To have or have not: A statutory minimum wage

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Cyprus and Italy are currently considering the introduction of a universal minimum wage floor by law. With this move, they would be joining 22 other EU Member States that already have one in place. In the remaining Member States – Austria, Denmark, Finland and Sweden – and in Norway, too, minimum wage rates are stipulated in sectoral collective agreements. This article reviews some examples of how EU countries set their minimum wages, why they opted for one or the other approach, and what impact their decision has had.

Spoiler alert: There is no one best-practice blueprint. Wage setting is deeply embedded in each country's economy and its institutional and industrial relations landscape, and outcomes do not – necessarily or exclusively – depend on what system is chosen.

Different strokes for different folks

Statutory minimum wages play different roles for the countries in the EU. For some – mainly the eastern European countries – they are essentially the only instrument for central social actors to influence wage setting in an otherwise fragmented company-level wage-setting environment. For other Member States, such as Belgium or Spain, they serve as an additional tool and establish a lowest floor, but they have relatively limited practical relevance given the higher levels of pay fixed within an extended set of sectoral collective agreements. With almost no exceptions, countries have favourability clauses that ensure that collective agreements cannot go below legal minima, so collective agreements and statutory minimum wages tend to be complementary to each other.

While by definition the legal minimum wage is brought into effect by law (or an equivalent regulation), the process for making or agreeing rate changes varies across the EU. Many countries have tripartite peak-level forums in which the government either consults the social partners on a set proposal, or in which it provides room for them to negotiate, and if no agreement is reached, it then unilaterally determines the level. In a few countries, there are bipartite or tripartite ad hoc negotiations or consultations with the social partners. Other countries have independent expert committees that research and monitor, consult a variety of stakeholders, and then make recommendations on rate increases. Additionally or alternatively, some countries have opted for fixed rules or formulas in which they link the statutory minimum wage to other wages or to economic developments. [1]

Cyprus and Italy contemplate their options

Cyprus and Italy are currently considering the introduction of a statutory wage floor. **Cyprus** has a set of statutory minima based on occupation. For instance, after six months of service, a monthly minimum wage rate of €924 applies to jobs including shop sales assistant, general office clerk and teachers' aide. These minima have been frozen since 2013. A decreasing number of other workers are covered by sectoral or company-level collective agreements, in parallel with an increasing number of workers who are not covered. In 2018, the newly inaugurated president announced his intention to introduce a universal wage floor, subject to the condition that the unemployment rate falls below 5%. The government has sought to obtain different proposals and is currently conducting a phased study. The social partners in Cyprus are divided over the issue, with the trade unions – in principle – being in favour, while the employers are against.

Italy currently sets minimum wages within sectoral collective agreements, which cover 80% of Italian workers. At the same time, it has been found that compliance with the collectively agreed minima is relatively low, particularly among smaller companies and in southern Italy. [2] With the Italian Jobs Act of 2015, the Renzi government introduced the possibility of setting a statutory minimum wage, a move criticised by both sides of industry. The issue was brought to the fore in 2018 when the new government parties Lega Nord and the Five Star Movement announced their intention to introduce an hourly statutory minimum wage for workers and sectors not covered by collective agreements. They proposed a law (No. 658) to the Senate's Labour Commission that stipulated a minimum gross hourly rate of €9 as a universal baseline or, if more favourable, the rate of the national sectoral collective agreements. A rate of €9 per hour would amount to around 80% of the median wage in Italy, according to calculations from the OECD, and thus be the most 'generous' level, in relative terms, across Europe.

Notes on the late adopters

Just three countries have in the past two decades made a major change to their wage-setting framework by introducing a legal minimum wage: the United Kingdom in 1999, Ireland in 2000 and Germany in 2015. In Germany, the move was motivated by the continuous decline in collective bargaining coverage, down to less than 60% on average and substantially less than that in some eastern German regions. This situation was similar to that of the United Kingdom in the 1990s, where the wage councils were abolished in 1993, and the earnings of the lowest-paid workers became decoupled from those of other workers, growing much less than average. In Ireland, the introduction was 'a social policy commitment to protect workers considered to be most vulnerable and at risk of exploitation and protect against poverty'. [3] Each of these 'newcomers' opted for an expert-based approach to adapting the rate, one that involves the social partners .

In **Germany**, the decision on the first rate of €8.50 per hour – passed in parliament with the support of the Social Democrats and the Green Party – was a political one and criticised by the social partners. However, the social partners have an important role in setting the rate, as the Mindestlohnkommission (Minimum Wage Commission) calculates increases based on average developments of collectively agreed wages. The commission makes its recommendation by balancing the appropriate protection of workers with ensuring a fair and functioning labour market for companies, while not harming employment. The introduction in 2015 was phased in, with exceptions for some sectors and groups of workers, to allow for a gradual adaptation and to prevent job loss. The evidence so far shows that the introduction does not seem to have harmed employment overall, but it did reduce the working hours of full-time minimum-wage workers, thus lowering their incomes.

Equally, in the **United Kingdom**, research commissioned by the Low Pay Commission (LPC) by and large shows no general negative employment effects. The minimum wage has also resulted in better pay increases for the lowest paid than anyone else, and about 30% of workers have benefited directly or indirectly from it. Another question the UK actors have pondered are the great regional differences in purchasing power: for instance, London is a much more expensive place in which to live than rural regions in Wales, and a one-size-fits-all minimum rate is difficult to set. This has triggered a living-wage campaign, run by the Living Wage Foundation. This organisation calculates a living wage rate based on the minimum wage needed to cover the essentials of life for a family in London and the rest of the United Kingdom.

Companies sign up to paying this wage on a voluntary basis. Meanwhile, the UK government in 2016 set a target for the LPC: to increase the minimum wage –now called the 'national living wage' – towards 60% of the median wage by 2020. The LPC monitors progress on this and its impact very closely.

Another question currently in focus in the United Kingdom is that of non-compliance. Even though it is hard to measure and estimate, recent research shows that it is not negligible, with about 23% of workers who are entitled to the minimum wage receiving less than it.

Some continue without

In those other countries without a statutory minimum wage, various actors have regularly revisited the idea of introducing one. But these debates have usually been short lived.

In **Austria**, due to compulsory company membership of the Federal Economic Chamber (WKO), nearly all employees are covered by collective agreements, and the rates set by these agreements remain very low. In 2017, the then Chancellor Christian Kern urged the social partners to set a minimum wage of at least €1,500 per month in their collective agreements, or the government would consider introducing a statutory minimum wage. Despite some political support for the suggestion, the majority of industry stakeholders and political parties were in favour of maintaining the existing system. In response, the peak social partner organisations commissioned their members and trade unions to develop a roadmap for introducing a minimum wage of €1,500 for all employee groups by the end of 2019, in order to avoid a unilateral legislative initiative on the issue.

The Scandinavian Member States – **Denmark**, **Finland** and **Sweden** – also function without a statutory minimum wage but manage levels through a large number of well-coordinated sectoral collective agreements. Further negotiations may take place at local company level on wages and working conditions, and overall wage levels are relatively high. All attempts to initiate a debate on the introduction of a legal floor have been met with resistance, particularly from the trade union side. Collective bargaining coverage continues to be high, as in Italy, through extension. Whether and to what extent those workers who are not covered by collective agreements are also low-wage earners is not really known – a bit surprising for countries with a usually extraordinary research evidence base. But there is ground to believe that the numbers of non-covered and low-paid workers are not large, as companies who do not participate in collective bargaining nevertheless orient their practices around collective agreements. In addition, in **Denmark**, trade unions have the legal right to demand that companies negotiate or apply collective agreements should they be found to underpay workers. Recent cases where underpayment was detected and the offenders brought to court largely concerned foreign companies in the construction sector.

Norway is another interesting case, as it has – in comparison to the other countries without a statutory minimum wage – comparatively low collective bargaining coverage: 'only' around 70%, although this varies substantially by sector. It also differs in that the employer organisations in the voiced more enthusiasm for the introduction of a statutory minimum wage. They saw it as a means to re-establish a level playing field in the context of rising competition from companies employing foreign workers at lower pay rates. The Norwegian answer was to extend sectoral agreements to all companies in sectors where underpayment was most widespread, including, for instance, construction, cleaning and fish-processing. This seems to have paid off: a recent study by Trygstad et al found that the share of cleaners receiving less than the collectively agreed minimum rate dropped from 31% to 9% after the first year of the extension, and to 5% five years later. [4]

Why introduce a legal minimum wage?

Research by Kampelmann et al (2013) covering 18 countries between 2007 and 2009 showed that the combination of sectorally agreed minima with high collective bargaining coverage is a functional equivalent to statutory minimum wages and that there is no evidence that one is superior to the other. [5] Higher collective bargaining coverage and a national minimum wage both tend to be associated with lower wage inequalities. Statutory minimum wages were found to cover workers more effectively than sectoral minima, but higher bargaining coverage can partially offset this. Eurofound (2014) also found that countries with a higher bargaining coverage tend to have a lower fraction of workers paid below prevailing minima. [6]

As with every instrument, policymakers should fully explain the motives behind a statutory minimum wage and assess whether there are other plausible pathways to achieving the same objectives. Where a large and increasing number of employees are underpaid relative to national standards, ensuring that every worker can earn a decent living could be one such motive. But the cause of underpayment should be established in the first place.

If it is due to low or falling bargaining coverage, a legal minimum wage could, in theory, ensure that a universal wage floor is set. This would ensure that all workers, including those not covered by any collectively agreed rates, have the right to receive a decent minimum level. If the underpayment is due to low compliance with rates set in collective agreements, however, the question is whether a legal minimum rate will be met with a greater degree of compliance and whether enforcement will improve. National authorities may, as another option, decide to enforce compliance with collectively agreed minima.

The rates within collective agreements or the market may be ‘too low’ for workers to ensure an adequate standard of living because companies are either unable or unwilling to pay to pay higher wages. Only in the latter case would a legal minimum be a remedy. Companies or sectors that cannot pay higher wages will sooner or later – all other things being equal – go out of business or decline. An alternative answer, however, could be that companies faced with higher wage demands start to innovate and improve their productivity. This is one aspect of the ‘Swedish model’, which is based on just such a high wages–high productivity path. It does require good instruments, however, to effect the transition of workers (and companies) to higher productivity.

Setting the level of the envisaged – countrywide or regionally differentiated – minimum wage rate puts a great responsibility on the shoulders of those actors entrusted with ‘getting it right’. Wage levels in general have to reflect the productivity of workers and companies and should ensure a decent standard of living.

Traditional and basic economic theory suggests that a level set too high will reduce employment (in terms of volumes of labour demanded – that is, working time). It may also trigger non-compliance and shift labour – at least partially – into undeclared work, with negative consequences for taxes and social security contributions. Empirical research over the decades has detected only limited impacts on employment on average and smaller negative employment effects for groups of workers with lower productivity.

What will happen to the rates set within collective agreements? Will collective bargaining partners in lower-paid and less productive sectors orient themselves towards – lower or higher – minimum standards, or will minimum wage increases boost the rates set in agreements?

High-level support for EU threshold

These are questions that only the Cypriot and Italian actors can answer for their countries. From the EU perspective, wage setting remains a competence of the Member States, although the European Pillar of Social Rights in Article 6 states the right of workers to an adequate wage. At the same time, there has been strong support for an EU minimum wage level, and the new Commission President Ursula von der Leyen, setting out her agenda for the next five years, has committed to proposing 'a legal instrument to ensure that every worker in our Union has a fair minimum wage'.[7] She will undoubtedly have the support of other EU leaders: French President Emmanuel Macron sees an EU minimum wage threshold as a means of reducing minimum-wage-related emigration,[8] while European Commission Vice-President Franz Timmermanns argued that it would reduce the growing wealth gap.[9] German Chancellor Angela Merkel has advocated 'comparable' minimum wages in the EU that reflect the different living standards and ensure similar working conditions.[10]

Any move to introduce a binding minimum wage at either national or EU level must be guided by three criteria: a good evidence base regarding the impact of changes to the minimum wages, next to a meaningful involvement of the social partners, within a process that is transparent and predictable.

References

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