorities of the goals for Wages Policy that have this time provided a watershed, from where the future path of Wages Policy is uncertain.

2. The Changing Priorities for Wages Policy

The relationships between the various goals of economic policy - macroeconomic (high growth in aggregate production and employment, low inflation, balance of payments stability) and microeconomic (allocative and productive efficiency in resource use) are complex. Similarly complex are the interrelationships between the various policy instruments of government (Fiscal, Monetary, Industry, Exchange Rage, and Wages Policies), and the relative potential contribution of each to the achievement of goals is more complicated than the assignment of particular instruments to particular targets. (These issues are considered in detail in Stegman (1987)).

It is a useful and not misleading simplification, however, to see the principal goal of the Wages Policy initiated in 1983 under Accord I, as the control of inflation. As an alternative to fighting inflation "down the Phillips curve", with policy to restrict Aggregate Demand and consequent costs in unemployment, the incoming Labor Government viewed control of wage-induced inflation as more efficiently achieved through more direct control over the general level of wage outcomes.

The primacy of the goal of control over the general level of wages, and its rate of increase, implies the need for a centralised system, with norms or principles for wage increases applied generally, and strict limits on the ability of wage and salary earners to achieve increases outside the principles.

Lacking the constitutional power to itself directly control wages, the Labor Government has sought to implement a centralised wages policy through a negotiated agreement with the peak council of the union movement, and to then have the agreed parameters ratified by the IRC in its determination of National Wage Cases principles. Thus the Commonwealth Government relies on the authority and standing of the IRC, the willingness of the IRC to incorporate the elements of Accord agreements in its determination of principles for National Wage adjustments, the consistency of the determinations of the various state and industry tribunals with National Wage Case principles, and the ability of the ACTU to provide compliance by its constituent unions with the "no extra claims" provision of wage awards.

The first major test for the Accord-based system came in 1985.

From 1983 to 1985 the system had proved successful in allowing both the pursuit of expansionary demand management policy and a winding back of the inflation rate. [Inflation averaged 6.9% p.a. over the period, compared with 10.3% p.a. for 1980-1982, employment grew strongly and the profit share of aggregate income recovered from its 1982/83 slump (See Stegman 1987)]. However by 1985 this pro-growth policy had run into the traditional problem for Australian policy makers - the Balance of Payments constraint.

Australia, with a high and inflexible import propensity, cannot sustain high domestic growth without commensurate growth in the value of its exports. By 1985, with a series of increasing Current Account deficits, and the resultant alarming rise in foreign debt (requiring debt servicing payments which themselves add to the Current Account deficit), continued growth urgently required a greater contribution from net exports. Australia's over-reliance on a narrow range of commodity based exports, the markets for which are subject to short-term instability and poor long term prospects, provided even more urgency to the problem for policy, as commodity prices weakened in 1985.

The essential requirement if restrictive policy was to be avoided, was a restructuring of domestic production in favour of new and expanded exports and (more controversially) some import replacement.

In pursuit of this restructuring the Government allowed a substantial devaluation of the currency in 1985. The gain in competitiveness for domestic industries and the shift in the relative prices of traded and non-traded goods, was to provide the impetus for the required shifts in the pattern of resource allocation and the composition of domestic expenditure.

Economic theory argues that such a policy requires a fall in real wages. If wage earners are fully compensated for increases in the domestic price of imports, then the competitive advantage and allocative signals sought from the currency devaluation are eroded by domestic inflation. Since Accord I had provided for full CPI based indexation, its principles were inconsistent with the restructuring policy.

A renegotiated Accord in 1985 provided for discounting of the indexa-

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tion formula for the estimated effects of the devaluation, and the resultant moderate wage outcomes under the principles of the 1985 and 1986 wage cases allowed the nominal devaluation to be translated into a real devaluation with consequent potential competitive advantages for Australian producers.

The principal goal of Wages Policy under Accord II remained the control of the aggregate wage outcome and general wage inflation - the achievement of this macroeconomic goal would provide support for the microeconomic goal of restructuring.

By 1987 the restructuring through devaluation policy had provided no relief for the external problem. Not only had the current amount failed to improve, there was evidence to suggest that the required shift in the composition of investment expenditure (necessary to provide the *capacity* for a restructuring of domestic production) had failed to materialise. (See Hillier & Stegman 1988). The emphasis of economic policy now became directed towards achieving increased competitiveness and allocative restructuring through productivity gains delivered by *microeconomic reform.*

Wages policy was asked to play an increasingly important role in this process. The wage determination system was required to provide the incentives for changes in work practices and award classifications, to make them "relevant to the competitive requirements of industry" (NWC 1991, p. 19).This emphasis is evident in the agreements of Accords III - V and the principles of the National Wage Cases of 1987-1989. These cases determined amounts payable across the board (as either flat rate or percentage increases) for wages generally, but the awarding of the maximum amount was made dependent on claimant unions demonstrating, on a case by case basis, productivity offsets or progress on award restructuring.

While the pursuit of the microeconomic goals of productivity enhancement and restructuring had become an explicit aim of wages policy, the control of wage based inflation remained as a principal goal. Since the maximum amounts allowable were determined by the Commission, control over the aggregate wage outcome was maintained.

Over the period 1987-1989 the wages system continued to deliver moderate wage outcomes and reductions in the level of real wages, but progress on microeconomic reform was slow. With no improvement in the external accounts, the Government was forced in 1989 to apply the monetary policy brakes with increases in interest rates. By 1990 the economy was heading into recession, with an exchange rate now generally regarded as overvalued.

Since a depressed economy and an overvalued exchange rate were acting to reduce inflationary pressures, the Government felt able to demand a greater contribution to microeconomic reform from Wages Policy, at the expense of its anti-inflationary role.

Accord VI, concluded on 21 February 1990 and renegotiated on 20 November 1990, represented a fundamental change in the direction of Wages Policy. Centralised control over the aggregate wage outcome was to be virtually abandoned in pursuit of the achievement of allocative and productive efficiency through decentralised bargaining.

3. Accord VI: Wages Policy as an Instrument for Microeconomic Reform

The ACTU claim, at the National Wage Case begun in December 1990, supported by the Commonwealth Government as part of Accord VI, comprised:

(a) $12 for all workers on the basis of a continuing commitment to structural efficiency;

(b) a phased in 3% increase in employer superannuation contributio;ns

(c) additional wage increases based on productivity and profitability through enterprise bargaining.

The superannuation element continues a policy, begun in Accord II, of seeking to translate some proportion of increased work-force rewards into superannuation benefits. While this policy has long term goals for both the Government (in terms of Retirement Welfare Policy) and the union movement (in terms of its policy of creating career structures), it can be presented as making some contribution to the alleviation of the Balance of Payments problem. To the extent that the Current Account deficit is interpreted as the result of inadequate National Saving, the translation of wage increases into forced saving, rather than being available for spending on imports, can be viewed as beneficial.

The crucial element of Accord VI is the scope it allows for enterprise bargaining.

Overaward payments at the enterprise and industry level have always been a feature of the Australian wage system. The main thrust of Wages Policy under Accords I - V was to control and limit the size and extent of these payments, through the 'no extra claims' provisions of awards, a narrow range of exemptions (under section 115 of the Act), and the use in some cases of 'paid rate' rather than minimum rate awards. The success of the Accord has been judged on the extent of its ability to minimise 'wage drift'.

The shift in policy towards authorisation of wage bargains based on productivity and profitability at the enterprise level raises two issues for the New Wages Policy:

(i) the extent to which enterprise level bargaining can produce the gains in allocative and productivity efficiency which will provide an easing of the external problem;

(ii) the industrial relations environment in which such enterprises bargaining will take place and the form it will take.

With regard to the first issue, criticism of the centralised wage system has always focussed on the lack of flexibility it provides for wage outcomes. Flexibility in wage relativities, both at the enterprise and industry levels, to reflect changes in demand and supply conditions and to provide the incentives and rewards for efficiency, is seen by advocates of a decentralised system as essential in a market based economy.

In relation to allocative efficiency there is a substantial amount of evidence that labour markets (both in Australia and overseas) can accommodate significant changes in relative labour demand and supply conditions through non-wage adjustments (eg. variations in employment opportunities, variations in hiring and separation rates). There is a substantial body of economic theory which suggests that such non-wage adjustments can be efficient in labour allocation (see Stegman 1987).

In relation to productive (operational) efficiency, however, gains achieved through changes to work place behaviour and relationships are won at the enterprise level, and would seem to require negotiations and agreements which take account of enterprise specific circumstances.

Nevertheless the argument that allocative and productive efficiency is stimulated by enterprise or industry wage bargains based on enterprise or industry *capacity to pay* is logically flawed.

In the competitive models which provide the theoretical basis for the decentralist philosophy, mobility of labour provides a tendency towards equalisation of wage levels for comparable labour. Competitive firms face similar wage costs.

In an imperfect world, capacity to pay wage outcomes will not only allow "sweetheart" wage agreements for firms with monopoly product market power, they will also allow low productivity firms to pay lower wages, thus prolonging the survival of inefficient firms and providing no incentive for investment to improve productivity (See Salter, 1966 p. 153). The operation of a capacity to pay system may be detrimental to the achievement of efficiency and productivity goals.

Assuming that an enterprise bargaining based system can deliver improvements in work practices, the magnitude of the resultant productivity gains and the contribution of these gains to correcting the Balance of Payments, remain matters of conjecture.The 1991 National Wage Case decision notes (p. 15) that the Commission was presented with no evidence on the magnitude of the potential productivity growth in devolution of the industrial relation system to the work place.

In relation to the dimensions of the structural reform and increased competitiveness required by the Australian economy, the most important need is for an appropriate level and composition of capital expenditure, both in plant and equipment and in infrastructure (see Stegman 1990). This is something Wages Policy cannot by itself deliver.

With regard to the industrial relations environment and the form in which enterprise bargaining would operate, Wages Policy as presented in Accord VI provided no consensus.

Although the Accord partners agreed on a system of enterprise bargaining based on productivity and profitability, their submissions to the NWC revealed some confusion as to how this concept would operate in practice.

Accord VI had provided that 'the increases shall be monitored by the parties and the IRC, to ensure consistency with the aggregate wage outcome' (NWC, 1991 p.14), but the ACTU submission argued that there should be no prescribed ceiling to the increases and that they should be provided in Section 115 agreements or in paid rate awards.

The Commonwealth submitted that 'the results of enterprise bargaining would most commonly be via overaward payments' (NWC, 1991 p. 15).

Neither approach would provide control over the aggregate wage outcome.

On the employer side, submissions to the NWC evidenced a variety of views as to how enterprise bargaining should operate.

The Confederation of Australian Industry rejected profitability as a criterion and saw the need for a provision which 'would place strong emphasis on consultation between employers and employees, without the requirement for prior union or Commission approval before any agreement reached could be implemented' (NWC, 1991 p. 28). The Australian Chamber of Manufactures' submission also opposed the use of profitability as a criterion but appeared to envisage the provision of enterprise wage increases in some combination of Section 115 agreements, variations in paid rates, enterprise supplementary payments, and overaward payments.

Both the Business Council of Australia and the Metal Trades Industry Association submission expressed doubt that the system was ready to accommodate enterprise bargaining.

While in favour of a shift to enterprise bargaining the BCA saw a need for 'the provision of institutional arrangements which make the emerging wage setting process sustainable economically and industrially' (NWC 1991, p. 29)

The MTIA was a 'reluctant party to the enterprise bargaining proposals arising out of the ACTU/ Government Accord' (NWC 1991, p. 30). The move was premature according to the MTIA because of inadequate progress on the structural efficiency principle.

There is some irony in this argument because such progress as has taken place under the application of the structural efficiency principle, has so far been much more in accord with a union movement agenda, than with employers' aims. Achievements have been concentrated in the areas of job classification, multi-skilling, career structures, and training provisions, rather than in the areas of working hours, over-time, penalty rates and increased use of part-time work. The result has been a tendency toward providing increased labour mobility and flexibility within a more formally structured labour market environment rather than a less structured one. This process, together with the general direction in which coverage issues have been determined, has provided a current environment for enterprise bargaining very different from the vision embodied in the industrial relations policy of the Federal Opposition. Rather than negotiations between individual employers and enterprise work force representation, the likelihood is for individual employers to face negotiation with large national unions, although the number of unions that an individual employer must deal with has been reduced.

Enterprise bargaining under these conditions places great bargaining power on the side of the unions, with the ability to 'pick-off' employers one by one.The experiences of the 1960s and 1981-82 suggest that such an environment is conducive to increased industrial disruption, excessive wage outcomes and the development of restrictive practices.

In summary, Wages Policy as presented to the IRC for endorsement in Accord VI represented a fundamental shift in the priorities of policy. The benefits of the proposed system were uncertain and the operation and implementation of that system was a matter of confusion and disagreement among the parties.

In the event, the IRC declined to provide the endorsement.

4. The National Wage Case Decision and the Role of the IRC

As has been argued above, the implementation of Wages Policy since 1983 has required the consistency of the principles of National Wage Case determinations with the elements of the ACTU - Government Accord. However the IRC has constitutional and legislated responsibilities and does not regard itself as a mere rubber stamp for Government policy. Although the Accord expresses the Government's approach to Wages Policy, the Commission's view is that it is not an 'agreement' for its purposes, since employers are not party to it (NWC 1991, p. 9). The Commonwealth's submission, like the submission of other parties, is considered and tested against the Commission's interpretation of its statutory responsibilities. The Commission's criteria include equity considerations and the promotion of industrial harmony. Under Section 90 of the industrial Relations Act of 1988, it is further required to take account of the effects of its decisions on inflation and unemployment. Therefore it is to some extent an independent source of Wages Policy with the opportunity to disagree with the thrust of government policy - in its 1991 decision it has done just this.

In National Wages Cases from 1983 to 1989, the elements of successive Accord agreements were generally included in the determined principles. The Commission had on occasion made minor modifications, and often expressed its reservations, but it had in the main been willing to endorse the Accord agreements and thus provide for the implementation and institutional processing of the Government's wages policy.

In its decision of April 1991, the IRC rejected all the major elements of Accord VI.

The main elements of the decision were:

(a) provision for an increase of 2.5 percent in all award rates, accessible on application, to maintain the process of structural reform;

(b) an adjournment of the superannuation element of claims pending a national conference on superannuation;

(c) a refusal to endorse any system of enterprise bargaining based on criteria other than the structural efficiency principle.

The awarding of a general increase on a percentage basis (rather than flat rate) reflects the Commission's desire to maintain stability in award relativities and its unwillingness to provide assistance to low paid workers by measures which compress relativities. The superannuation element of the decision recognised the widespread perception that the implementation and administration of award based superannuation schemes are subject to continuing problems - both with diversity of conditions and extent of non-compliance. The Commission obviously thinks the administrative problems should be sorted out before further moves on award based superannuation are undertaken.

It is the refusal to sanction any system of enterprise bargaining based on productivity and profitability which directly confronts the Government's new Wages Policy. The Commission's refusal was based on its concerns about the consequences of such a system for inflation and for industrial relations.

The Commission was loathe to discard the equity and industrial harmony benefits of distributing productivity gains as a "national dividend" in general increases, by moving to a system which would generate instability in wage relativities. It believed that there was a "lack of a receptive environment" in which the sought after productivity gains from enterprise bargaining might be achieved - without such an environment there was a likelihood of industrial disputation and excessive wages growth (NWC 1991, p. 37).

In summary, the Commission was not prepared to endorse and implement a system which provided no controls over the aggregate wage outcome.

The immediate reaction of the Commonwealth Government to the 1991 National Wage Case determination was to join the ACTU in rejecting the decision, and to begin a process of seeking to subvert the decision through the fostering of industry and public sector wage agreements based on Accord VI and therefore outside the National Wage Case principles. While the legal standing of such agreements for workers covered by Federal awards may be uncertain, to the extent that the awards of state and industry tribunals ratify Accord VI-based agreements, the nexus between the principles applied by these tribunals and those of the National Wage case will be broken.

The refusal of the IRC to act as the vehicle for the implementation of the Government's New Wages Policy, and the refusal of the Government to accept the National Wage Case decision as a constraint on the pursuit of this policy, has destroyed the institutional relationships which have provided the framework for the operation of Wages Policy since 1983.

When the principal goal of the Government's Wages Policy was the control of inflation via control over aggregate wage outcomes, this framework had proved resilient and successful. It has proved incapable of accommodating the shift in the principal goal of Wages Policy to the provision of the impetus for microeconomic reform through enterprise bargaining.

At the time of writing, in the immediate aftermath of the National Wage Case decision, future developments in the implementation framework for Wages Policy are difficult to predict. There is no doubt however that the authority and standing of the Commission, and thus its ability to control the general level of wage increases in the future, has been damaged, perhaps irreparably, by the confrontation between it and the Government. In the current conditions of recession, an eruption of wage inflation may seem unlikely (although the experience of 1981-82 demonstrates that high unemployment and wage inflation can co-exist). The real test for any emerging system will come when the economy begins to recover from the present recession, or if there is a devaluation of the currency. In such circumstances there may be a need for a shift back in the priorities for Wages Policy to again concentrate on the control of inflation.

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