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RECORD OF MEETING

ECONOMIC, EDUCATION, JOBS & SKILLS COMMITTEE

AND ASSOCIATE PROFESSOR STEVE KATES

11am Friday 18 December 2015
55 St Andrews Place, East Melbourne

Mr ELASMAR: What's your view on who will benefit from portable long service leave?

Associate Professor KATES: I don't know that anybody would actually benefit from portable long service leave. My view is that the way the labour markets work, people are paid more or less the value they bring to the business. What you would do is just change the way this would unfold. The immediate impact would be something of an issue to confront but as time elapses less will be paid in wages, more would end up in the kind of contingency fee for the long service leave. There would be, over time, no actual increase in cost, no actual benefit of increased return to the employee.

I think what is more likely is that you would end up with some slight shift in employment away from these industries because the relative cost would shift slightly. Other than that I don't think there's any benefit to anyone but over time there's not an awful lot of cost either.

Mr ELASMAR: And which sectors would benefit least from portable long service leave?

Associate Professor KATES: Well I'm assuming basically that it will come in the form of money so that there'll be this contingency pro rata. If it's typically like in construction that you move from job to job to job or something like that you may not actually take the time. It's not like being in a business and you're there for 10 years and then suddenly you're gone for three months. This will often be just the money will come in the same way. It'll just be some kind of payment.

If it does however come in the form of lost time so that the three months, you actually get to three months and someone's paying for this I see two forms of problem. The smaller the business the bigger the potential disruption, so that public service you wouldn't notice it. Someone goes, someone slots in.

The smaller the business and especially if you see someone's been there long enough to have actually been there long enough to accumulate long service leave the disappearance of someone for a period of time, for the three months can be a problem, a serious problem, difficult to find people to replace people for such short periods of time, to get those skills. You have to train them up beforehand. There will always be inefficiencies that are introduced. It just adds a bit of sand to the gears. It just doesn't work as well.

For the employees themselves with so many things that are paid like annual leave so if you work casual you get your annual leave as kind of a lump loading. For some employees they actually may prefer to just get the payment. Then they're not having to defer seven to 10 years into the future.

The actual introduction of this will have I think limited benefits to anybody but will have costs that will have to be borne for the businesses and I even think for the employees.

The market is a very finely tuned instrument and it's surprisingly accurate so that over time and the economy's going to increase productivity and we're going to be able to pay everybody more so this will shift along.

Within all of this there will be this, very fine, hard to even notice it, but the employers who are now suddenly greeted with this impost that they didn't have before will find they just simply can't pay as much. They will be making these provisions for long service leave, there'll be whatever actual accountancy or administrative costs that will build into whatever they do, so employees, as they flow through over time, will just simply find that the amount of money they take home will be shaded.

This is not huge amounts but it is nevertheless they will find that they're getting paid less. The market will adjust. It will accommodate this so that they may say great, we've now got this long service leave and maybe they may even think that, but I don't think most people actually understand the true subtleties of the market. You say to them you're going to end up with lower take home pay over the next seven years that will finance this because that's what must happen. They may, if you give them that option, say no I'd rather not, I'll take the money now thank you very much.

Ms RYALL: We have spoken to another economist and he talked about it's sort of like the economy, what happens in terms of those adjustments that are made to balance out. Can you give us examples of where that might have happened in other instances?

Associate Professor KATES: I was back in the Chamber of Commerce in the days of the super guarantee and the productivity case back in '86. Everybody agreed, there was simply agreement across the bar table from everyone that over time the super guarantee would be paid for by employees.

Even though employers were paying it, the system was employer-funded superannuation, everybody knew that the way that over time things would evolve people would get a payment of a certain amount, based on how much value they create, how much they can afford to pay you and some of that would be shifted into the super guarantee and employees would end up with less take home pay.

The market has to work like that. Nobody can pay you more than you're worth but also the interesting thing about the market is nobody typically gets paid less than they're worth. A market like this where everybody has lots of opportunities, people can find jobs if they go looking for them. The market tends to keep the amount individuals get paid pretty close to what the market value is worth.

Ms RYALL: What do you see as the economic impacts that would occur? Obviously over time the economy adjusts but what would be those short term if you like economic impacts of introducing this?

Associate Professor KATES: Short term, well I used to run a business, you'd get this notice from the tax office and you go oh God, not this. You get this notice and suddenly you find you have this new impost. You go to your accountant or whatever and say how can I do this?

There will be this spinning of the wheel. This is just simply dead effort. It doesn't create any productivity. It doesn't cause any growth. It doesn't make your economy stronger. It's just simply one more adjustment that you have to accommodate through the external environment, soon there'll be that.

I'm sure this will be sort of phased in if it's introduced. It will make the employer suddenly— the more they are conscious of this, and they are conscious of this, they will, where they're offering wages for new employees, where they're offering different kinds of packages, this will be there. They may even feature this and they say you get long service leave but the more they're focused on it themselves the more they appreciate that there's workers comp and there's this and there are a million other costs and they will simply know the totality of what it costs.

Over time those industries will find that they are employing fewer people. It's a relative thing. You don't want to go over the top about it. This is not going to massively change industry but there will be this shifting, this accommodation that goes on as every individual employer takes this added burden into consideration on how they do things.

I wouldn't think over time the aggregate employment effects across all industries will be affected at all but in the particular industries where this is newly introduced there will be some relative contraction of employment compared with what otherwise would have been the case.

Mr NARDELLA: With your argument, Steven, somebody taking a month's leave with holiday pay can't be replaced and therefore the business fails. Is that your argument? Because what you're saying is that if somebody takes a month off on long service leave or three months of long service leave unlike holidays, we're going into the holiday period now, it may be impossible for them to be replaced and therefore that particular contract or that particular function can never be done and therefore you have all these business failures. That isn't the case, is it?

Associate Professor KATES: No, I certainly didn't intend to imply that but it will be an inefficiency that will actually affect some businesses—I mean you have five employees in a business say and everybody has a really important function, a well-oiled team and they all work together and then comes Christmas, everybody goes off and then they all come back. There's annual leave and people schedule that in.

This one comes and maybe they can accommodate this but the 10 years comes up and they say I want my long service leave, I'd like to go do this.

In fact one of the strangest things I ever found when I got to this country was that so many people I knew took long service leave. I said what did you do? Oh, I just stayed home. They didn't even use it and I thought that was odd.

Mr NARDELLA: Yes, absolutely but you've got somebody from the NGV, we've had people in here from the National Gallery of Victoria. The National Gallery of Victoria gives the contractor money to employ somebody and then the contractor changes. We've had evidence that about one per cent of that payment is for long service leave.

Over every three or four years that contract changes, NGV have paid for long service leave for whoever's there, the contract changes, that money just stays with the contractor and that bloke or that woman doesn't get any long service leave and they might be there 15—we've had instances of cleaners being in the job for 23 years. Because the contract's changed—the contractor's been paid for long service leave, it's only been about a per cent —but they've never gotten long service leave.

Do you think that's fair? Is that inefficient? Is that efficient? Is that just the market forces operating?

Associate Professor KATES: Yes, the word fair is a tricky one here. There's so many different kinds of accommodations that the labour market makes to all kinds of circumstances. But it's the—you can't—you say, well look, the money's been paid and you didn't get it. That seems like a slip in the system.

The kind of point I'm making here is that the—23 years of working this woman had this job. That's fantastic. She did have that job.

Mr NARDELLA: And the contractor got paid for that 23 years for long service leave.

Associate Professor KATES: I understand but you know, it was money that was pocketed by the contractor and who knows whether that was an important difference to their own profitability and profit and loss statement.

So far as they're concerned this is just all part of what they got and it's to run and operate their business. It was intended for this woman and had they maintained the contract with the company, with NGV they would have happily paid but they didn't have to.

Hard cases make bad law. The woman was happy to have her job. She may feel that this was a real—she would have loved to take that three months off. Why didn't she get it? I don't know. If you can fix that you can fix it but the money has gone into that pocket. The contractor's gone. You say to the NGV well look you've got to do that and then the NGV starts to put that on their own books.

The point I keep making is suppose you take this woman—I don't know how you're intending this to work but suppose she is now, you give her something and she is six years into the pro rata and she says I'd like another job. She quits but she's got to six years pro rata. She's now a problem to some other employer because she goes there and says or they say to her what's your long service leave entitlement by the way? I'm up to six years. Oh they say, six years. Does that mean you want to take long service leave next year or whatever? She says yes, I'm looking forward to it next year.

She brings a problem to a business by having this contingency standing there with her. She comes along and the business will be more reluctant to hire her than they otherwise would have been. You put an extra burden—you actually made her less employable, less marketable by the fact that you put it on her.

Now if this money just went up into the cloud somewhere and you could just—she could pull it down as money that's one thing but if she wants it as time off, which is what I presume you mean, she wants it as time off I can see it that there is this problem that someone's actually really been somewhere for 23 years and she was a contractor and didn't get it. If you said to her, someone, you now have this thing and it's owed to you no matter who you work for, the second employer will be very reluctant to take someone on who has that contingence liability sitting right there.

To replace an employee on long service leave you've got to find someone, know exactly what they're doing, they do the same work. We are not all interchangeable. We're all academics up at the university but someone goes away who's a specialist in interest rates and operation of the dealing room, well someone else has to be found.

Large organisations find it easier. The small organisations, the NGV I suspect would be towards the larger end. A company of five or six would be towards the smaller end and suddenly you just simply say that here is this lost time. This person will go and then you go goodness gracious and you hope that someone, everybody who is working really is that kind of person, they are an indispensable part of the operation, that you'll miss them if they're not there.

I think of the Melbourne Symphony. The conductor was the one saying that their lead flute, flautist or the cellist or whatever, he'd gone off sick and he says you know most people can't tell this but we can tell this. It's like you get second best cellist in Melbourne playing but there is that loss of whatever.

Ms RYALL: Can you think of a way where at a contractual level perhaps the government could make a consideration about that so as an alternative to introducing a sector-wide portable long service scheme there may be some way that actually deals with this issue that's creating a significant problem?

Associate Professor KATES: See if it's in terms of just money then the market already does that. People are getting paid—she's getting paid relatively more and in this case, in that particular case she's not.

If it's in terms of time lost I really do think the potential disruption that an employer will have to consider is a live issue. Someone comes with a pro rata already accumulated of six, seven years that they will say okay my long service leave is due, you won't have to pay me money but next year I'm going off.

If it was the same employer and there was some kind of fund that was built up that would actually—rather than going off to the contractor themselves there would become an entity where they own the actual obligation.

Ms RYALL: Rather than a sector-wide scheme it could just deal with these contractual issues.

Associate Professor KATES: That's right. I always go back to the 38 hour week and the great shock that everybody had because the recession that followed that was just so extraordinary. I remember Cliff Dolan used to be flabbergasted at how it just completely all fell apart. That was years ago, back in '82 or something. It just all fell apart. Within a year the unemployment rate went from about four per cent to 11 per cent. It was like wham.

It was absolutely causation, and I mean it came with money as well so there was large money and there were the hours but I always was very aware that once you start dealing with working time it's different because money's kind of like fungible. It goes in different pockets.

Once you start dealing with time worked you start changing the real situation at the workplace in a much more profound way. Everybody wants everybody to have everything and I understand. In the community people will appreciate that really you're basically getting paid anyway. The market is working for you and it's giving you as much as it can.

Nevertheless there may well be this grizzling, I don't get long service leave and all these other people do. If you're going to do it you'd have to attach it to the person and it would have to be as you said for someone who is at an enterprise, a particular and for the period of time. Once they move that's it. It wipes out. It's just simply you no longer have that long service leave.

Nevertheless I say that in recognition that the university system of course has this transferrable long service leave so you can go from Monash down to RMIT and you keep your long service leave. I think that's right. If you can have something like that but universities all agreed amongst themselves that that would be okay.

The universities, they're all in on it. They've agreed amongst themselves that we'll happily take on and in fact that's important for flexibility. People will move. If you're going to lose your long service leave somewhere—in fact that's one of the problems with something like that that comes only—say you're there seven years and the pro rata starts, by the time you enter the fifth year you want to move, you're not going to go. You keep it in your head that you've got two years, in two years' time I'm going to get this.

It becomes a kind of an obstacle to the free flow so the universities overcame this by just saying okay we will take your contingency so if you have an obligation, someone's been there eight years, we'll take that eight years and they can get it in two years when they come to us. What they lose by taking someone at eight years they also are able to—academics will move from one university to another without any problem.

A system like that might work but it would require everybody to be in agreement and that's very hard.

Ms RYALL: Part of our brief is to look at the economic impacts and the job impacts in this context. Obviously labour market mobility impacts those things. I just want your views on these issues.

Associate Professor KATES: You know we talk about the natural rate of unemployment. I find that a really empty concept but nevertheless you look at the gross statistics. There'll be this unemployment rate, five, six per cent. Okay this is more or less we're operating at peak efficiency. Although I remember when I came to this country the unemployment rate in Australia was one per cent.

The thing that's always struck me when I was dealing with this is that you take the gross productivity stat, you take the gross real wages stat and you can just see what's going to happen in unemployment. At the aggregate level it's just so clear that people on an average wage, the average wage is dependent on how fast the real underlying strength of the economy rises.

While that's true for the whole economy it may not be necessarily true for any particular individual but for the average person that's what goes on. The labour market, all markets, are just a piece of genius.

Ms RYALL: They adjust.

Associate Professor KATES: They adjust—people adjust—and every bit of that information gets filtered through someone that's trying to make a decision, an employment decision, a decision to relocate, to anything. It's all in there. Something like this, it just becomes one more, just one more bit that they have to accommodate. There are people who will in 23 years never have long service leave but they're a casual or they're a contractor and this is how it is. You say if you want long service leave you've got to get into a business that you work for that business. You can't do it as a contractor. A contractor may not work for you. It just may not work.

Mr BOURMAN: Some people don't have a choice though. I came from the IT field before I did this. Contracting is now becoming a way of life.

Associate Professor KATES: I'm just saying people do what they can so these are the compromises you make. As a contractor you may well find yourself less secure in other different ways.

I guess the point I'm really trying to make is that although someone like this woman will think that she's been hard done by I could sit down with her—and I don't even know—but I would say, well you know, the markets work, you did okay, you got the job, you kept it for 23 years, had a lovely environment at the NGV and this, this and this, you had all the security, you own whatever, you've got your house. You had this job so it's worked out.

If I think about long service leave, my neighbour across the road, she went back to Greece and so you say okay well not everybody can get everything. It's easy to be—I could be very philosophical about other people's problems. If you could fix it, if you could fix it without a serious—like adding to the burdens and in fact if you just said to someone I'm going to give you this option, you are a contractee, you can either—we'll give you this long service leave as a condition there and then whatever your employer after 10 years will have to pay, but that'll cost you or you can take this as kind of a lump sum of money and put some figure on it, the way they do with casuals. You take the lump sum money and you don't have that obligation ever but you'll get a little bit extra pay right now.

Mr BOURMAN: We had another economist on a while ago and they said obviously portable long service leave will be an impost but it would actually in some cases at least give people, an employer incentive to be more efficient obviously other than shedding staff.

Associate Professor KATES: Well I've heard it before often. You know at the end of the day it's just a business who will sit down and do the arithmetic. The productivity calculation is something that business will do automatically.

If you say that—I mean we can make, we can raise the productivity of the economy by raising real wages. I used to describe it as—in fact the phrase I used was 'spurious productivity'. You can get an increase in the aggregate level of productivity in the economy by sacking your least productive workers so the average will rise

They're trying to contain their costs. I mean a business that doesn't contain its costs until it's forced to the wall, in doing it is gone.

I mean it will do those things automatically. They won't leave the lights burning all weekends.

To raise labour costs as a way to force other economies on a business is very short sighted.

I mean this does happen, business start looking around at other ways to actually meet their payroll. If you push up costs they will do things, but ultimately the cost will be unemployment.

The labour market adjusts. Unemployment goes up and then it just disappears. We are a very, very adaptable economy. I'm always amazed by Australia. We do pretty good and we do pretty good at passing on productivity to workers. The real wages keep going up all the time, which is good.

But it is I think a serious error to actually try to force it, to say we'll raise productivity by making your employees unaffordable to you.

Ms RYALL: In terms of what you've said, if you sat them down and said look you'll either get it now or it's going to cost you in the long run, you have to make a decision, would that be ultimately happens? Do you want it now or do you want it later

Associate Professor KATES: Probably take the money now. Nobody waits. This is a very subtle issue that we can discuss amongst ourselves but the population's not made up of economists. They don't think about this. They know they're going to get their just due.

Everybody's got a short term horizon. They just take it.