Pay progression for low-paid workers

Research Paper 1: The role of tax and wage regulation

James Kirkup
Scott Corfe
Kathryn Petrie
Nicole Gicheva

Social Market Foundation

FIRST PUBLISHED BY

The Social Market Foundation, June 2019
11 Tufton Street, London SW1P 3QB

ISBN: 978-1-910683-68-2

THE SOCIAL MARKET FOUNDATION

The Foundation's main activity is to commission and publish original papers by independent academic and other experts on key topics in the economic and social fields, with a view to stimulating public discussion on the performance of markets and the social framework within which they operate. The Foundation is a registered charity and a company limited by guarantee. It is independent of any political party or group and is funded predominantly through sponsorship of research and public policy debates. The views expressed in this publication are those of the author, and these do not necessarily reflect the views of the sponsors or the Social Market Foundation.

KINDLY SUPPORTED BY

This report was funded by the Joseph Rowntree Foundation.

JRF JOSEPH ROWNTREE FOUNDATION

CONTENTS

Acknowledgements

The SMF is grateful to the Joseph Rowntree Foundation for sponsoring this report. The views in the report do not necessarily reflect those of the Joseph Rowntree Foundation. The Social Market Foundation retains full editorial independence with respect to its research.

The authors are grateful to all those who participated in the two roundtable discussions held as part of the work. The authors would like to thank Salima Ali for her input during the project.

About the Social Market Foundation

The Foundation's main activity is to commission and publish original papers by independent academic and other experts on key topics in the economic and social fields, with a view to stimulating public discussion on the performance of markets and the social framework within which they operate. The Foundation is a registered charity and a company limited by guarantee. It is independent of any political party or group and is funded predominantly through sponsorship of research and public policy debates. The views expressed in this publication are those of the author, and these do not necessarily reflect the views of the sponsors or the Social Market Foundation.

About the authors

James Kirkup

James Kirkup is the director at the SMF, was born and raised in Northumberland, where he attended a comprehensive school. The first member of his family to go to university, he studied politics at Edinburgh University and began his career in journalism at The Scotsman in 1997. He later covered European politics and economics for Bloomberg News, moving to Westminster in 2001. He returned to The Scotsman as Political Editor and columnist before joining the Telegraph in 2007. He was Political Editor of the Telegraph and then Executive Editor – Politics, overseeing and writing commentary and analysis on politics, policy and economics.

Scott Corfe

Scott Corfe joined the SMF as Chief Economist in 2017. Before joining, he was Head of Macroeconomics and a Director at the economics consultancy Cebr, where he led much of the consultancy's thought leadership and public policy research. His expert insights are frequently sought after in publications including the Financial Times, the Sunday Times, the Guardian and the Daily Telegraph. Scott has appeared on BBC News, Sky News, Radio 4 and a range of other broadcast media.

Scott was voted one of the top three forecasters of UK GDP by Focus Economics in 2016.

Kathryn Petrie

Kathryn is a senior economist at the SMF. She has worked on several policy areas since joining the SMF including education, social care and financial services.

Prior to joining the SMF Kathryn worked at the National Employment Savings Trust (NEST) as a Strategy Analyst. She has a BSc in Economics from Brunel University and an MSc in Economics from the University of East Anglia.

Nicole Gicheva

Nicole is a Researcher at the SMF. She has worked in a range of fields including education, savings policy, and competition.

Prior to her appointment, Nicole worked as a research assistant at the Department of Economics at Royal Holloway, University of London while studying for her MSc in Economics. She also holds a BSc (Hons) in Economics.

EXECUTIVE SUMMARY

This research report seeks to understand whether and how government can use tax and regulation policy to promote wage progression and career progression among low-paid workers.

The problem of progression out of low pay

Experiences in the labour market are at the heart of the political and policy debate about the modern economy. There is a growing sense that work is no longer providing a reliable route to better living standards and social mobility. A key part of the social contract – that "work should pay" – is being broken. Without reform, there is likely to be growing anger about the UK's economic model.

Successive governments have done much to increase the wage floor over the last 20 years, and the Low Pay Commission is near to fulfilling its target of reaching 60% of median earnings. Despite these achievements, the UK still has a very significant low pay problem. About a fifth of employees earn less than two thirds of the median hourly wage, contributing to high levels of in-work poverty.

Not only are many on low pay, but many remain stuck on low pay for considerable periods of time, with only a sixth of low-paid workers in 2006 managed to consistently escape low pay by 2016.

Even if the wage floor in the UK eventually rises to two thirds of median hourly wages, as has been suggested by the current Chancellor of the Exchequer Philip Hammond, an ongoing concern in the UK economy is likely to be individuals not progressing up the income distribution. It is crucial, in our view, that policymakers ensure that individuals do not remain stuck at the prevailing wage floor – and use the tools at their disposal to provide additional wage and career progression opportunities.

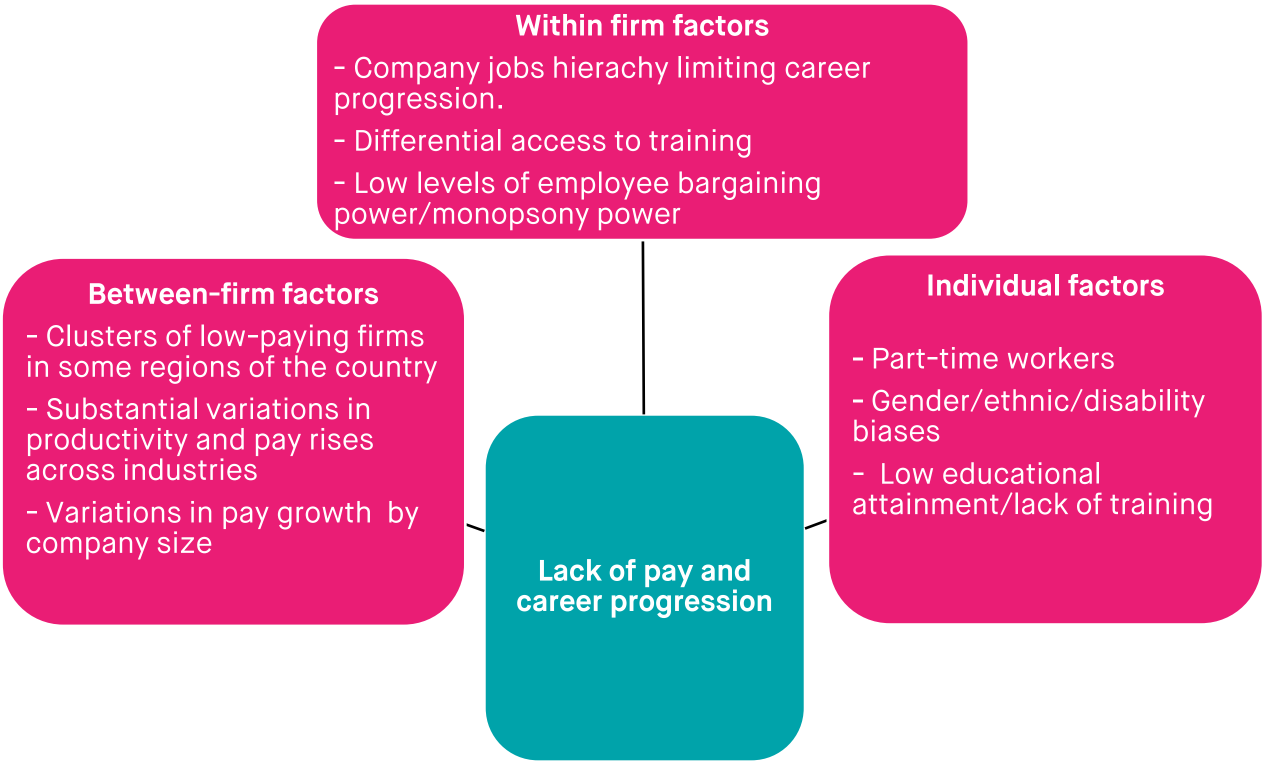
Focus of this report

Our research concerns itself with two routes to higher living standards for workers – **wage progression** and **career progression.**

- By "wage progression", we mean pay rises among workers in a given job position. We focus here, in particular, on wage rises beyond increases driven by changes to the basic minimum wage floor.
- By "career progression", we mean pay rises achieved through a change in job position – whether that be a promotion within a company or by shifting to an employer offering better-paid job positions.

The factors that affect progression out of low pay

Chapter 2 discusses in depth the factors that drive limited pay and career progression among lower earners in the UK, and identifies three overarching categories:



Informed by this analysis, the remaining Chapters consider what can be done through tax and regulation policy to address some of these factors and promote wage progression and career progression.

This report is the first of two on wage and career progression. While this report focuses on tax and regulatory measures to promote progression, the second report will explore the role of corporate decision-making and softer measures such as guidance and social norms.

Wage regulation

Chapter 3 considers whether wage regulation could be used to *require* wage progression, with higher earnings for workers who are more experienced, older or have served more time. It concludes that any such policies would be accompanied by major disadvantages, including additional rigidity and inefficiencies in the labour market, potential perverse incentives (such as for workers to remain with their current employer), and additional complexities which are likely to make compliance harder for firms and enforcement harder for government. The report also reveals that specific age-related minimum wages for young workers are not used as reference wages.

For this reason, the report argues that additional age-related or tenure-related minimum wages are not, on balance, advisable.

However, the report argues that softer measures, which seek to offer guides to firms about wage and career progression, or which put pressure on firms by making public their record on wage progression for the low-paid could be beneficial. This is something the SMF will discuss in more detail in a second report.

Profit-sharing

Profit-related pay (PRP), whereby firms distribute part of their profits directly to workers, could offer an important political message that the economy is there to serve the interest of workers as much as owners.

Beyond this, evidence indicates that profit-sharing can – if designed well – help improve productivity. As it stands, only one in three employers offer PRP and the overwhelming majority of these (84%) offer it only to managers. Our analysis shows that a large number of (though not all) employers of lower-paid workers are profitable, suggesting that a widespread PRP scheme could affect a large number of low-paid workers.

Our analysis concludes that **the Government should explore incentivising PRP to help increase the wages of low-paid workers**, although it would not have any impact on their occupational progression. It is important to ensure that PRP is rolled out in a way that does not result in lower base rates of pay for employees.

Drawing on analysis of international examples and previous schemes, the report recommends how any PRP policy should be designed. These include: promoting PRP to all workers not just managers and ensuring that bonuses are distributed relatively evenly across the workforce; directing incentives – such as tax reliefs – at the employer rather than the individual; and, classifying PRP payments as separate from wages for the purposes of minimum wage compliance and for Universal Credit assessments.

Using tax incentives to promote wage and career progression

Chapter 5 analyses whether business taxes could be effective instruments with which to incentivise employers of low wage workers to increase their wages and provide career progression, and considers what activities by firms should be encouraged.

First, it discusses the effectiveness of tax incentives as policy instruments more widely, and points to Japan where a landmark tax relief policy has recently been introduced to incentivise wage rises for workers.

The report assesses three major UK business taxes: Corporation Tax, Business Rates and Employer National Insurance contributions. It concludes that no single tax on its own would incentivise all employers of low wage workers to offer higher wages to all low-paid workers. However, a relief on corporation tax (on profits) is likely to have reasonably good coverage across low-paid workers and would be the best candidate for a government pilot scheme. **Tax reliefs could be made conditional on employers achieving a pre-determined percentage increase in wages for low-paid staff, at the bottom end of the income distribution, not directly affected by the minimum wage floor**.

Our analysis then turns to training. Training is widely accepted as a path to higher wages and to career progression. However, those on lower wages are less likely to be offered training and to take up training. Outside of the Government's flagship apprenticeship scheme, existing policies and allowances appear to be insufficient to encourage employers to provide training to low-paid workers.

A range of countries use tax incentives to increase the training of workers, often with a particular focus on SMEs. Evidence from the UK and elsewhere demonstrates that training-based policies can be effective but that there are risks about deadweight costs. The latter may be minimised if low wage workers are specifically targeted because we know already that little training takes place.

We propose that behavioural trials are undertaken to assess which form of tax incentives would be most likely to achieve an increase in training opportunities for low-paid workers.

Finally, we consider an important geographic dimension to low pay progression that often gets overlooked: namely that opportunities for low-paid workers to progress their earnings and their careers may be particularly limited in some localities where the labour market is dominated by sectors that offer low-paid work and typically weak wage and career progression opportunities. An example of this is many coastal communities, where employment is concentrated in low paying industries such as retail, hospitality and care.

Introducing into the locality a wider range of better paid jobs could offer opportunities for both wage increases (by individuals moving to better paid jobs in other sectors) and career progression (by individuals moving into sectors that on average have better occupational mobility).

The report discusses the **concept of 'Economic Growth Areas', which could be piloted by local authorities, city governments or national government**. These would offer tax incentives to firms in higher paying sectors to relocate or start a business in an area where there is poor industry mix and where the economy is dominated by low paying sectors.

It may be beneficial to complement any such policies with additional training opportunities and advice opportunities for low-paid workers in these localities – to ensure they benefit from progression opportunities arising from firms relocating to an area.

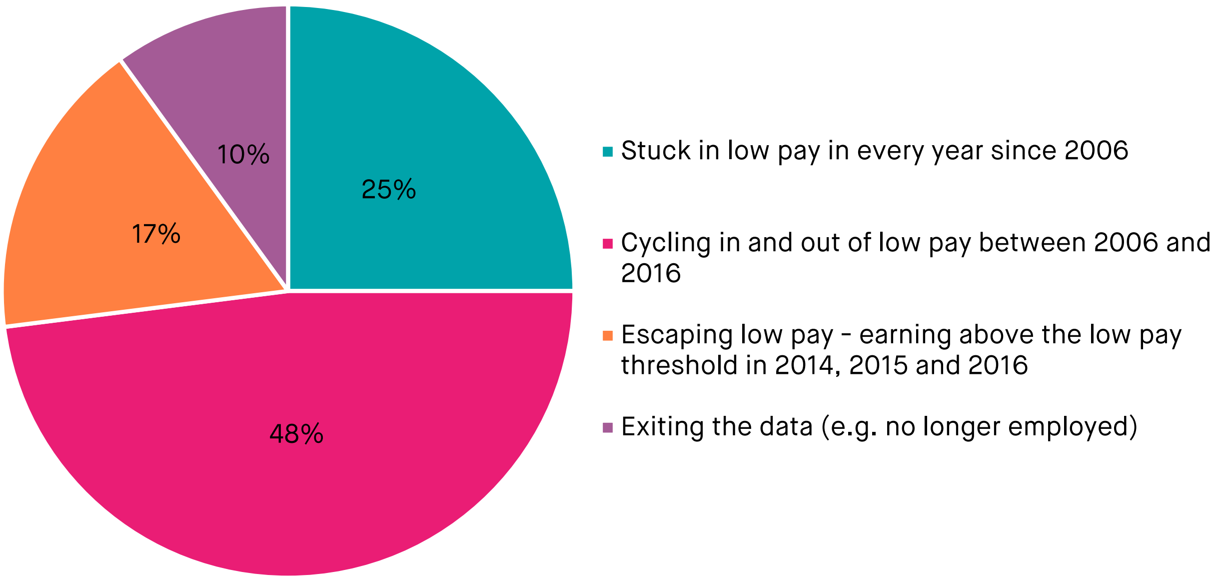
CHAPTER 1: INTRODUCTION

Experiences in the labour market are at the heart of the political and policy debate about the modern economy. There is a growing sense that work is no longer providing a reliable route to better living standards and social mobility. A key part of the social contract – that "work should pay" – is being broken. Without reform, there is likely to be growing anger about the UK's economic model.

In particular, the UK economy has a problem with low pay. Research by the Joseph Rowntree Foundation showed that eight million working age adults and their children who live below the poverty line live in a household where someone is in work.[1] About a fifth of employees (close to 5 million people) earn less than two thirds of the median hourly wage.[2]

Critically, evidence suggests that many of these workers remain trapped in low pay, rather than progressing onto higher earnings over time. A 2017 report by the Resolution Foundation found that just one in six (17%) of low-paid workers in 2006 managed to consistently escape low pay by 2016.[3] About half (48%) cycled in and out of low pay over this ten-year period while a quarter (25%) were stuck in low pay in every year between 2006 and 2016.

Figure 1: Situation of those who were low-paid in 2006, in 2016



Source: Resolution Foundation (2017), "The Great Escape? Low pay and progression in the UK's labour market". Low-paid defined as earning less than two thirds the median hourly wage.

Successive governments have done much to increase the wage floor over the last 20 years. From 1 April 2019, the National Living Wage was set at £8.21. Fears that a minimum wage would be accompanied by significant unemployment have not materialised.[4] The Low Pay Commission is near to fulfilling its target of reaching 60% of median earnings and the current Chancellor of the Exchequer, Philip Hammond, is exploring the case for increasing the living wage to 66% of median earnings.[5]

While increases in the National Minimum Wage and National Living Wage can increase the pay *floor* in the UK, they are only part of the solution to reducing poverty and boosting the household incomes of those at the lower end of the income distribution. Given that many individuals remain stuck at the lower end of the wage distribution, more attention needs to be given to measures which improve pay and career progression for those on relatively low incomes. Such measures have, in our view, been overlooked in much of the policy debate about low pay in the UK. This report explores, in detail, the role that such measures could play in boosting living standards going forward.

The focus of this report

Our research concerns itself with two routes to higher living standards for workers – **wage progression** and **career progression.**

- By "wage progression", we mean pay rises for a worker *within* a given job position. We focus here, in particular, on wage rises beyond increases driven by changes to the basic minimum wage floor.
- By "career progression", we mean pay rises achieved through a change in job position – whether that be a promotion within a company or by shifting to an employer offering better-paid job positions.

As discussed later in the report, in some parts of the economy it may be very difficult for policymakers to achieve career progression, and increases to wages (accompanied by improvements in productivity if higher wages are to be sustainable) may be a more realistic goal.

Specifically, in this report we also focus on the role of **tax policy** and **regulation** in improving wage and career progression. Such measures can incentivise or require action. Further, there is scope for these measures to adjust social norms and increase pressure on businesses to improve pay and career progression for lower earners. These measures can also send signals to employers and to society about political priorities.

Furthermore, given that much of the UK's "low pay growth problem" can be attributed to the economy's "low productivity growth problem",[6] there is a case for exploring the role that tax incentives can play in encouraging firms to be more productive. There is a clear link between employee pay and productivity in the economy, which needs to be reflected in policy. Ultimately, pay rises and progression may not be sustainable if they are not accompanied by increases in company productivity.

We also note a growing international interest in the use of tax and regulatory tools to improve wage growth in the economy. Japan, for example, is experimenting with corporate tax incentives to encourage stronger rates of employee pay growth. The corporate tax cuts announced by the Trump administration in the US have been pitched as a boon to workers, with the administration arguing that they will translate into higher employee wages[7] We explore some of the emerging international evidence on the effectiveness of tax incentives in boosting wage growth in the economy.

By limiting the study to these policy measures, we are not implying that other policies are unimportant. Policies set out in this report are by no means comprehensive solutions to the problems of low pay and poverty in the UK. As has been mentioned by others, welfare policies (such as tax credits) and measures aimed at boosting employee incomes (such as what we set out here) should be seen as complements, not substitutes.[8] Ultimately, a mix of welfare and wage policies is required to effectively tackle poverty. Improving employee collective bargaining power through, for example, trade unions, also has a role to play in supporting living standards.

However, given the prevailing political rhetoric about welfare restraint – at least within the Conservative Party – tax and regulatory measures aimed at improving living standards might be more feasible than significant welfare reform in the short-run. Further, high pay and progression can reduce welfare expenditure by reducing the need for it – providing a further political incentive to investigate policies which improve pay and career progression.

We note also significant complementary activities that are already taking place or have been proposed which focus on alternative industrial policy interventions such as human resources practices, access to finance (to facilitate productivity-enhancing investment) and major training programmes (such as apprenticeships) to name but a few.

The structure of this report is as follows:

- *Chapter 2* discusses the underlying drivers of the lack of pay and career progression among lower earners in the UK;
- *Chapter 3* explores the role that wage regulation policy could play in improving pay and career progression;
- *Chapter 4* examines the role of profit related pay (PRP) schemes in improving pay progression for lower earners;
- *Chapter 5* evaluates the role that tax incentives – at a regional and national level – can play in improving pay and career progression.

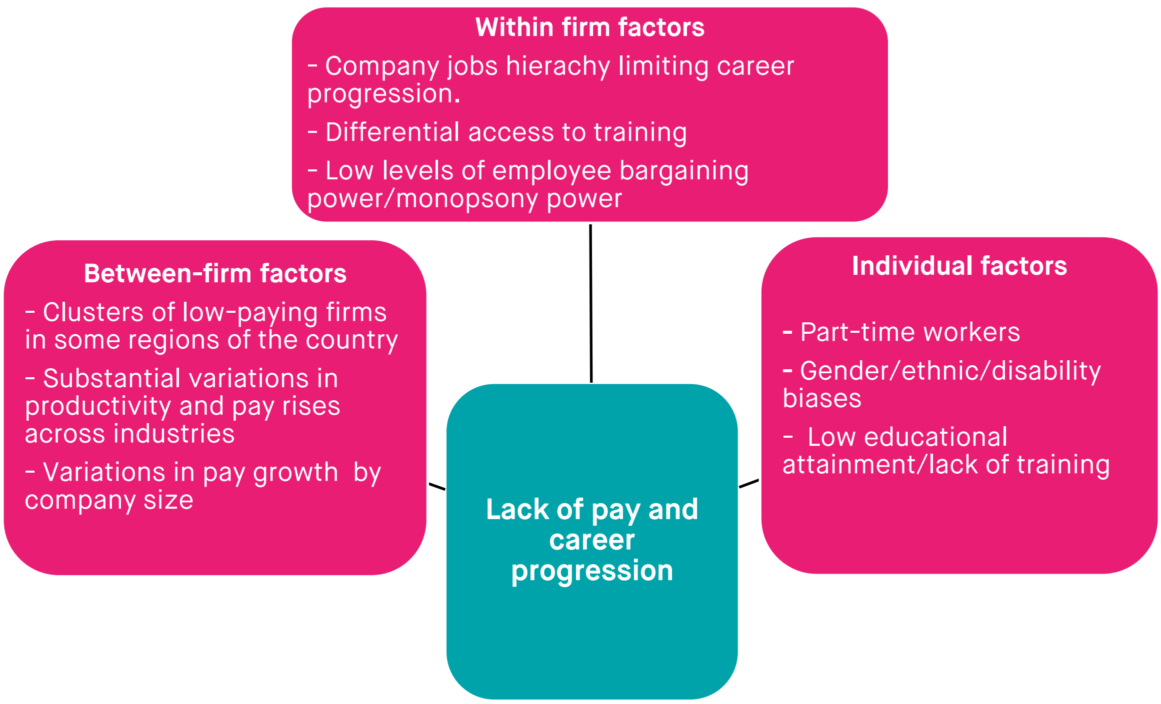
CHAPTER 2: WHAT DRIVES VARIATIONS IN PAY AND CAREER PROGRESSION?

This Chapter seeks to build a deeper understanding of drivers of differences in pay levels and progression across the economy as background to the policy analysis which is developed in subsequent chapters. Our analysis predominantly draws on existing published evidence from the UK and other comparable countries, though we also supplement this with new evidence.

One way of thinking about these drivers is to place them into three categories:

1. **Within-firm factors** - drivers which lead to variations in pay progression for employees *within a given company.* For example, pay progression might be more limited among lower earners than among higher earners, or vice versa, due to differences in wage bargaining power between employees working in the same company.
2. **Between-firm factors** - drivers which lead to variations in pay progression *between companies.* For example, pay progression might vary across companies depending on their size and the industries in which they operate, or indeed between similar firms in the same industry.
3. **Individual characteristics –** characteristics of an individual which limit their ability to achieve pay rises and pay progression. For example, those that must work part-time, due to the need to care for relatives, and those lacking the qualifications needed to access better-paid work.

As we discuss in subsequent sections of the report, each of these three types of pay and career-limiting drivers is likely to require different policy interventions to address them. This chapter explores these three categories – how they might manifest and the extent to which academic evidence and data provide insights into their prevalence and contribution to the lack of pay and career progression among lower- earners.



Within-firm factors

Academic evidence and data suggest that there is significant variation in pay and career progression *within companies*, with lower-paid employees often lacking the wage bargaining power of higher-paid, more senior workers.[9] Company pay-setting processes – such as the use of benchmarking by remuneration committees in setting senior executive pay – might also lead to situations where earnings growth is generally greater among higher earners within a company.

Intuitively, we might expect employee bargaining power to be lower towards the bottom end of the pay scale for several reasons. First, if jobs are lower-paid because the skills required to perform these roles are in abundance, then wage bargaining power is likely to be constrained by the relative ease with which employers can find suitable workers who are willing to work for lower rates of pay. In higher-paid roles demanding more niche skillsets, wage bargaining power is enhanced as employees are aware of the difficulties that employers would face in finding cheaper, alternative workers. This gives employees more leverage to demand higher rates of pay.

Second, limited financial buffers – such as savings – may also curtail the wage bargaining power of lower-paid workers, if demands for higher wages and career progression are perceived as risking job security ("they might fire me if I ask for more pay"). In addition to having reduced bargaining power in the setting of wages, lower-paid workers may also lack the bargaining power needed to request other benefits of employment – such as learning and training opportunities, access to qualifications and flexible working hours.

Widening pay gaps over time

Divergences in wage bargaining power within a company, as described above, can lead to widening pay disparities over time. This raises questions around the extent to which lower-paid workers are able to share in the proceeds of company growth, and benefit from pay progression as company performance improves over time.

One of the most widely-discussed metrics of within-firm wage variation is the ratio of CEO pay to average employee pay. This ratio has increased substantially in recent decades, with the average FTSE 100 CEO now earning over 100 times more than their average employee, up from less than 50 times in 1998.[10] Arguably, this trend is indicative of high levels of wage bargaining power at the upper end of the salary scale, which allows CEOs to achieve pay rises in excess of that justified by their performance. It might also be indicative of relatively weak wage bargaining power further down the pay scale.

The widening divide between senior executive and average worker pay is in part driven by the nature of the pay-setting process for executives. Of particular concern is the extent to which remuneration committees have effectively created a ratchet effect, where executive pay consistently rises more rapidly than that seen for other workers. One key way that such a ratchet effect is created is through the benchmarking of CEO pay. Many remuneration committees set pay by drawing up a group of comparable companies and using this as a basis for setting the pay and reward-based bonuses of senior executives. A key issue is that many remuneration committees seek to pay above median or upper quartile rates of pay, compared with their benchmark groups, as a way of attracting talent. If many remuneration committees adopt this mindset, then pay starts to ratchet up regardless of company performance.

Differences in the wage-setting process across company job hierarchies are likely to lead to significant differences in wage progression over time, regardless of an individual's performance or relative skill level. For example, if senior executive pay is set using benchmarking, as described above, but the same is not true of "average" workers in a company, then pay gaps will tend to widen over time.

Company hierarchies and career progression

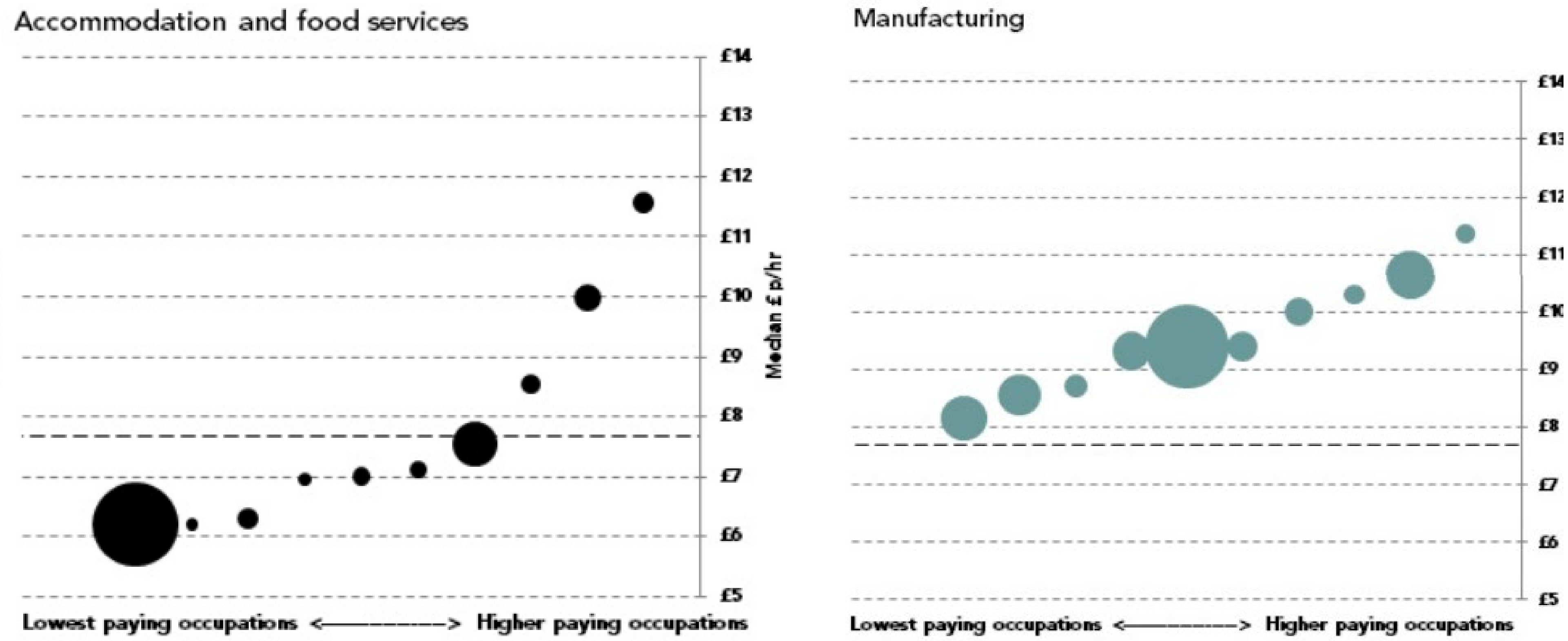
Job hierarchies within companies can have an impact on the ability of lower-paid individuals to realise pay and career progression. Companies with more even spreads of jobs across the pay scale are more likely to provide opportunities for pay and career progression within a company. In contrast, companies with many low-paid employees, a small number of high-paid executives and a limited number of "middling" job roles are likely to offer much more restricted career progression opportunities, given the difficulties of leapfrogging from a low-paid to an executive job position in one go.

Research by the Resolution Foundation for the Social Mobility Commission suggests that "career constraining" job hierarchies are particularly prevalent in sectors such as accommodation & food services, where job roles are concentrated towards the lower end of the pay scale. This contrasts with sectors such as manufacturing, where employment is spread more evenly across the pay scale, suggesting more opportunities for within-company career progression.[11] The nature of company hierarchies has implications for the extent to which career progression – in the sense of promotion – is likely to be achieved for lower-paid workers. In sectors such as retail, with a relatively high number of low-paid jobs, policy might be better focused on lifting the wages of workers within a given role, rather than improving their prospects of promotion – given the inherent difficulties of imposing career hierarchies on a company. It may be possible to improve the productivity of the worker and their pay without the individual formally progressing up the career ladder, for instance through the wider application of technology.

Although company hierarchies might be a function of the industry in which a company operates, evidence also suggests that there is variation between firms within a given sector. Research by IPPR, for example, found that the number of middle skill occupations within a given industry varies across countries. For example, they found that, in the UK and France, mid-skilled work accounted for 45% of employment in the manufacturing and utilities sector, compared with 57% in Belgium and 63% in Spain. Belgium was found to contain more mid-skilled positions than France, Spain or the UK, whilst the UK had slightly higher proportions of high-skilled occupations.[12] These differences are likely to reflect a wide range of structural and policy factors such as: human resource practices, levels of unionisation, the sub-sector composition of these industries, historical factors and the business models of the firms that operate in those sectors.

Career progression within a company might also be determined by whether lower earners can access training. If training opportunities are limited, it might be difficult for employees to transition up the jobs hierarchy. If lower paid workers lack bargaining power relative to higher earners, they may be less able to bargain effectively for access to training.

Figure 2: Occupational ladders within sectors (2013)



Source: Resolution Foundation, Social Mobility Commission

Are employees wage-takers or wage-setters?

There is a growing academic literature, especially in the United States, which examines the extent to which employees are wage-setters or wage-takers in the economy. If employees tend to be wage-takers, rather than wage-setters, then their ability to achieve pay rises and promotion is likely to be more limited. They might also be less likely to access things that increase their ability to realise a promotion – such as training and development opportunities.

A key issue here is the extent to which firms have *monopsony* power when it comes to hiring employees, which makes them wage-setters rather than wage-takers. Much as a monopoly (oligopoly) has substantial market power when it comes to *selling* goods and services, a monopsony (oligopsony) has substantial market power when in comes to *buying* goods and services such as labour and raw materials. A monopsony or oligopsony can use its/their market power to force down wages and other costs.

A recent paper by Abel, Tenreyro and Thwaites (2018), from the Bank of England and London School of Economics, found that higher levels of labour market concentration (where a small number of employers account for a relatively high share of jobs in an area) are generally associated with lower pay among workers in the UK.[13] An exception to this was where employees were covered by collective bargaining agreement; where such agreements exist, the association between labour market concentration and pay was found to be greatly reduced or in most cases to have disappeared completely. Intuitively, this makes sense, as collective bargaining power counteracts the wage-setting power of monopsonies/oligopsonies. This suggests that collective bargaining and trade unions have an important role to play in improving labour market outcomes for lower-paid workers – though we do not focus on these issues in this report, which focuses on tax and regulatory policies.

In their research, Abel, Tenreyro and Thwaits also found that the link between productivity and wage levels is weaker when labour markets are more concentrated. That is to say, under monopsony situations, workers are less likely to share in the proceeds of company growth and performance improvements. This can lead to widening within-firm variations in pay progression - for example, with CEO and senior executive incomes growing more strongly that than that seen lower down the pay scale.

The research of the UK economy matches findings from the US on the impact of monopsony power on labour market outcomes. Benmelech, Bergman and Kim (2018) found that wages tend to be lower in highly concentrated labour markets in the US, and that the connection between wages and employer concentration has increased over time, potentially due to the decline of trade unionism and collective bargaining.[14]

In a 2018 speech,[15] Alan Krueger argued that other factors, beyond the decline of collective bargaining, might be increasing monopsony power in labour markets and eroding employee wage bargaining power – leading to a growing slice of the economic pie going to employers rather than employees. This includes:

1. A growing reliance on temporary help agencies, staffing firms and outsourcing in the US. One implication of this practice is that firms can wage discriminate (pay employees different rates for performing the same or very similar roles), which facilitates the exercise of monopsony power. If a hospital has persistent vacancies for nursing positions, for example, it can reach out to a staffing firm that pays its nurses a higher salary to supply

additional nurses without having to raise its wage scale for incumbent nurses. Variation in the use of outsourcing across pay scales within a company can in turn lead to differences in within-firm pay progression.

2. In the USA, increased use of non-compete restrictions in job contracts might be reducing employee wage bargaining power, by narrowing worker options and reducing their ability to migrate to different roles. Just over one in five workers in the US who earn less than the median wage are bound by a non-compete restriction on their current or previous job.[16] This problem may be less prevalent among low wage workers in the UK, although the evidence base is incomplete.
3. Growing collusion among firms in the setting of employee wages. Krueger argued that collusion does not have to be explicit; it could take place because a certain wage, such as the National Minimum Wage and National Living Wage in the UK, becomes a focal point from which employers are reluctant to deviate, especially if employee bargaining power is relatively low. Natalya Shelkova (2014) provides evidence that the large and persistent spike in the wage distribution at the minimum wage is consistent with focal point collusion.[17] If the minimum wage serves as a focal point for the setting of pay, then in monopsony/oligopsony situations where employees are wage-takers rather than wage-setters, this can lead to workers being underpaid relative to their productivity.
4. More generally, Krueger notes, tacit collusion in wage-setting could come about because employers and workers were shocked by the depth of the recent global financial crisis, making workers fearful of bargaining for higher wages and employers disinclined to offer higher wages despite worker shortages, because they grew accustomed to having a queue of well-qualified applicants during the recession and for a long period afterwards.

Conceivably, each of these factors may play a role in increasing monopsony power in the UK, and curbing pay progression for those on lower incomes.

While the current *level* of monopsony power in the UK labour market might be a cause of concern, evidence suggests that monopsony power might be decreasing rather than increasing – raising questions, for further research, around the extent to which it accounts for variations in pay growth in recent years. Research by the Resolution Foundation found that labour market concentration – measured by the extent to which large firms account for total employment – has declined since the early 2000s.[18] Having said that, it is possible that monopsony power held steady or decreased despite declining labour market concentration – for example, if firms engaged in (tacit or explicit) collusion.

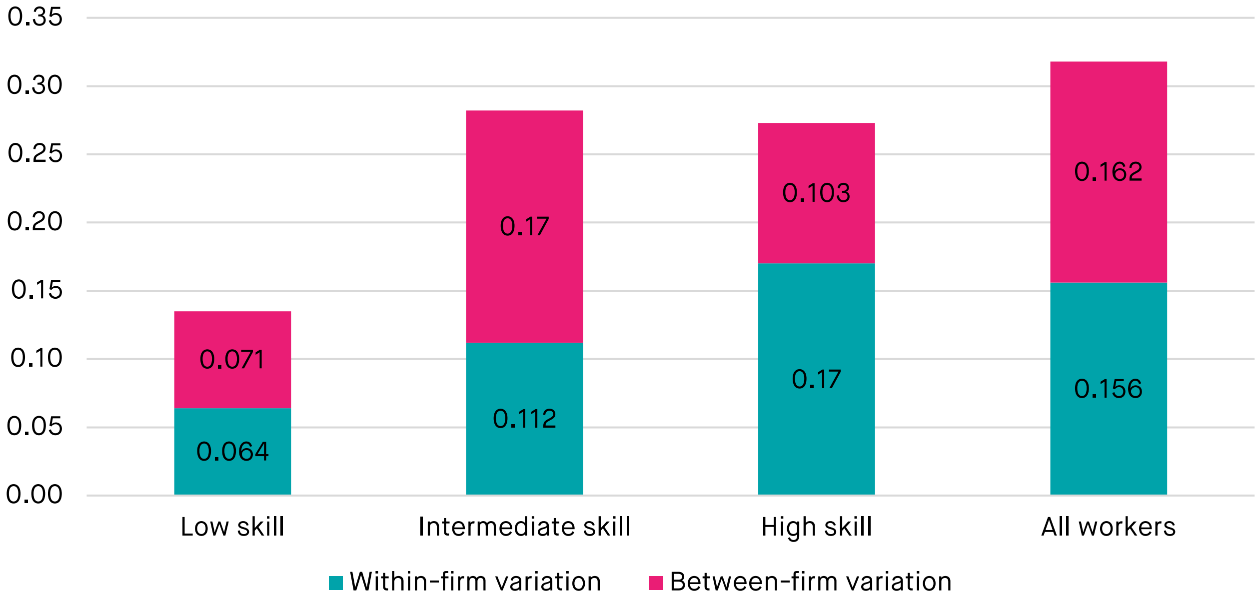
To what extent are within-firm factors driving variations in pay and career progression?

As we have discussed, there is evidence to suggest that company hierarchy, and monopsony power, can play a role in generating differences in pay and career progression within companies. The rise in CEO-to-worker pay ratios in recent decades might be indicative of substantial differences in wage bargaining power within companies, leading to a widening pay gap between those at the top and bottom ends of the pay scale.

Having said that, evidence suggests that within-firm factors are only part of the increase in inequality seen in recent decades. In a US-based study, Song et al (2016) found that over two thirds of the increase in earnings inequality from 1981 to 2013 can be accounted for by the rising variance of earnings *between* firms and only one-third by the rising variance *within* firms.[19] In a UK-based study, Aghion et al (2017) found that, for those on low and intermediate skill levels, the majority of wage variation is explained by between-firm differences rather than within-firm differences.[20] This is not the case for high skill workers, in part because such workers tend to be clustered together within high-performing firms. Notably, Aghion et al find that low-skill workers in innovative firms do better than low-skilled workers elsewhere in the economy.

Schaefer and Singleton (2018) found that just over 40% of the increase in wage inequality was accounted for by between-firm variation in Britain over the past two decades.[21]

Figure 3: Variance decomposition of UK wages, 2004-2014



Source: Aghion et. Al (2017)

Given that the academic evidence suggests within-firm factors alone are unlikely to explain all of the variations in wage levels or wage growth seen in recent years, it is necessary to explore between-firm factors and the extent to which these are contributing to variations. It is to this that we now turn.

Between-firm factors

Between-firm variations in wage growth are likely to play a key role in explaining variations in pay and career progression in the UK economy, with evidence suggesting substantial variations in pay growth in different regions, sectors and sizes of business in the UK.

A long tail of unproductive companies in the UK, with limited scope to raise wages

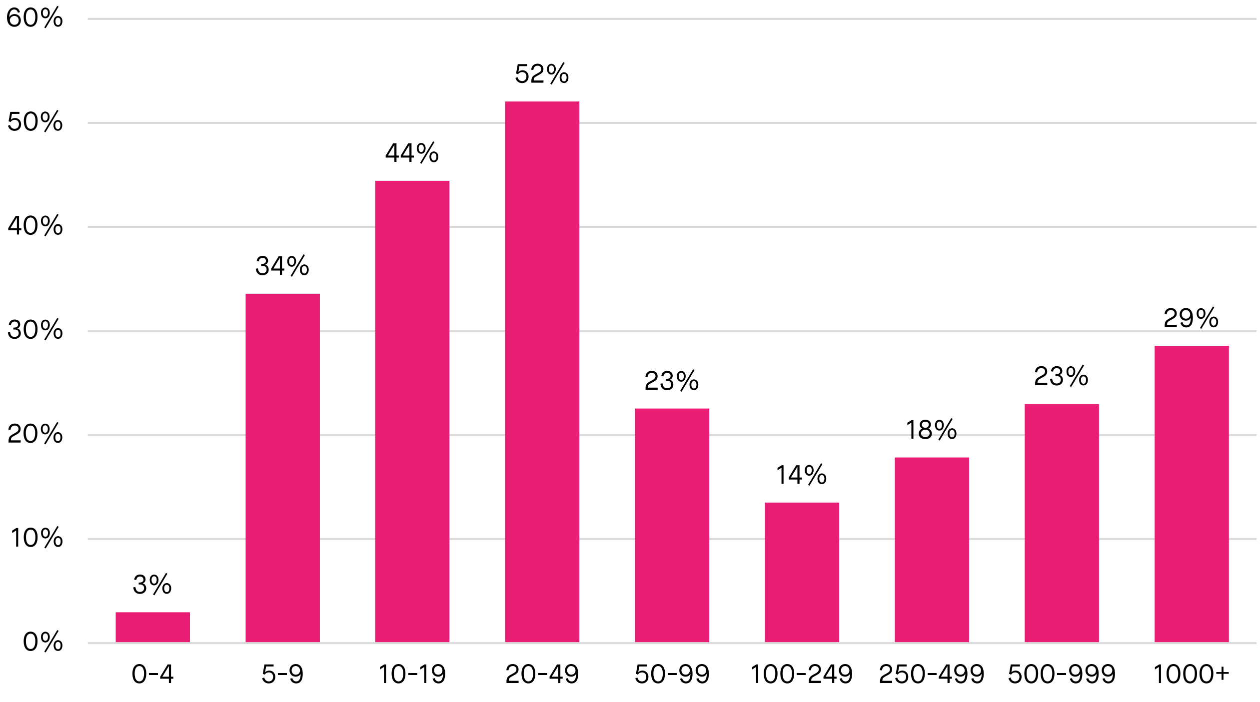
Research by McKinsey and Company shows that, compared with Germany, the UK has a long tail of employees working in relatively low productivity companies.[22] That is to say, employment in the UK is more skewed toward low productivity, low paying work compared with Germany. The analysis shows that variations in company productivity are greater in the UK than in Germany. Individuals working in low productivity companies are likely to have more limited opportunities to see pay growth (given the link between productivity and company profitability). Furthermore, career progression might also be more limited, if lack of company growth means the creation of fewer job roles higher up the pay scale.

A growing pay gap between smaller and larger companies

SMF analysis of data in the ONS Annual Survey of Hours and Earnings suggests that there are substantial variations in employee pay growth across different sizes of business in the UK. Between 2003 and 2015 (the years for which the ONS provided comparable data[23]), median employee pay in firms with 1,000 or more employees grew by close to 35%. In stark contrast, median pay grew by about 10% among firms with less than 20 employees. Deeper analysis of this issue is beyond the scope of this project, but it is worthy of further analysis to assess whether it is the size of the firm, or other associated factors, that are driving these variations in wage outcomes. We note, however, that our observation on the size of business matters in and of itself because policies often vary according to firm size.

Indeed, the data suggests that median employee pay for small companies with less than 20 employees was lower in 2015 than in 2009. Rather than reflecting pay cuts within companies, this is likely to be due to company start-ups in recent years being in relatively unproductive sectors of the economy – raising questions around why more businesses are not being established in better-paying, more productive industries. As the chart below shows, wholesale & retail and accommodation & food services accounted for 44% of the growth in the number of businesses with 10-19 employees between 2010 and 2018. Among businesses with 20-49 employees, these sectors accounted for over half (52%) of growth in the number of businesses.

Figure 4: Proportion of growth in the number of businesses accounted for by the wholesale & retail and accommodation & food services sectors, by employee size band, 2010-2018



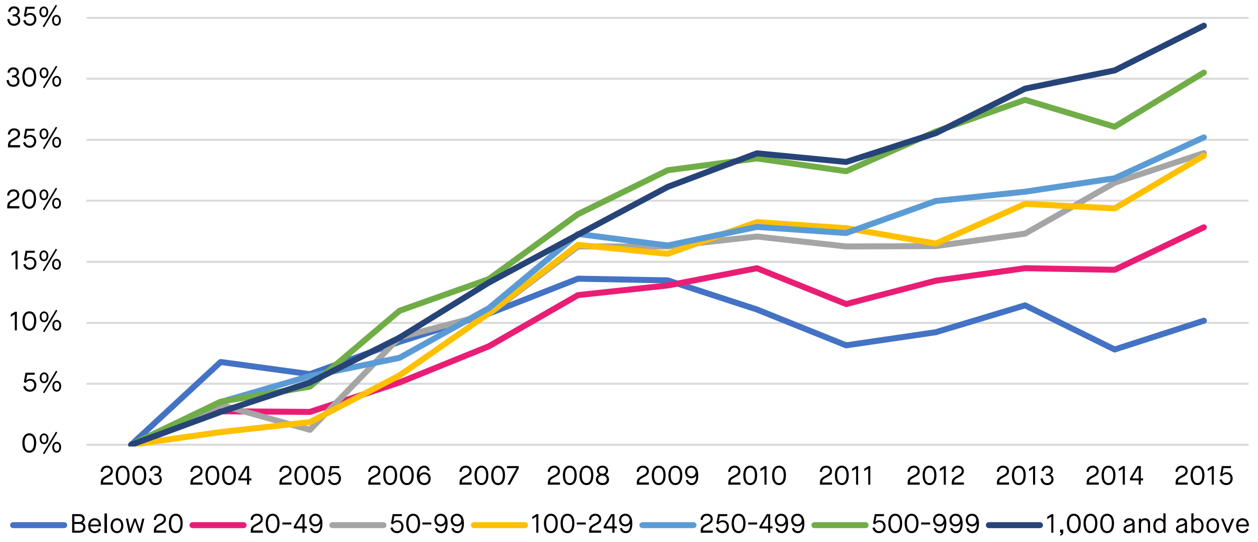
Source: ONS, SMF analysis

Notably, our analysis of the pay growth gap across different sizes of company shows a much smaller difference in pay growth when just looking at *full-time* employees. When just looking at full-time workers, we find that median employee pay increased by 27.6% between 2003 and 2015 among firms with less than 20 employees, compared with 32.9% among firms with 1,000 or more employees. For full-time employees, it is those in firms with 20-49 employees, rather than those with less than 20 employees, which saw the slowest growth in median pay between 2003 and 2015.

The narrowing of the weekly pay growth gap when looking at full-time employees suggests that weak pay growth among part-time workers is a key driver of variations in pay growth across different sizes of company. Employees in small companies with less than 20 employees are disproportionately likely to be working part-time; while these companies accounted for 14.2% of *all* employee jobs in 2015, they accounted for a lower 11.5% of all *full-time* jobs.

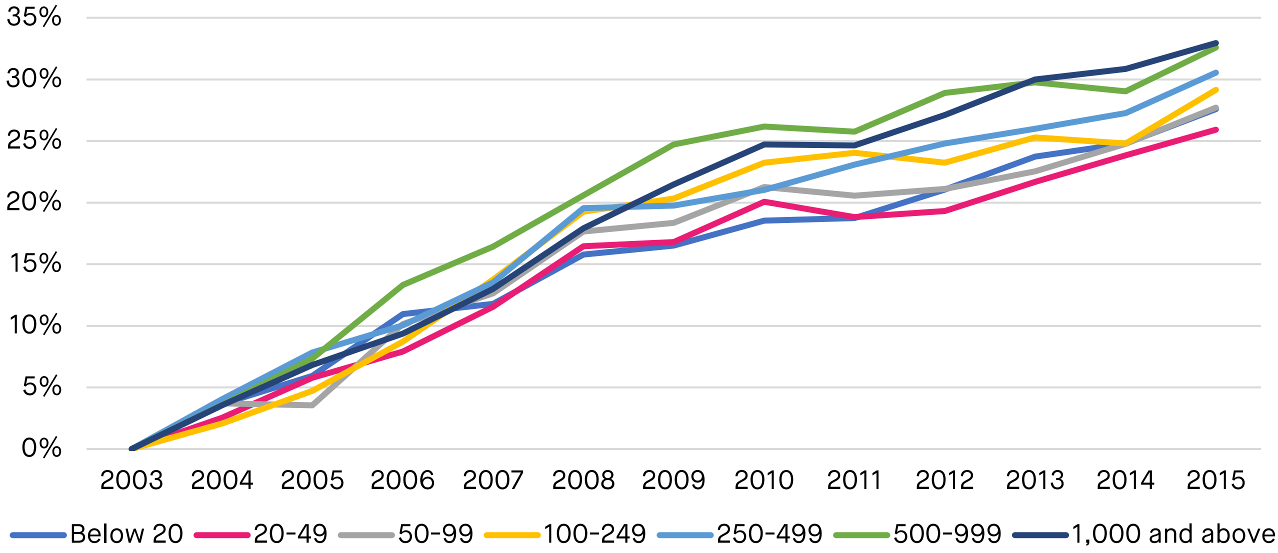
Subdued pay growth for part-time workers in small companies could be a reflection of curtailed working hours, or simply sluggish growth in hourly pay rates – something which is worth exploring in future research.

Figure 5: % change in UK nominal median gross employee weekly earnings since 2003, by employee size band of company, all employees



Source: ONS Annual Survey of Hours and Earnings

Figure 6: % change in UK nominal median gross employee weekly earnings since 2003, by employee size band of company, full-time employees only



Source: ONS Annual Survey of Hours and Earnings

Variations in pay growth among different sizes of business are, in part, likely to reflect differences in productivity performance in recent years. For example, ONS research found that, among firms with between 10 and 49 employees, there was an increase in the share of businesses with negative levels of economic output (gross value added) between 2003 and 2015.[24] Firms can have negative levels of value added per worker in specific periods when they report larger values of purchases than their total turnover.

Beyond productivity, another factor which might be contributing to variations in pay growth is the impact of government policy changes which have had a disproportionate impact on small and medium-sized businesses. The introduction of pension auto-enrolment, for example, is likely to have had a more significant impact on small-to-medium sized companies as they were less likely to have had pension provisions in place to begin with. Making pension contributions may have, in some instances, caused firms to rein in pay rises in order to offset this cost increase, or to reduce working hours – though it is difficult to discern this from the data graphed above, given that auto-enrolment occurred towards the end of the time horizon. Intuitively, at least, there are reasons to believe that regulatory measures such as auto-enrolment might have suppressed pay growth in smaller sized firms, as employers attempted to offset cost increases associated with the measure.

Different business models – “high road” versus “low road” employers

Another driver of variations in wage growth between businesses is likely to be different operating models. Some of the literature has made a distinction between “low road” and “high road” businesses.[25] Low road businesses are those that primarily focus on low costs, including wages, as a means of providing competitive advantage in the form of low prices. Such an operating model might also entail lower levels of investment, given the focus on low costs.

High road businesses, by contrast, are those that focus more on product quality and innovation as a source of competitive advantage – rather than cost control. Such firms are more likely to invest in physical capital and human capital, such as training. Investment in productivity-enhancing technologies and training should in turn translate into higher wages and career progression opportunities.

	"Low road" business	“High road” business
Source of competitive advantage	Low costs (e.g. wages) as an enabler of low selling prices	Focus on quality, sophisticated products and technology
Growth drivers	Maintaining low wages and containing other costs	Innovation, investment and training

Understanding the extent to which different business models are driving variations in wage and career progression is difficult, given that official labour market datasets such as the Labour Force Survey do not provide insights into the extent to which a firm is a “high road” or a “low road” employer. This is thus an area where there is scope for further research, including the gathering of additional data to support statistical analysis on the importance of business models to wage progression.

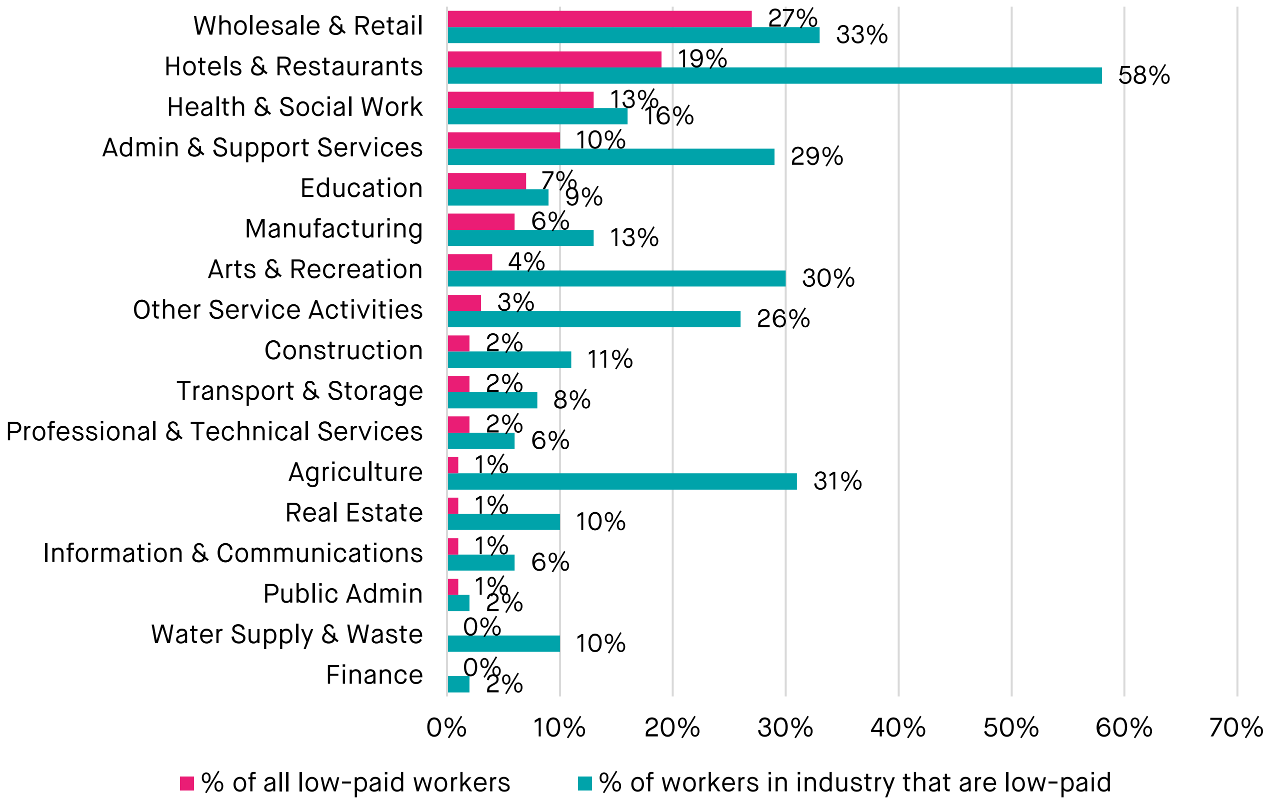
Regional and sectoral variations in pay, wage progression and career progression

Low-paid workers are concentrated heavily in a small number of sectors of the economy, suggesting that between-firm factors are a key driver of variations in pay and career progression. We acknowledge that headline sectors are not homogenous and that they contain more productive and less productive businesses as well as firms with stronger and weaker track records of providing wage progression. For instance, the financial services sector contains very high value (and high paid) investment banking, alongside lower value (and lower paid) functions such as call centres and back office functions. However, existing research suggests that major sectoral differences exist in terms of low pay and pay progression.

Research by the Resolution Foundation suggests that the Hotels & Restaurants and Wholesale & Retail sectors together account for almost half (46%) of all low-paid workers in Britain (with low pay defined as earning less than two thirds of median employee hourly pay).[26] Health & Social Work (13%) and Administration & Support Services (10%) also account for a relatively high proportion of low-paid jobs in the UK. This affects wages. It also affects poverty rates. Analysis by the JRF has shown that workers in many of the same sectors also have particularly high rates of poverty: accommodation and food services; agriculture, forestry and fishing; administrative and support services; and wholesale and retail.[27]

As we discussed earlier in this chapter, industries such as hospitality and retail not only have low levels of average pay, but they have job hierarchies which limit wage and career progression over time compared with other sectors such as manufacturing, due to a lack of mid-ranking job positions in terms of pay

Figure 7: Distribution of low-paid work by industry, Great Britain, April 2017



Source: Resolution Foundation

Analysis by the Low Pay Commission has shown that many minimum wage jobs are concentrated in a small number of sectors.[28] Almost half of all minimum wage jobs are in just three low-paying sectors: retail, hospitality and cleaning and maintenance.[29] Importantly, some of the same sectors are also associated with poor prospects for workers to escape low-paid work: remaining in the sales or hospitality sector has also been found to be negatively associated with progression.[30]

Low-paying industries are much more prevalent in some parts of the country than in others. Regional concentrations of low-paying businesses can curtail pay and career progression by limiting the ability of workers to find better work elsewhere. Similarly, a lack of businesses in relatively high-paying industries such as finance and information & communication can also limit pay progression by creating a dearth of good jobs. We return to this later when looking at regional tax.

A simple one-variable analysis suggests that the combined proportion of retail & wholesale and accommodation & food services businesses in a local authority can explain about two fifths of the UK-wide variation in low pay rates (defined here as 30th percentile earnings for those resident in each authority). [1]The combined proportion of information & communication, financial services and professional services businesses in an area explained about two thirds (65%) of the variation in low pay rates in the UK in 2018. Where these businesses are more concentrated, pay rates are notably higher.

Figure 8: 30th percentile earnings of full-time employees versus the % of business units in wholesale & retail and accommodation & food services, by local authority, 2018

Source: ONS, SMF analysis

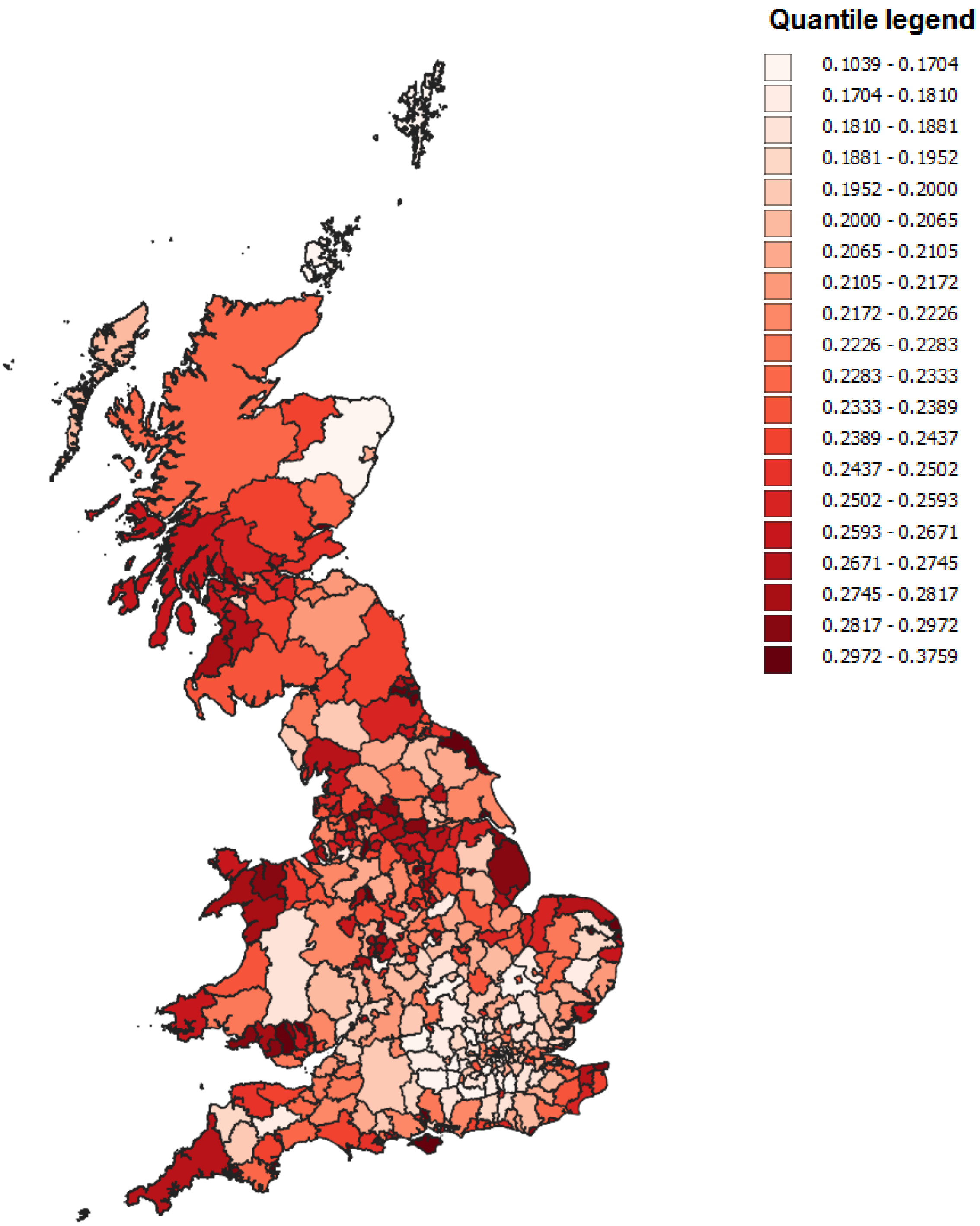
[1] Note: We tested our analysis by local authority and by 'Travel To Work Area'. We report our findings based on local authority as these are the most robust statistically. We accept that some workers will live outside of the local authority in which they work. However, longer commutes are more common among those on higher wages.

Figure 9: 30th percentile earnings of full-time employees versus the % of business units in information & communication, financial services and professional services, by local authority, 2018

Source: ONS, SMF analysis

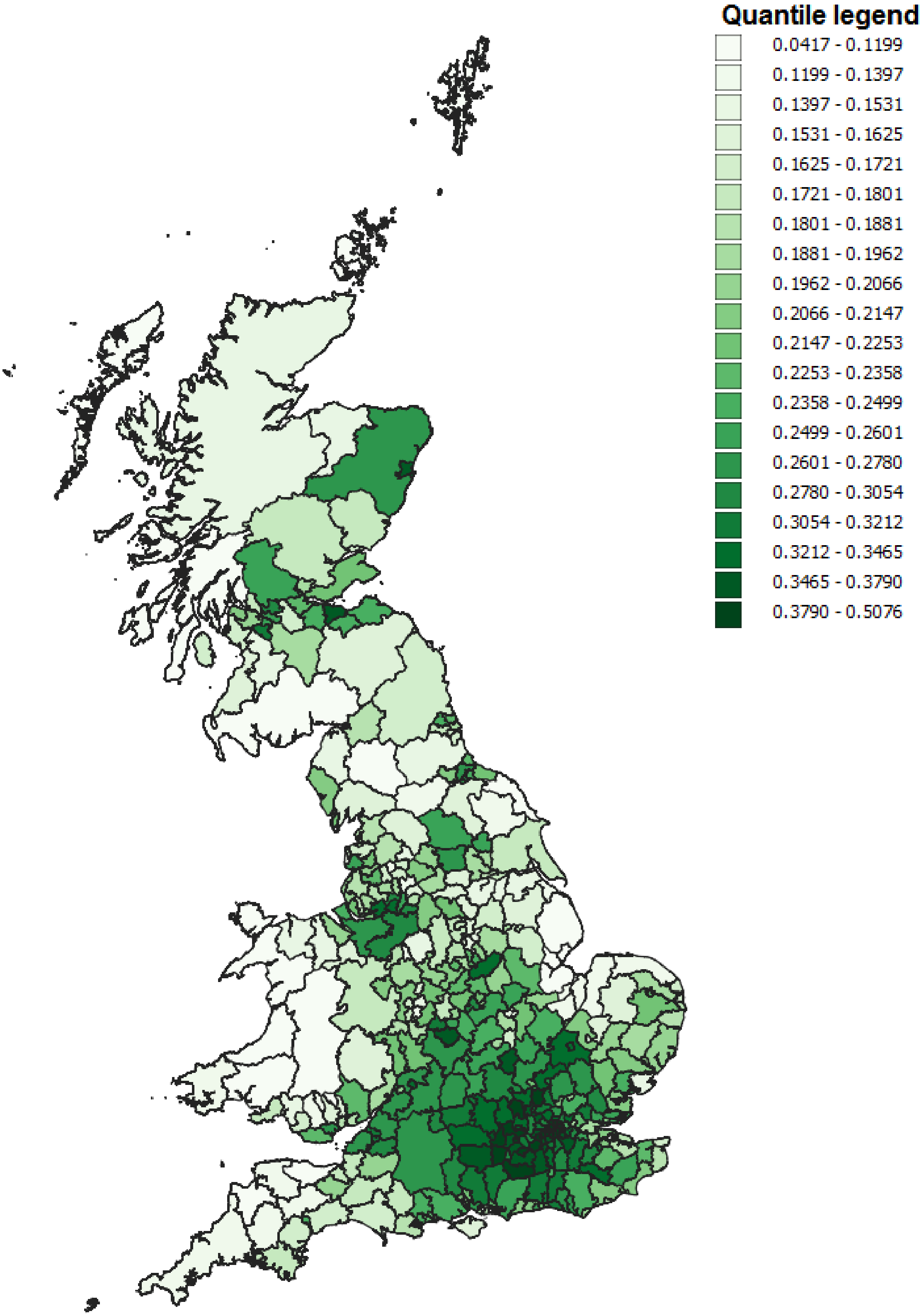
As the maps overleaf show, there is a significant regional dimension to the concentration of low-pay and high-pay industries across the country – highlighting the need for regional policy solutions to tackle variations in pay progression. We note, in particular, that high paying industries in England are heavily concentrated in and around London, while low-paying industries (namely wholesale & retail and accommodation & food services) are heavily concentrated in the North of England, parts of Wales and in coastal communities. Past SMF research has suggested that low pay is pervasive in many of the UK's coastal communities, given a lack of industries with higher rates of average pay. Poor transport infrastructure in coastal communities can further hinder the ability of individuals to access better-paying work.[31]

Figure 10: Percentage of business units in either wholesale & retail or accommodation & food services. Darker red implies a higher proportion



Source: ONS, SMF analysis

Figure 11: % of business units in information & communication, financial services or professional services. Darker green implies a higher proportion



Source: ONS, SMF analysis

Individual characteristics

In addition to the characteristics and behaviours of businesses across the UK, variations in pay progression may also be driven by the characteristics of *individuals*. If an individual's qualification levels, or their life circumstances, make it more difficult to bargain for higher pay or to achieve a promotion, then their pay progression may be more limited. We acknowledge that the impact of these individual characteristics may be compounded by business structures and cultures (for instance, the culture of viewing full-time workers as more committed and ambitious compared to part-time workers).[32]

Here, we focus on the links between individual characteristics and likelihood of having a low level of pay. As we discussed earlier, evidence shows that most low-paid workers struggle to escape low pay, meaning that low pay levels are closely linked to low rates of pay and career progression. There is currently only limited evidence on personal characteristics and how this influences wage progression and career progression.

Part-time workers

Analysis by the Resolution Foundation suggests that just over half (57%) of low-paid workers, with earnings below two thirds of median hourly pay, are part-time workers.[33] Just over a third (36%) of all part-time workers in the UK are low-paid, on this definition. The number of years worked part-time is negatively linked to wage progression, raising questions about the quality of part-time work in the UK.[34] **Not only are average pay levels relatively low for part-time workers, but evidence suggests that their pay *progression* is more limited too.** Resolution Foundation research has shown that part-time workers are much less likely to achieve pay progression over a ten-year period, and that getting stuck is becoming more common for this group.[35]

Part-time workers might struggle to achieve pay progression for several reasons. First, lack of pay progression might reflect some of the individual characteristics of part-time workers – such as their qualification levels relative to full-time workers. Analysis by the ONS, shows that those with no qualifications are more likely to be working part-time, compared to those with qualifications.[36] There are also important interactions with gender and motherhood, as women are much more likely to work part-time to take time out of the labour market.[37]

Another plausible explanation is that part-time workers struggle to achieve promotions and associated pay rises because of their *need* to work part-time, for example due to caring responsibilities. While an individual may be able to work part-time in their current job role, higher-level roles (such as managerial positions) might only be available on a full-time basis in some instances – meaning such individuals cannot apply for better-paid positions. In some cases, this is likely to be because of culture and historical practices; in other cases, it may be due to practical considerations for the employer.[38] For example, in some job positions, it might be significantly less efficient to have two part-time workers performing a role, rather than one full-time worker.

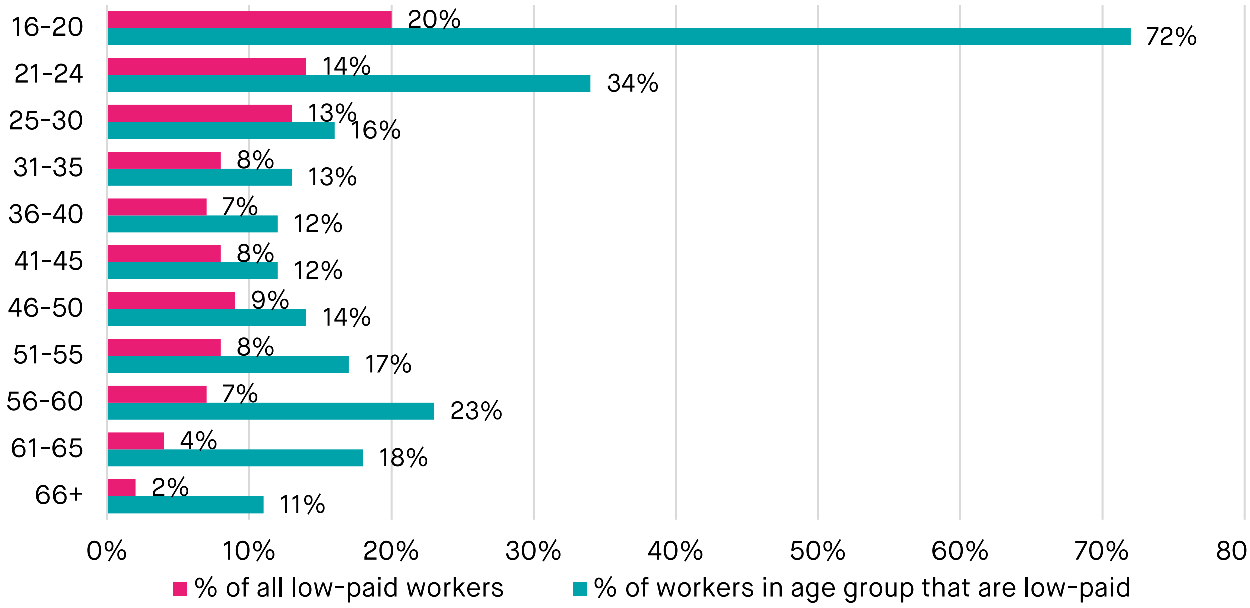
Age, gender, race and disability status

There are significant variations in the prevalence of low pay across age groups, gender, race and disability status in the UK. Such characteristics are also related to pay and career progression, reflecting issues such as discrimination in the labour market.

Women account for just over three fifths (61%) of all of those on low pay in the UK.[39] As has been widely discussed in recent years, a gender pay gap persists across most sectors of the UK economy, with men on average earning more than women. This raises a range of questions around issues such as discrimination in the labour market, as well as societal norms such as the common expectation that women will be responsible for most aspects of caring for children and other relatives. Caring expectations can increase the need for individuals to work part-time which, as we have discussed, limits pay progression.[40]

The prevalence of low-pay varies by age group. Workers aged 30 and under account for about half (47%) of low-paid workers in the UK. Indeed, 72% of workers aged 16-20 are low-paid, as are just over a third of 21-24 year olds. We note that the proportion of low-paid workers by age group declines up to the 41-45 age group, but then starts to rise by age. About a quarter (23%) of 56-60 year olds are low-paid. Conceivably, variations in low pay by age group might reflect differences in skill levels; younger workers might have lower level skills due to inexperience, while older workers might lack the most up-to-date skills needed to undertake well-paying working the modern economy (such as computer proficiency). The rising proportion of lower-paid workers in older age might also reflect lifestyle changes – such as individuals choosing to work part-time or switching to lower-paid but less stressful work as they approach retirement.

Figure 12: Distribution of low-paid work by age group, Great Britain, April 2017



Source: Resolution Foundation

Race and disability status also have a bearing on the extent to which individuals are likely to be on low pay. While less developed than the academic and political discussion of the gender pay gap, there is emerging evidence that pay gaps exist across racial groups and between disabled and non-disabled individuals.

Trade Unions Congress (TUC) research published in 2018 estimated that disabled workers earn £2,730 a year less on average than non-disabled workers and that disabled workers are more likely to work in lower-paid occupations.[41] The TUC research suggests that this might be a reflection of the fact that disabled employees are more likely to work part-time, and also less likely to have higher levels of education – limiting their access to jobs with higher rates of pay.

Research by the Resolution Foundation suggests that substantial pay gaps exist across racial groups. They estimate that, between 2007 and 2017, the total annual cost of pay penalties experienced by black, Indian and Pakistani/Bangladeshi men and women amounted to £3.2bn per year.[42] While this analysis suggests that some of this gap can be explained by differences in educational attainment, this is unlikely to explain the entirety of the pay gap. For example, the research found a 17% pay penalty among black *graduate* men, compared with white men. Ultimately, factors such as discrimination may also play a role in limiting pay progression among some groups. Evidence shows that there are barriers to progression up the career ladder for some ethnic minority groups who are in work. A report by Hudson and Radu (2011), commissioned by the Joseph Rowntree Foundation, found that persistent barriers to progression included the operation of informal selection criteria and organisational cultures that are not committed to countering racism.[43]

Research also suggests that “homosocial reproduction” – the tendency of individuals to hire people similar to themselves – is a driver of labour market discrimination, and reduced career progression opportunities for some groups.[44]

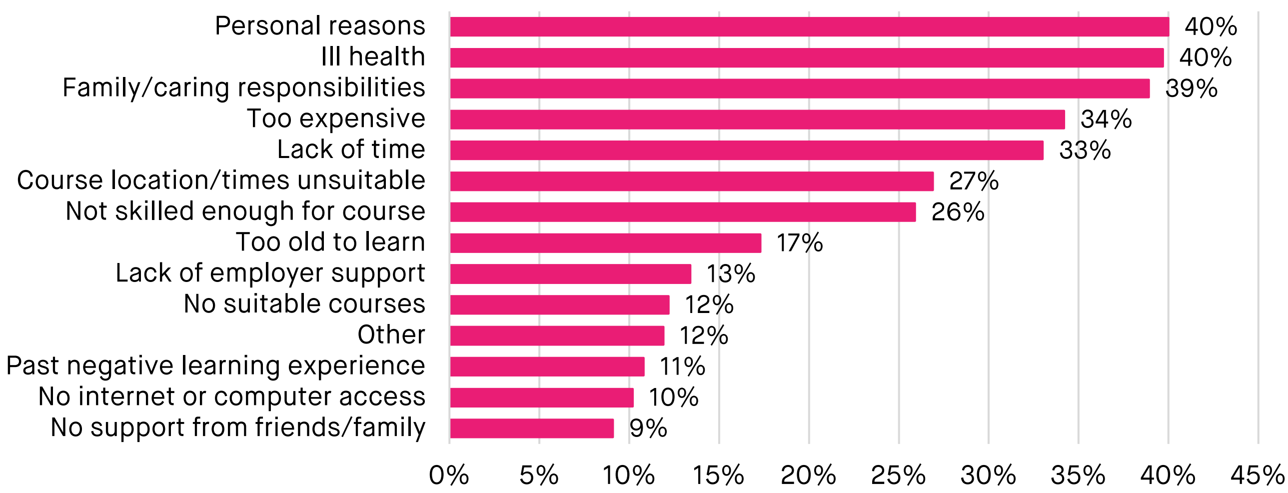
Learning and training

Access to training and qualifications – either provided by employers or undertaken by individuals of their own volition - can play a key role in enabling lower earners to transition into better-paid work.

Within a given job role, learning and training (investment in human capital) should in theory contribute to higher pay if it translates into greater levels of employee productivity. It can also assist career progression, by enabling individuals to realise internal promotions or switch to better-paid work with a different employer.

However, many individuals report barriers to learning and training. According to the 2016 Adult Education Survey, about two fifths of those with no qualifications cited ill health and caring responsibilities as barriers to learning and training. Just over a third (34%) cited the expense of education as a barrier, while 13% cited lack of employer support as a factor.

Figure 13: Cited barriers to learning and training among those with no qualifications



Source: Adult Education Survey, 2016

Lack of employer support for training might reflect, in part, a lack of (perceived) long-term benefits for the employer – for example, if an employee is not expected to stay at the company for long, in which case training costs might exceed benefits. Indeed, training might make it easier for employees to leave an employer through opening up new job opportunities – further undermining employer support despite a significant proportion of firms reporting that a lack of basic skills is impeding productivity.[45] This economic theory applies especially to generic skills training which make the worker more valuable to other prospective employers as well as the host employer.

The theory also applies to workers in all occupations. However, previous research by the SMF has reported that those with low qualifications are less likely to be offered training and to take up training.[46] This is discussed in more detail later in the report. This may be explained by a range of potential factors including:[47] employers reporting significant shortages of generic skills in lower-paid occupations (which, as discussed above, they may have a weak incentive to invest in); higher turnover among low-paid workers; less intense human resource oversight and support for lower-paid workers; and the wide range of barriers associated with their wider lives which impose barriers to taking up training.

Conclusions

This chapter has shown that a lack of pay and career progression among lower earners is likely to be driven by a range of factors, including:

- Low levels of employee bargaining power, such as when an employer has monopsony/oligopsony power in setting wages. Trade union density has decreased and this is an important area for further research and policy development (though not one we cover in this report).
- Company job hierarchies which limit the ability of lower-paid workers to achieve pay progression via promotion.
- Variations in productivity and pay growth by size of business and industry sector.
- Regional concentrations of low-paid and high-paid work which limit the ability of workers to realise pay progression by changing employer.
- Individual characteristics, such as a need to work part-time and disability status.

Tackling each of these drivers of low pay and limited career progression will require different policy solutions. For example, while within-firm differences in pay growth might be targeted through mechanisms such as mandatory profit-sharing, regional variations are likely to be best tackled with policies which aim to increase the proportion of high-pay industries in regions suffering from low average levels of pay. These potential policy solutions are the focus of the following chapters of this report.

CHAPTER 3: MINIMUM WAGE POLICY

In this chapter we consider whether wage regulation could be adapted to encourage pay and career progression. Currently, evidence shows that minimum wage increases do not affect the probability of progressing out of a minimum wage job.[48] Minimum wage policy focuses on the lower bound of wages.

In fact, while regulated wage floors can increase wages at the very bottom, they may result over time in more people only getting a pay increase because they are close to the wage floor. As the minimum wage rises, a greater number of employees will be caught at or just above the lower bound of wages. The coverage of the national minimum wage is expected to reach 3.4 million people in 2020, compared to 1.6 million in 2018.[49]

The UK's main rate is set soon to hit the Government's target of 60% of median wages, and the Chancellor has set out an 'aspiration to end low pay in the UK' (accepted typically to be two thirds of the median) and is consulting on the Low Pay Commission's remit to this effect.[50] But, as has been noted elsewhere, increasing the wage floor does not directly address the problem of large numbers of people being stuck at the lower end of the income distribution.

Rationale for considering minimum wages

There are two potential rationales for considering wage regulation policy as a mechanism for promoting career progression and wage progression. First, a minimum wage helps protect workers with weak bargaining power. This argument applies to workers on the very lowest regulated wage floor. However, weak bargaining power may also affect workers paid wages higher than the wage floor. Theoretically, therefore, minimum wages policy could be designed to give higher wages to this wider group, such as through more age-related bands.

A second circumstance in which wage regulation may be considered beneficial is when it can drive productivity improvements among this part of the workforce. These would in turn, increase the economic value of low-paid workers. While evidence on the effects of minimum wages on productivity is mixed, wage regulation can drive productivity improvements both at the business level and more broadly at the economy level. In some cases, businesses respond to increased labour costs due to minimum wages by implementing organisational change, training and efficiency.[51] One study found that the introduction of the National Minimum Wage (NMW) in the UK led to improvement in labour productivity in all the low-paying sectors, and particularly in larger firms.[52] However, other analysis has found little evidence that low-paying sectors have increased their productivity.[53] Despite this, it is worth noting that some low paying sectors in the UK – such as food processing – are less productive than equivalent industries in other European countries, so there are productivity gains to be made in these areas.[54]

Minimum wages in the UK

The UK already has elements of progression related to age and experience in the its minimum wage system. As shown in the table below, there are varying rates for those under 25 years old, for whom the respective NMW applies. Other comparable countries have similar age-based rates, although they tend to have fewer age bands.

These rates are set by the Low Pay Commission (LPC), who consider factors such as economic growth, average earnings, productivity and effects on employment.

Table 1: UK minimum wages rates

	Minimum hourly rate		% increase
	2018-19	**2019-20**	**Year-on-year**
25+	£7.83	£8.21	4.90%
21-24	£7.38	£7.70	4.30%
18-20	£5.90	£6.15	4.20%
16-17	£4.20	£4.35	3.60%
Apprentices	£3.70	£3.90	5.40%

Source: http://www.minimum-wage.co.uk/

In particular, the differentiated rates are set to protect younger employees from being priced out by older employees. These rates also reflect the reality that younger employees tend to earn lower wages, as a consequence of lower average experience and higher training costs.[55] As they gain experience and training, wages for young employees should increase. For example, apprentices over the age of 19 who have completed the first year of their apprenticeship are entitled to the NMW for their age. Following the existing logic that more experience equates to a higher minimum wage, the question arises of whether this approach could be applied further up the age spectrum.

Wage structures linked to progression: an international perspective

Multiple wage rates

There are several examples of wage structures, both in the UK and internationally, that could encourage pay and career progression. Of the countries operating a statutory minimum wage, approximately 50% set legal minimum wages by occupation, industry and/or company size.[56] Just over half of OECD countries with minimum wages have graduated or "sub-minima" rates for young people.[57] The table below shows examples of other minimum wage systems; the number of age-related rates varies, from none in Germany, to 5 in France.

A number of initial insights can be drawn from this comparison of international practice. First, none of these countries have different wage thresholds for workers aged over 25. Indeed, most do not have special rates for workers beyond 18 and 21. Second, the UK's existing system already has one of the largest number of different wage rates.

Table 2: Youth minimum wage rates of other countries, 2017

Country	No. of age-related bands	Maximum age
Ireland	3	19
Belgium	4	20
France	5	17
Greece	1	25
Germany	0	-
Luxembourg	2	16
Malta	3	17
Netherlands	7	21
US	2	20

Source: Eurofound, Statutory minimum wages 2018

Table 3: Youth minimum wage rates of other countries, 2018

Country	Age-related bands	Percentage of minimum wage
Ireland	Under 18	70%
	18 and in first year of employment	80%
	Over 19 and in second year of employment	90%
France	Under 16 working in the summer holidays	80%
	15 and 16 with less than 6 months experience in the sector	80%
	17	90%
	Professionalisation contract	55-100% (depending on age and previous qualifications)
	Apprentices	25-78% (depending on age, seniority and the applicable sectoral agreement)
Belgium	Working students and part student/part employee	% increase according to number of years in employment or in college (wage levels determined by social partners of each sector)
Germany	No age-related bands	-
Greece	Under 25	87.2%
Luxembourg	15 and 16	75%
	17	80%
	Over 18 and qualified	120%
Malta	16	94%
	17	96%
	Employed by same employer for one (two) years	1.8% (3.5%)
Netherlands (from July 2019)	15	30%
	16	34.5%
	17	39.5%
	18	50%
	19	60%
	20	80%
	21 and over	100%

Source: Eurofound, Statutory minimum wages 2018

Age- and experience-related pay rates

Ideas and lessons can also be learned from specific wage regulation policies in other countries and specific sectors as well as in public sector wage setting and private sector practices. Experience in Japan and in the UK public sector does not indicate that time-served pay increases are a good idea[58].

In Japan, there has historically been a seniority wage system where salary rises are based on length of employment. In theory, this system could boost productivity because firms invest in long-term employees who will be motivated by their wages rising over the years. Although workers are assured of pay rises, the obvious downside is the incentives on workers to stay in the same job, even if their productivity has not improved. Also, because of structural changes in the economy, firms are unable to guarantee a job for life and there has been an increase in part-time jobs which can offer limited access to training.[59] These combined factors mean that in recent years there has been some movement away from seniority wages, with a shift towards performance-based pay instead.[60] This was encouraged by the prime minister, who supported a reform of pay structures to improve labour efficiency. Japan has a far lower productivity compared to other leading OECD countries. Although evidence is mixed, a study found that productivity has increased in firms following the introduction of performance-based pay, but only when accompanied with measures of procedural fairness.[61]

Public sector pay in the UK has also traditionally been structured around pay scales, with some workers automatically progressing up the scale through time served. However, this is now largely being phased out, although councils can choose the criteria on which to grant increments, including the length of service.

Below, we describe some examples of wage structures that associate age or experience in the labour market with an employer with higher pay. The Agricultural Minimum Wage still exists in some parts of the UK, with some claiming the pay rates encourage progression. These examples are useful to consider in the debate about low pay progression, but we have limited evidence of how these wage structures affect progression.

International examples

Agricultural minimum wages in Wales and Northern Ireland

Agricultural workers must be paid at least the Agricultural Minimum Wage (AMW), which depends on the worker's job grade and category (or the NMW if it is higher). The grade is based on the worker's skills and responsibilities. Duration of employment is also relevant for certain grades, for example if they have worked in agriculture for at least 2 of the past 5 years.[62]

The AMW was abolished in England; it was seen as bureaucratic and unnecessary given the existence of the wider minimum wage regime. However, the rates remain in Wales and Northern Ireland, with supporters claiming that the pay rates attract new entrants and reward skills, experience and qualifications. Some also believe it could encourage the long-term competitiveness of the sector.[63]

Minimum wages in Greece

The minimum wage in Greece differs by age and job category, as well as length of employment. For example, the minimum wage for employees over 25 increases by 10% after 3 years of work experience and 30% overall after 9 years of work experience (the percentage increase differs for technicians and craftsmen).[64]

Minimum wages and bonus system in Bolivia

In Bolivia, as well as the minimum wage there is a yearly bonus that is adjusted for the duration of employment of the worker in their present position. A second bonus is awarded if the company has made a profit in the previous year.[65]

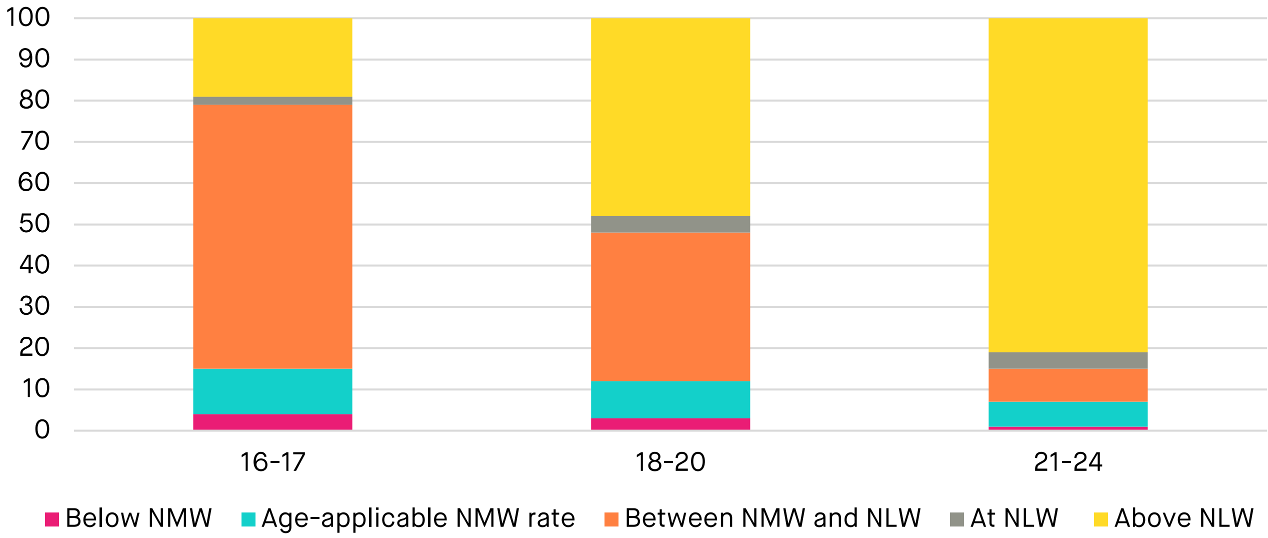
Minimum wage rates based on age brackets

One way to encourage wage progression through the minimum wage could be to introduce more age-related rates above 25. However, our analysis also suggests that the case for establishing additional age-related rates is weak. The rationale for setting the NLW for over 25s was because 21-24-year olds had the highest ratio of minimum wage to the hourly median wage amongst this group of workers. People within this age bracket had much lower pay and higher unemployment.[66] In comparison, the distribution of earnings for 25-year olds converges to those between 35-49 and 50-64. This indicates that the evidence to support the introduction of another age bracket above 25 is weak, unless we decided to add multiple age brackets such as at 30, and so on. Comparing internationally, it is rare for countries to have wage rates over the age of 25.

Having different wage rates can create administrative costs for employers, who may prefer to pay a similar rate for those with the same role. As well as this, some think that employees will be demotivated if pay is differentiated on the grounds of age.[67] Although the presence of existing youth rates is important for reasons outlined above, there is less of a case for additional age-related rates.

Figure 14 shows that the proportion of jobs that are paid the corresponding age-related rate is relatively low for each age group. For 16-17-year olds, only 11% are paid the age-applicable NMW rate, whilst 64% are paid between this and the NLW. 6% of 21-24-year olds are paid the relevant NMW rate, and 5.2% of 25-30-year olds are paid the NLW.[68] This suggests that these age-related wage bands are not used as the reference in the same way that the NLW is used for workers aged 25 plus.

Figure 14: Distribution of hourly pay, by age group, 2018



Source: Low Pay Commission Report 2018

Linking the minimum wage to tenure and training

Linking wage level to tenure

The incremental increases in wage rates for those under 25 are in place because they correspond with experience in the workforce and average earnings. Theoretically, this concept could be extended by linking further increases in the minimum wage to length of time in the workforce, rather than setting another age bracket. If employees that have been in the workforce for longer are gaining more experience and becoming more productive, their wages should be increasing to match this.
However, there are likely to be multiple disadvantages of this approach. First, such a policy might benefit workers who are not necessarily more productive despite having spent longer in the workforce. To minimise this, the reform could be designed to apply only for a limited amount of time, such as one year after receiving NLW, although this would also reduce its impact on wages. Second, it could create incentives for short-term contracts with employers releasing workers ahead of any automatic wage increases. Third, as with other regulation policies discussed, it would introduce additional complexity to the system, making it more difficult to enforce and costlier for employers to implement.

Linking wage level to training

Improving training can be an effective way to increase progression. There have been attempts to use the minimum wage system to incentivise employers to provide training. In 1999 employees over 21 years old were eligible for the Development Rate (or "accredited training rate"), which was lower than the NMW, for a maximum of 6 months when starting a new job with a new employer and engaging in training.[69] This is similar to the current sub-minimum apprentice rate; after one year of experience those over 19 are then entitled to the minimum wage for their age.

There was a low take up of the historical training rate, partially because of lack of awareness of the scheme, and the costs and complexity associated with operating the accredited training schemes. This older worker's Development Rate was abolished in 2006, following the LPC's recommendation – this conclusion was reached because the rate was only used infrequently.[70]

Similar training rates recently existed in Ireland, but these were abolished in March 2019 following recommendations from the Irish LPC about the low take up and the definition of training.[71]

Looking at this historical example, using wage regulation to encourage training has not been successful in the past. It can be complex, and perhaps due to the complexity or other reasons there was very little take up. There could be softer approaches to support wage and career progression through training, that we discuss in the next section.

Potential challenges of complexity

Finally, we note more broadly that a more complex minimum wage framework could lead to a rise in the number of workers who are paid below the legal minimum amount, as more employers could become intentionally or unintentionally non-compliant. Research from the Low Pay Commission found that the introduction of the National Living Wage in 2016 (which saw employees aged 25 or above be paid at a higher rate) increased the number of underpaid workers.[72] This was a particular problem for low-paid employees aged 25 and above, one in five of whom were underpaid in 2016 (up from 15% in the previous year).[73] Should more expansive minimum wage regulation result in a higher non-compliance rate, enforcement measures would also need to become more extensive. HMRC's budget has been increasing since 2009/10 and is set to continue to rise as more resources are needed such as investigating and enforcement officers.[74] Additionally, softer enforcement initiatives might be needed such as increasing awareness among employers about changes in the structure of minimum wages and among employees on the channels available to complain if they suspect they are being paid below the legal minimum rate.

Looking to softer wage setting policies

The discussion above suggests that introducing additional age-, experience- or training- related wage rates is likely to be inadvisable.

Using wage regulation to encourage progression can be complex to implement and enforce, and quite rigid in nature. Previous attempts to do this, such as the Development Rate which encouraged training, had extremely low take up. Softer measures, such as guidance, might be a more effective way to support progression without causing unintended consequences such as adverse incentives (e.g. from tenure related wage increases).

In addition, we recognise that employers vary significantly and that different firms will need to take an approach that fits their business. Softer measures may help to raise awareness and change the culture throughout businesses to make low-wage progression a key part of the conversation – right from business plans and board meetings, to between employees and their employer.

Softer measures will be discussed in more detail in our second report on career and wage progression.

CHAPTER 4: PROFIT-RELATED PAY AS A ROUTE TO PAY PROGRESSION

This chapter explores the scope for considering profit-related pay (PRP) schemes as a method to boost pay among low-income earners. PRP includes payments or bonuses tied to the profit levels of all or part of the organisation, which are distributed among managerial and non-managerial staff.

Rationale for considering profit-related pay

Profit-related pay in theory

PRP schemes have the potential to improve employee earnings whilst boosting productivity across the economy: in theory, giving employees a share of their employer's profits acts as an incentive for workers to improve company performance.

Schemes operate by distributing a percentage of annual profits to participating employees, typically proportionate to their wage level. Ultimately, the success of profit-related pay as an instrument to increase wages among low-paid workers is dependent on the profit made by their employer and the proportion of profit which would be distributed to workers.

The Labour party proposed a version of PRP in 2018: an 'inclusive ownership fund', mandatory for companies with more than 250 employees. The fund would hold 10% of the firm's equity on behalf of employees. Workers would not be able to buy or sell this equity, but they would benefit from dividend payments, capped at £500 per employee.[75]

The long-term dynamics resulting from offering a PRP scheme to employees may benefit both the employer and employees across the wage distribution. If PRP increases productivity, then the policy may have benefits to individual workers, the employer and the economy.

Additionally, one of the principal disadvantages of linking pay to company performance - the resulting volatility of income – could also be one of its the main advantages. On one hand, employees may face volatility in their PRP income as it would vary up and down with profits. However, this flexibility could also enable firms to adapt when economic conditions change. In a downturn, as turnover falls, the profit-related component of an employee's salary reduces total wages in lockstep, acting as a safety net for jobs. Policymakers need to be alert to risks to workers as well. A policy that encourages employers to substitute from reward through wages to reward through profit sharing could lead to more volatile earnings. It could also potentially lead to lower earnings overall if for example, a firm made this switch and then suffered a year of weak profits. In such an instance, the worker may end up with lower base rate of pay and zero income from profits.

Profit-related pay in practice

Research on the impact of PRP schemes suggests mixed results. A 2017 UK study found that PRP is associated with positive effects on outcomes such as job satisfaction, organisational commitment, and trust in management, as long as these schemes are implemented in a transparent manner and extended to a large proportion of the workforce.[76]

On the other hand, evaluation of historic PRP policies, which attracted tax relief, showed that base wages reduced for participating employees. Estimates suggest that nearly all early schemes were already existing bonus packages converted to PRP and 60%-70% of later schemes were based on a salary sacrifice principle, where employees take a pay cut which is topped up by a profit-related payment.[77] This impact may have been a product of the design of the policy. As discussed later in this chapter, the legislation for tax breaks for PRP schemes was abolished in 2000 because employers were offering schemes mainly as a means to take advantage of the tax relief rather than in order to improve worker productivity or remuneration. Additionally, we note that the risk of lower base wages may not arise for workers on the minimum wage floor (because it would be illegal to reduce their hourly wages).

Evidence on the effect on productivity is also mixed. Research focusing on past PRP schemes has been broadly supportive of the view that profit-related pay boosted productivity.[78] Other evidence suggests that how PRP is implemented may influence its impact. A UK-based study concluded that 'the financial mechanism that links employees' pay to group or company performance, was positively associated with labour productivity'. However, the design and coverage of the scheme had a significant impact: in isolation, PRP or share ownership schemes led to lower productivity.[79] In contrast, when part of a broader compensation plan, such as being offered alongside a share ownership scheme, PRP initiatives lead to improvement in labour productivity.[80] Employee participation in PRP schemes are linked to improvements in job satisfaction, organisational commitment, and trust in management, as long as the mechanism for distributing profits is perceived to be equitable.[81]

Literature has suggested that the mechanism by which these benefits may arise goes beyond the straightforward financial incentive on the individual. Classical economics would suggest that the financial incentive would equate only to the marginal difference that the individual could make to the performance of the firm. In a large firm, a single employee could make a minimal difference single-handedly and the incentive would therefore be extremely modest. Theoretically there would also be a risk of 'free riding', because gaining a share of profits would not be contingent on individual contribution to overall performance.

However, there is a growing literature suggesting that the positive effect that arises from workers sharing in profits arises from group behaviours and norms.[82] While there is a risk that individual financial rewards crowd out intrinsic motivation, conversely, 'pro-social' rewards – when an individual's performance affects the reward of others – have been shown to be more effective, whether through peer norms, interdependency and commonality of interest. Research also suggests that PRP may influence productivity specifically in low wage sectors.[83] Analysis of the factors affecting productivity performance in low wage sectors in the UK compared to other countries found that 'performance related pay' was associated with higher levels of 'total factor productivity' among the workforce (i.e. factors other than labour quality and capital intensity). This definition of 'performance related pay' included payments based on individual, team or organisation performance (i.e. profit sharing).

PRP and the politics of the market

In addition to the evidence on their economic impact, *politically*, PRP initiatives may be important to demonstrate that workers can benefit from the market economy and that capitalism is designed to meet in their interests. It could be a positive step towards improving employer-employee relations and helping bridge the divide between the remuneration of managerial and non-managerial staff. Committing to distribute a proportion of profits among workers would also encourage businesses to consider their (perceived) treatment of workers.

The prevalence of low pay in firms which make profits

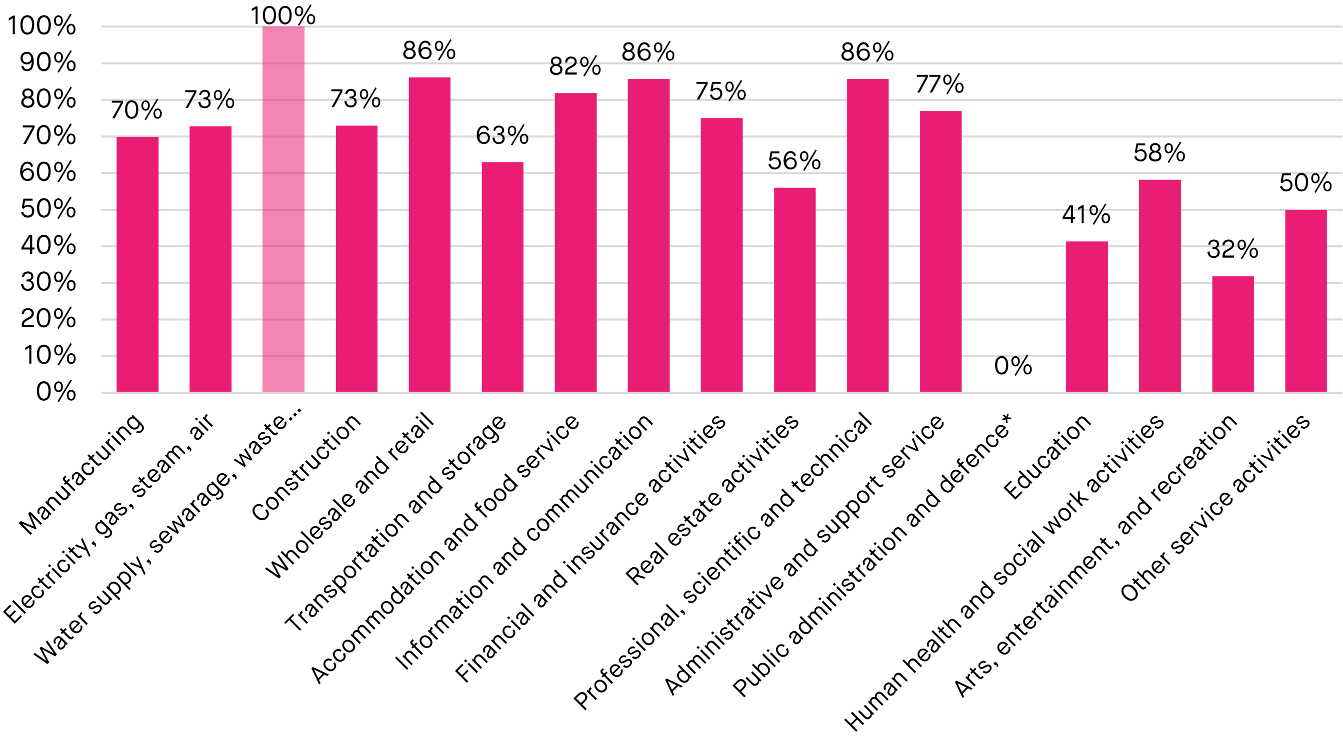
This section seeks to understand whether low-paid workers would be affected if PRP were widespread: are low-paid workers employed in organisations that make profits?

It is difficult to assess the extent to which low-paid workers are employed by profitable firms. One resource we can use is the 2011 Workplace Employment Relations Survey. Although this is now eights years old, and took place in a more subdued economy, it does provide data on wage levels and profits. In 2011, the median hourly pay in the UK was £11.24, making the threshold of low pay £7.49 per hour, equivalent to annual earnings of £13,600 for a 35-hour working week.[84]

SMF estimates suggest that 67% of *employers* surveyed in the 2011 Workplace Employment Relations Survey generated a profit in that period.

Figure 15 displays the disparities in the proportion of profitable firms in 2011 by industry. This data indicates that a majority of firms in low-pay sectors such as retail, accommodation and food and health generated a profit – suggesting potential gains that could be realised for workers from profit-related pay, holding everything else (such as other elements of pay) constant.

Figure 15: Proportion of profitable firms in 2011, by sector

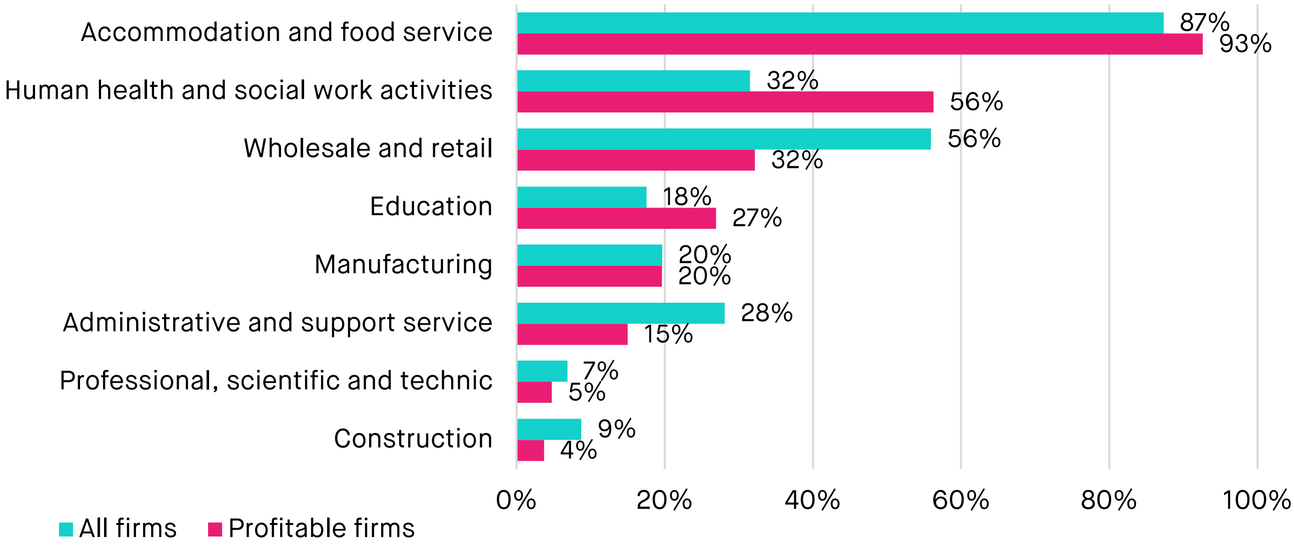


Source: SMF analysis of WERS 2011
Note: Small sample size for employers in the Water supply, sewerage, and waste management and Public administration and defence sectors.

Next, we seek to analyse whether the profitable firms are those that also employ low-paid workers. We find that a quarter (27%) of firms that generated a profit also paid more than half of their workforce £7.50 per hour or less. (We use this measure as more than half of the workforce earning below two thirds of median pay indicates a severe reliance on low-paid workers.)

Figure 16 shows that 93% of firms in accommodation and food services making a profit hired more than 50% of their workers at a low pay rate. The figures for the health / care sector is 58% and for wholesale and retail 32%.

Figure 16: Proportion of firms in which more than 50% of workers were low-paid



Source: SMF analysis of WERS 2011
Note: Due to data coding, we define low pay as earning £7.50 or less per hour
Note 2: Other sectors have been excluded from the analysis due to small sample size

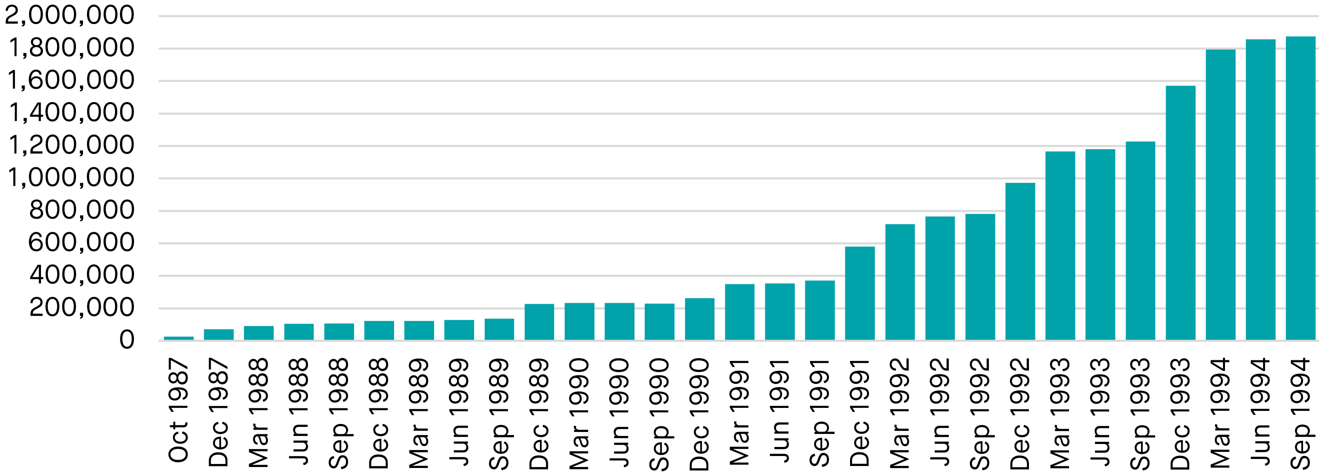
Further analysis of the coincidence of low pay and profits in the UK economy now would be very beneficial. Our current analysis indicates that a large number of profitable firms employ large numbers of low-paid workers. However, many low-paid workers are likely to be employed by unprofitable firms and would thus not benefit from PRP, at least in the short-term. Another consideration is low-paid employees working in the public and charity sectors which are run on a not-for-profit basis; these individuals would not benefit from PRP.

Profit-related pay in the past

Profit-related pay schemes attracted generous tax relief in the UK in the past, and the policies offer important lessons for the design of any policies in the future.

Legislated in 1987 in a bid to increase workers' pay without an accompanying rise in inflation, the Government applied an income tax break to profit-related payments up to £3,000 (£4,000 after 1991) or 20% of the employee's annual pay (whichever was lower). The scheme could apply to the whole company, or a division or a smaller unit. It had to cover at least 80% of the workforce.[85] The policy led to many more schemes, with around 1.9m employees received a profit-related payment top-up to their salaries from over 7,700 registered schemes in 1994.

Figure 17: Employees participating in a PRP scheme

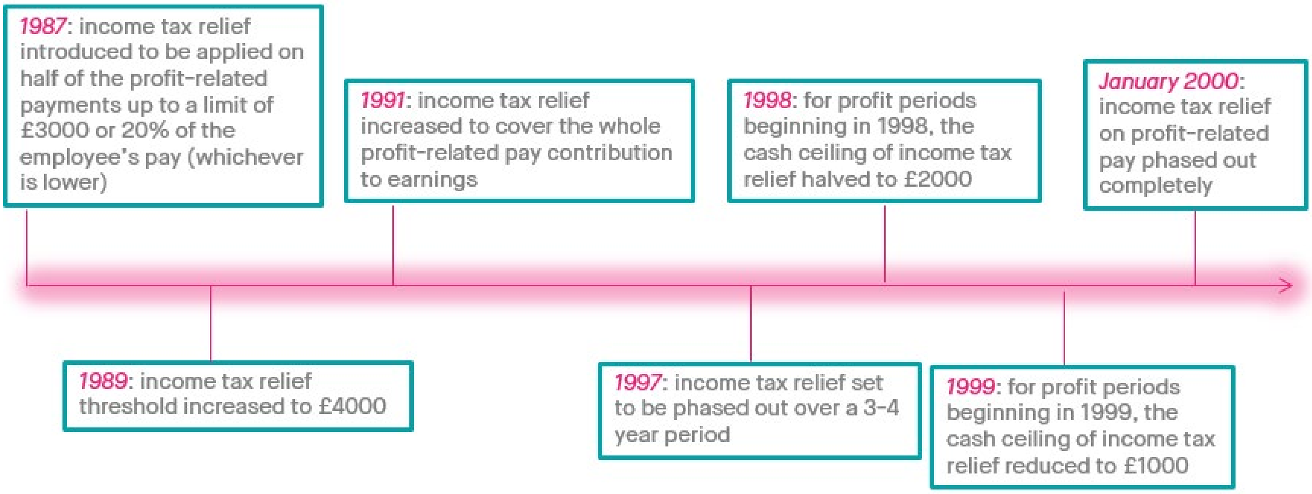


Source: National Archives

However, the size of the final tax break translated into employers offering PRP schemes mainly to take advantage of the tax relief, by finding ways to classify any kind of pay as profit-related.[86] As such, an overwhelming majority of PRP schemes were 'cosmetic' and had no impact on the behaviour of employees or employers.[87] Inland Revenue research from 1995 found that, without the tax breaks offered, at least one in three employers would not have incorporated profit-related payments to their wage bill.[88] Whilst tax efficiency was a significant incentive, employers cited employee involvement as the top motivator for offering a PRP scheme.[89] Improvements in productivity and pay flexibility were not commonly mentioned as perceived benefits.[90] Profit-related pay schemes, legible for tax relief, were also shown as contributing little towards maintaining employment stability amongst low-paid workers in small firms.[91]

Many businesses discontinued their PRP schemes after the tax allowance was phased-out in 2000, suggesting that the key reason profit-related pay was offered was to take advantage of the associated tax break. An estimated 60-70% of later PRP schemes were estimated to have been "salary sacrifices", where employees took a pay cut which was replaced with PRP[92]. A survey of FTSE-350 firms found that a third (36%) planned to abandon their profit-related pay arrangements following the removal of tax breaks, which would result in employees taking a pay cut of 6%.[93]

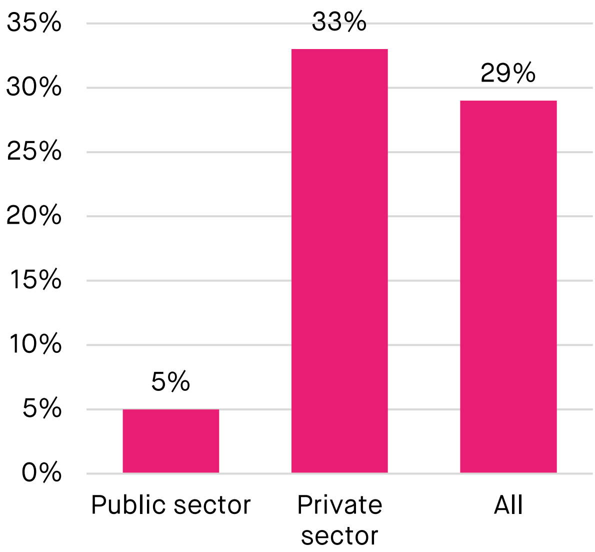
Figure 18: Profit-related pay in the UK (1987-2000)



Current prevalence of PRP among UK employers and employees

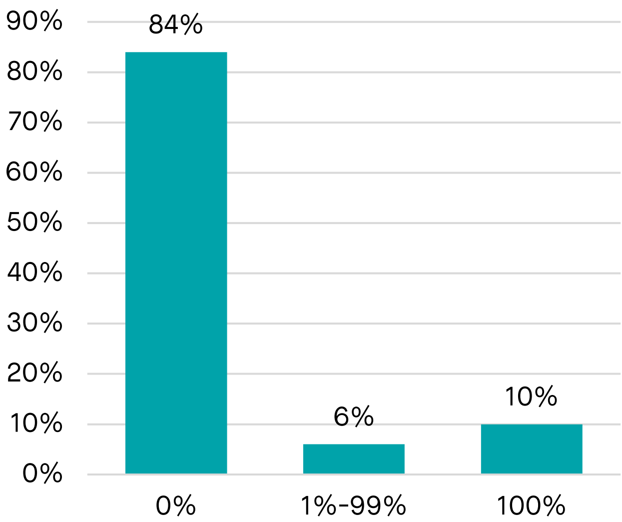
In 2011, three in ten (29%) of workplaces in the UK operated a profit-related pay scheme in the form of payments or bonuses.[94] Comparison over time shows that the proportion of workplaces offering profit-related payments has remained relatively stable since 2004. A majority of PRP schemes are offered and/or taken up by employees with managerial responsibilities. Looking at those employers who offer PRP schemes, our analysis shows that 10% offered a scheme to all workers, with an additional 6% of employers covering some non-managerial employees. The vast majority offered the scheme only to managers

Figure 19: Workplaces using any PRP incentive



Source: SMF analysis of WERS 2011

Figure 20: Within-workplace PRP coverage of non-managerial employees



Source: SMF analysis of WERS 2011

International practice and evidence

PRP in various forms is more common in some other advanced economies and are promoted by a range of policies. Below we describe practice in France, Germany and the United States of America.

Profit-related pay abroad

France

French legislation makes it mandatory for companies with 50 or more employees to offer a profit-sharing plan. Profit-sharing comes into effect once a company's annual profit has exceeded 5% of equity.[95]

Voluntary profit-sharing schemes are also commonplace, where bonuses are awarded against certain company performance indicators such as increases in productivity or lower rates of absenteeism.[96]

Compulsory and voluntary profit-sharing schemes are not mutually exclusive, however the amount of profit to be shared cannot exceed 20% of the total gross wage bill. The exact proportion of shareable profit is calculated annually using a legal formula, and is dependent on the company's equity, wage bill, and value added (and taxable profit).[97] The amount received per employee cannot exceed half of the assessment ceiling used in calculating the employee's social security contributions.

Distribution: Profit-sharing funds are eligible for income tax breaks. The money can be held in employee savings accounts, which are usually accessible after five years, or it can be made available immediately. A number of exemptions are in place which facilitate early access such as the employee getting married, having a child, or leaving the company.

Impact: Academic research has shown that the payment of profit-related bonuses to employees between 2000 and 2007 had no significant effect on total compensation of employees (between businesses which offer profit-sharing schemes to their employees and business which do not have such practices).[98] Several years after implementation of profit-sharing within firms, base wages are lowered, which is offset by profit-sharing bonuses.[99]

Germany

Profit-sharing in Germany is at an average level by international standards.[100] Schemes are not supported by government tax incentives and are mainly offered to boost the productivity of employees. The availability of profit-related pay schemes is largely dependent on the size of the firm and the industry in which it operates.

Take up: In 2007, 9% of all German firms offered a profit-related scheme to their workers.[101] This proportion rises to 36% among companies with 20 or more employees, and peaks at 70% in large firms with 2,000 or more workers. Employees in financial services and wholesale and retail trade had the highest rate of take-up of PRP (58% and 55%, respectively), compared to one in four (24%) of workers in the construction sector.

Distribution: Profit-related payments in Germany are more likely to be distributed in the form of an annual bonus rather than as a regular part of monthly pay. Only a minority (23%) of PRP schemes offered by firms with 20 or more employees were paid out monthly.[102] Additionally, only 18% of these schemes covered all employees in the organisation.[103]

Impact: Academic research shows that introducing a profit-sharing scheme positively affects profitability.[104] Additionally, profit-sharing participation has been linked to improvements in product innovation in the manufacturing sector.[105]

United States

Profit-sharing arrangements are not dictated by federal law in the US. Rather, payment of profit-related bonuses to non-management employees is at the discretion of the company and employment does not constitute an entitlement to such bonuses.

Profit-sharing plans fall in two broad categories: cash bonuses or deferred profit-sharing plans. Cash bonuses are usually paid out annually and are subject to income tax. In 2017, 6% of workers in the private sector had access to cash profit-sharing.[106] Deferred profit-sharing plans are not subject to immediate taxation as long as employees do not have easy access to these funds. In the private sector, money from deferred profit-sharing plans can be added to employees' defined contribution retirement plans. In 2015, 19% of private sector workers who had a defined contribution retirement plan benefited from deferred profit-sharing.[107]

Policy proposals

Sharing profits with workers could act as a strong political statement and it also has the potential to improve employer-employee relationships. Our analysis suggests that many low-paid workers are employed in firms that make a profit.

However, scheme design is extremely important and is likely to affect who benefits as well as the wider economic and social effects of the policy. Past experience indicates that real care is needed so that major drawbacks can be minimised or avoided.

Policy area 1: Encouraging firms to share profits with workers

We believe that a profit-sharing policy should be explored by Government with some headline principles in mind:

Principle 1: The policy should be designed specifically to encourage wide coverage amongst workers on low wages. As noted above, of the firms that offer PRP and schemes such as employee share ownership, many do so to managers but not to general staff.

Principle 2: Profit-related bonuses should be distributed among all workers, regardless of their pay level.

Principle 3: Incentives should be directed at the firm rather than the individual. There are multiple problems with tax incentives aimed at individuals. First, tax reliefs aimed at individuals are likely to skew take-up to higher earners: lower paid workers have less incentive to engage in the schemes because by definition they have less tax to be relieved on; such schemes rely on high levels of knowledge about tax relief. Second, we have seen above that income tax relief was also widely gamed in the past.

Options that the Government should consider for promoting participation include mandation (as in France) and tax incentives.

- **Principle 4**: PRP payments should not constitute part of earnings for the purpose of employers' compliance with minimum wage regulations. This would reduce the risk of substitution from wages to PRP and ensure PRP is additional. There remains a risk that employers reduce wages (or more likely reduce wage growth) among workers paid above the minimum wage to pay for PRP. However, this risk could potentially be reduced through clear labelling so that workers can see their wages and their PRP separately on their pay slips. This idea would benefit from testing through behavioural insights experiments.
- **Principle 5**: Consideration should be given to excluding PRP bonuses from the Universal Credit means-test assessment. There is otherwise a risk that PRP payments – if for instance paid as an annual sum – could interact damagingly with monthly Universal Credit assessment periods.
- **Principle 6**: Policy makers should consider promoting additional complementary measures to ensure that PRP is undertaken in combination with other worker engagement policies rather than on its own. This could include worker representation on boards which is not common practice in the UK. For instance, any tax incentives could be made conditional on introducing other policies. Such policies would have to be additional beyond the minimum requirements in The Companies (Miscellaneous Reporting) Regulations 2018.

CHAPTER 5: TAX INCENTIVES AS ROUTES TO PAY PROGRESSION

In this chapter, we explore how tax incentives could be used to influence the behaviour of businesses, including tax incentives for wage progression, increased training and regional tax policy.

Rationale for considering tax incentives

Governments use tax incentives for a wide range of policy goals. For instance, the UK Government uses tax incentives to encourage (to name but a few): capital investments that lead to energy savings; research and development; firms to locate in specific regions; and the employment of younger workers and apprentices. While the impact of tax reliefs varies significantly dependent on their design and their purpose, a review of R&D reliefs in OECD countries has concluded that R&D tax incentives are a useful tool to stimulate private R&D and increase the level of R&D.[108]

Particular issues that require consideration include: coverage of the tax – which businesses pay the tax and therefore might be influenced by the incentive; risks associated with adding complexity to the tax system; potential size of the incentive on firms; what condition needs to be fulfilled to earn the relief; the additionality generated by the policy and risk of deadweight (i.e. would firms be doing the activity anyway?); and, whether the policy would be open to being easily gamed by firms. We discuss these factors below.

Businesses pay a range of taxes including, but not limited to, Corporation Tax, VAT, business rates and National Insurance. Survey evidence suggests that adjusting the tax burden could be a powerful measure to incentivise small businesses to alter their behaviour. Along with competition, regulations and red tape and staff recruitment and skills, small businesses cite taxation, as the biggest obstacle to success.[109] This suggests that offering relief on tax could stimulate behavioural change.

Changes to corporate taxes to promote wage progression

Below we consider which businesses pay different taxes and could therefore potentially be incentivised by a relief, and how far employers of low-paid workers would be covered.

Corporation Tax

Corporation Tax (CT) is levied on profits. Since the financial crisis the rate of CT has reduced considerably from 30% in 2007/08 to 19% in 2019/20. The government has stated an ambition to cut the rate further to 17% in 2020.[110]

As CT is based upon the profits of the business it works as a proxy for productivity within the firm and therefore firms who pay increasing amounts of CT, should be offering their workers' pay increases. Evidence on the effectiveness of CT reductions as a mechanism for increasing wages is mixed, being more effective in countries where workers sit on company boards.[111] However, the UK could look to replicate the system used in Japan and make the CT reduction conditional on certain behaviours.

Case study: Japan tax incentives for wage increases

In April 2018, the Japanese Government introduced corporation tax reductions for firms who increase wages and invest in capital.

Companies who raise wages by 3% benefit from paying only 20% in corporation tax rather than 30%; these companies also need to boost investment in factories and equipment. The policy will be in place for three years from 2018. Companies in Japan have large cash reserves, as in the UK, and the hope is that this policy will encourage firms to use these reserves on wages and investment.

It is too early to see the full effect of the policy change; however, workers' real wages rose by 2.8% in June 2018 from a year earlier, accelerating from a 1.3% increase in May and marking the fastest pace of growth since January 1997.[112]

A conditional policy such as in Japan, could enable businesses to partially offset the cost of a wage increase through a lower CT liability. This could function as a straightforward relief, or the 17% CT rate could be reserved for firms that fulfil the requisite conditions.

Analysis in Chapter 4 suggested that a large number of low-paid workers are employed by firms that make profits and therefore pay CT, although there are likely to be many low-paid workers in firms that are not liable to pay CT. The distribution of CT liabilities is highly skewed, with fewer than 1% of companies paying more than 57% of the CT liabilities in 2016/17.[113] However, 82% of SME employers generated a profit in the last financial year.[114]

Business rates

Business rates are collected by local authorities from businesses who occupy non-domestic property. The amount charged is dependent upon the multiplier (a penny in the pound value), which is set by national government, and the property's 'rateable value'. If a business has a rateable value of below £12,000 it is exempt from paying business rates and if the value is between £12,001 and £15,000 the business is eligible for rate relief. Local authorities raised £23.8 billion from business rates in 2017/18. The government has announced that by 2020 local authorities will be able to retain all business rates that are collected locally.

Some local authorities are already offering business rate discounts to firms that pay the Living Wage. Such a policy therefore could be taken forward either nationally or locally.

Business rate reduction in London Boroughs

In 2015, Brent council became the first in the country to offer a scheme that allows business to benefit from business rate reductions as an incentive to pay the London Living Wage.[115] At the time of introduction, it was estimated that 30% of Brent residents were earning less than the Living Wage. The Council has promised to give a one-off discount on business rates to the first 100 local businesses who receive accreditation from the Living Wage Foundation. This discount is set at five times the accreditation fee paid to the Living Wage Foundation, with a maximum discount of £5,000 for large employers.[116]

When the scheme was proposed the Living Wage Foundation reported that the cost of the discount would be shared between central government (50%), the Greater London Authority

(20%) and Brent Council (30%). However, due to business rates devolution Brent Council now retains 64% of business rates and the current division of costs is unclear.

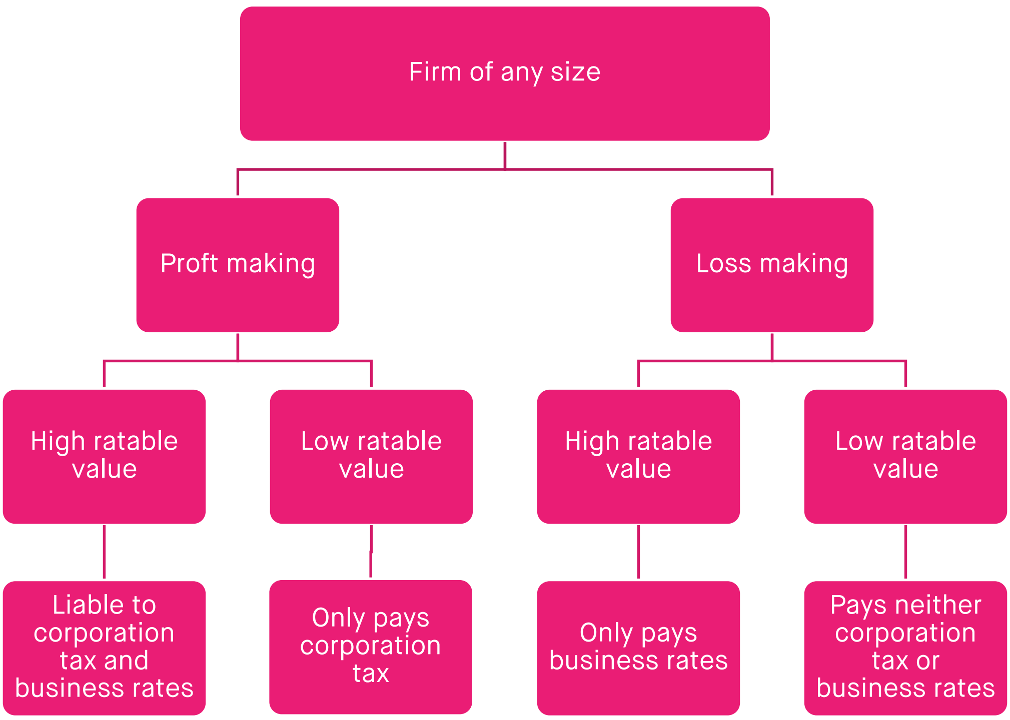
There are a range of boroughs in London that are now offering similar schemes, such as Greenwich and Ealing. Dundee City Council is seeking to become the first Living Wage City, through use of policies such as local accreditation and awareness raising.[117]

As of 2019, of the 31 Living Wage employers in Brent 22 have taken up their business rates discount, although it is not possible to infer that the scheme is effective as an incentive (we do not for instance know how many firms paid the Living Wage before the policy and we do not know how far the financial incentive influenced the employers' behaviours). The cost of the reduction totals £10,590. As a result Brent council has lost approximately £4,700 in rates income since 2014.[118]

The coverage of business rates is incomplete across the business population. Research conducted by the Centre for Cities suggests that across England and Wales 65% of properties are exempt from paying business rates, although a large number of such organisations may have no employees.[119] In some geographies a significant proportion of businesses do not pay business rates. This is particularly the case in deprived areas. For example, in Blackpool and Southend, where wages are known to be relatively low, fewer than 30% of properties are liable to pay business rates. Therefore, changes to business rates may not be effective as a national policy to promote higher wages or career progression for low-paid workers as there is a risk that in areas where there are very low property valuations the incentives would not be strong enough to translate into higher wages. This policy is likely to prove more effective in areas with high valuations, such as in London and other major cities.

Overview of Corporation Tax and business rate impact

Figure 21: Taxes payable based on business information



National Insurance

The policies above are centred around changes to taxation of property or profits. An alternative would be to reduce the National Insurance (NI) paid by employers. There is a precedent of using NI as a tool to incentivise the hiring of certain groups within the UK. For instance, in April 2015, the government removed the requirement to pay NI for workers under the age of 21 who earnt less than £3,863 per month. In April 2016, this scheme was expanded to cover apprentices under the age of 25 who were also earning under the £3,863 threshold. Both measures were implemented to boost youth employment, with a particular focus on the lower income groups who tend to be the most affected by youth unemployment.[120] While we know that Government has used this approach as a policy, there is currently no evaluation demonstrating its effectiveness.

In 2019-20, employers start to pay NI contributions for their staff if the staff member is earning more than £166 per week (equating to £719 per month or £8,632 per year). For those earning above the lower threshold of £719 and below the upper earnings limit of £962 per week, employers are eligible to pay 12% of their salary in national insurance contributions.

A potential benefit of using NI as the route to incentivise employers is that the amount payable is directly linked to the number of employees and their earnings rather than the profit or property valuation of the business, and all employers could theoretically be captured. However, as NI is only payable on earnings over £8,632 per annum, this policy would not necessarily act as an incentive for firms employing part-time workers. This is particularly problematic given the fact that part-time workers are at a higher risk of being in low-paid work than full-time workers and higher risk of being stuck in low pay. For instance, an organisation employing a worker earning at the National Living Wage (£8.21 from April 2019) would not be eligible to pay NI contributions unless they worked more than 20 hours a week.

Separately we know that part-time workers account for 57% of all low-paid workers in Britain. Just over a third (36%) of part-time workers are low-paid. This compares with 11% of full-time workers.[121]

Table 4: Advantages and disadvantages of different tax incentive methods

Tax method	Strengths	Weaknesses
CT tax reduction	Paid only by businesses who are making profit so does not penalise unprofitable firms. By choosing a policy based on profit we are selecting a set of business which should be able to raise wages.	Only payable by those making profit which could exclude several businesses with low-paid staff. There is a risk that a small percentage reduction in CT would only reduce the CT liability by a small amount per worker and therefore not act as a strong incentive to raise wages in the long term.

Business rate reduction	Applies to all firms (with rateable values above the threshold) and is not based on profits.	Due to low rateable values in some parts of the country the number of businesses who pay business rates is very low. There is a risk that it is the parts of the country where the businesses are exempt or receiving relief that are most in need of pay increases. Small businesses are likely to have small premises and therefore may pay very little business rates. Business rates are being localised, and a national scheme could run counter to this policy.
National Insurance reduction	The tax based solely on the number of staff and their wages rather than profits or the value of property.	Only payable on the salaries of those earning over £8,623. This reduces the number of workers captured by this policy and excludes the lowest paid in society.

As the table above indicates, all policies have limitations. For instance, NI would incentivise employers of full-time workers. However, the incentive would not bite for part-time workers working fewer than 20 hours a week. National insurance changes do not appear to target the workers most in need regardless of location or business profits and therefore it is not suitable as a mechanism to incentivise wage growth.

Existing evidence suggests that corporation tax is paid by a significant proportion of employers across all size bands and therefore we can theorise that this could be an effective method through which to incentivise higher wages.

The best approach is likely to be a series of pilots in different localities where different tax incentives are tested out. One additional variation that would be worth assessing is whether firms could be able to choose which tax incentive they apply for. We accept that this would be more complicated than offering a single relief. Not least because business rates are raised and (largely) retained locally by councils, whilst National Insurance and corporation tax are levied by central government. However, given the incomplete coverage of each individual relief, we believe that the concept would be worth further consideration. There is a clear trade-off between the complexity and coverage of the scheme, whilst offering businesses options increases complexity it also increases the number of individuals who would benefit from the scheme due to greater coverage and therefore may warrant the additional complexity.

Policy area 2: Tax reductions in exchange for pay rises

Our research indicates that there is scope to explore further the potential for using tax incentives to encourage firms to increase wage levels for low-paid workers. Whilst the tax incentive scheme in Japan is still in its early days, the initial evidence is positive and shows how firms may react to tax incentives when these incentives are designed correctly.

We propose that the Government pilot a tax incentive policy for firms to promote wage increases for low-paid workers.

No single tax would capture all employers of low-paid workers. However, corporation tax appears to have the best coverage and least unintended consequences. All companies have an incentive to put themselves in a position to make profits, and therefore to pay corporation tax. Our own analysis of which employers pay different business taxes has shown that many employers of low-paid workers pay corporation tax, although there are likely to be many firms that employ workers on low wages who do not make a profit in any one year. We note also a wider debate about the UK's business tax system and the fact that some firms pay a lower level of business tax than seems fair. This is important, though beyond the scope of this project.

It may be possible also to pilot offering a wider range of tax incentives which would capture a wider range of firms. Based on the evidence above and the coverage of different taxes, offering employers the option to select a reduction in corporation tax and business rates would enable a larger number of individuals to benefit from a wage change. This would obviously add significant complexity, but could potentially be trialled in a region.

Such discounts could be offered conditional on employers increasing the wages of lower paid workers who would not find their wages automatically increased through the NLW. Designing a scheme that drives wage progression out of low pay would be extremely complicated, especially as workers may move jobs and individual wage outcomes would have to be tracked over time.

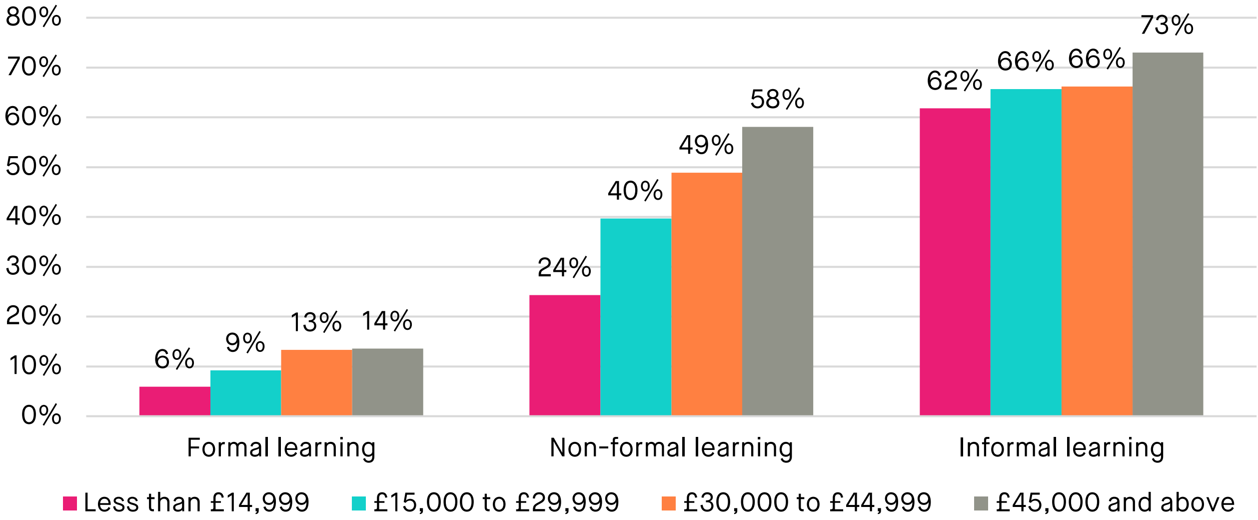
The design of the policy would require careful consideration to ensure employers cannot game the system by deferring annual wage increases before making an increase in wages that would entitle them to the tax relief, or by giving pay increases and then freezing pay (if the tax relief is time-limited).

Using tax to incentivise training

Most adult training occurs in the workplace. Whilst skills provision has undergone significant reform in recent years through the introduction of the Apprenticeship Levy, apprenticeships are not appropriate for all workers. In certain low-paid sectors, such as retail, apprenticeships have been shown to add little value.[122] However, wider evidence shows that training can boost wages including of lower-skilled workers.[123]

Those on lower earnings have the least exposure to training.[124] As Figure 22 demonstrates, there is a considerable difference between the amount of training taking place between the income groups, across all forms of learning. This could be attributed to different opportunities available within the workplace and / or employment status. Findings from the Adult Participation in Learning Survey show that when considering social grade, working status, highest qualification and age, all four variables are significant predictors of the likelihood of the participation in training.[125] The likelihood of participating in training increases as social grade and highest qualification increase and decreases as age increases. Compared with full-time employment, the likelihood of learning decreased for those in retirement or not seeking work.

Figure 22: Learning undertaken in the last 12 months, by net household annual income



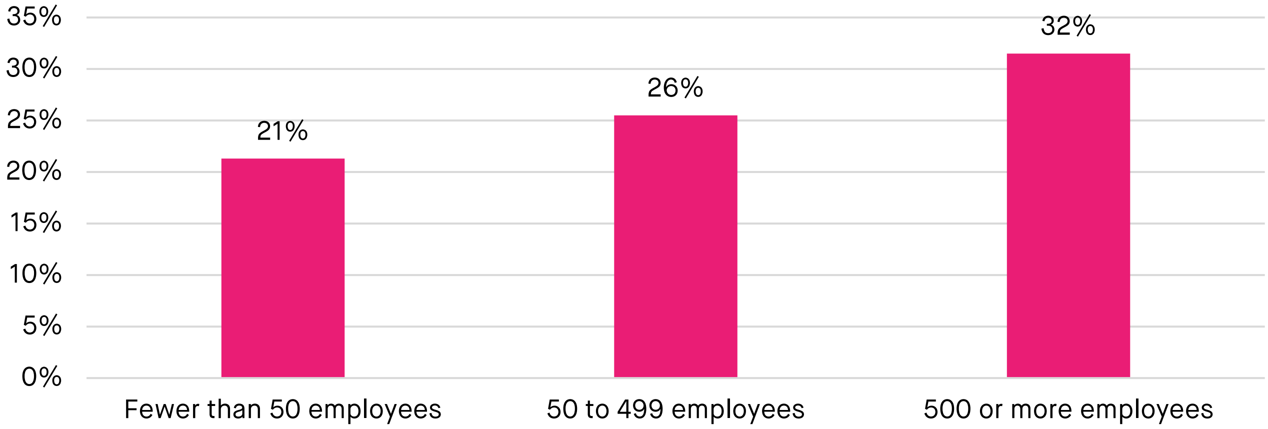
Source: Adult Education Survey 2016 (unweighted base: 8,822)
Note: Definition of training:

- *Formal learning: learning that is intended to lead to a nationally recognised qualification*
- *Non-formal learning: a course or taught class that does not lead to a nationally recognised qualification*
- *Informal learning: self-directed learning with the aim of improving knowledge of a subject*

In addition to the relationship between income and the likelihood of undergoing training, there is also a strong relationship between the size of the employer and training participation.[126] Approximately one in five (21%) of employees at small businesses (fewer than 50 employees) participated in training in 2017, compared to almost a third (32%) of employees at businesses with more than 500 workers.

Some firms might devote little time to staff training due to concerns that these will not translate into benefits for the organisation. For example, this might be the case if employees are expected to leave shortly after training takes place – in which case training would be a net cost to the employer. Other potential factors that may limit employer investment in training for lower-paid workers were discussed in Chapter 2. Together these factors motivate the case for more public investment in this part of the labour market.

Figure 23: Percentage of people who participated in training in 2017, by number of employees at workplace



Source: SMC (2019) LFS 2017 July – September quarter, people aged 25 to 64 in employment (weighted)

If workers at the lower end of the pay scale, particularly those working in smaller businesses, are often not able to improve their skills or to use training and qualifications as a signal for enhanced productivity, this could explain some of the poor pay progression.

Currently, employers that train their staff can already deduct the costs of training. However, this does not appear to be a strong enough incentive to encourage training provision for the lower paid. There have been multiple attempts by government to encourage the uptake of training in the UK.

Train to Gain (TTG) is one example of a government intervention that did not have the desired outcomes. The scheme offered subsidies to businesses who offered training to workers, a full subsidy was offered for individuals who undertook specific courses or qualifications and partial subsidies to other training paid for by employers. Unfortunately, the subsidy was often used to offset the cost of training that would have already occurred, with around half of employers who put their staff through TTG stating that they would have offered training without the subsidy.[127]

TTG and other schemes suggest that if additional subsidies are offered, policymakers need to be aware of the risk of deadweight loss and having a policy where the benefits are not passed to those most in need.

If financial support is targeted at low-paid workers, this reduces the risk of deadweight because we know that those on low wages are less likely to be offered and to undertake training. It does not eliminate the risk. Such a policy could also complement the Apprenticeships Levy, with recognition that not all workplace training is best undertaken through apprenticeships.[128]

Some other countries already offer tax incentives to increase the provision of training, often with additional incentives for smaller organisations.

International case studies

Netherlands

Prior to 2004, there were three tax deductions for work-related training: 1) firms were able to deduct 120% of training costs from turnover 2) an additional deduction for firms spending less than a specified amount (to target SMEs) 3) additional deductions for training provided to workers over the age of 40. The Netherlands has one of the lowest gaps in employer-sponsored training by firm size, for firms of 10-49 employees have a training participation is 36% compared to 42% for firms of over 1,000 employees. Evaluations of the scheme shows that whilst the scheme was widely used it did not appear to boost training to the desired levels, or impact wages. Deadweight losses (associated with firms of all sizes) coupled with fiscal pressures meant the scheme was terminated in 2004.[129]

Belgium

The Flemish regional government developed a fiscal incentive to encourage employers to train their workers. The scheme consisted of a property taxation reduction equivalent in size to the expenditure on training. The scheme was only open to employers who had a stable workforce and who had recently expanded their training expenditure and were from specific sectors. The deadweight loss associated with the scheme was estimated to be small based on the requirement that training expenditure had been historically poor but on the rise. The average number of training hours spent by small firms as a result of the scheme was greater than for the larger firms by 40%. The scheme was eventually cancelled as the scheme contravened EU regulations.[130]

Evidence from the UK and the international examples suggests that training-based policies can be effective but that there are risks about deadweight costs. There are also risks that employers engage in poor quality training in order to capture any subsidies, as with previous apprenticeships programmes.[131] This means receiving training in areas that are beneficial to them in their current career and their future development and targeting the policy so that groups such as low-paid workers benefit. These individuals are much less likely to receive training and therefore targeting the policy would help reduce deadweight costs.

Policy area 3: Tax incentives for training low-paid workers

Given the lack of access to training for lower paid workers, the Government should consider offering employers additional tax reliefs when they train low-paid employees.

Further testing with employers would be required to understand the most effective form of the tax incentive.

This could be taken forward as a policy on its own or as an additional conditional requirement for firms to be eligible for tax relief on top of wage increases for low-paid workers.

Regional tax policy

There is currently no analysis that assesses whether the concentration of low-paying industries locally affects the likelihood of progression out of low pay, whilst controlling for other factors. It is likely that such analysis would be extremely difficult to produce given the sample sizes of longitudinal datasets and comparatively local nature of labour markets for low-paid workers.

However, we believe that there are sufficient grounds to consider this phenomenon more closely. Chapter 2 showed that many areas and regions with a high quantity of low-paid staff have limited diversity of employment opportunities. This is likely to limit opportunities for pay and career progression for many workers in these areas, especially where the predominant sectors also typically have poor pay progression opportunities. For example, areas with a high concentration of retail & wholesale and accommodation & food services businesses often have a high proportion of low-paid workers. This includes coastal communities and areas in the North of England and the Midlands. These are also the areas with a considerable proportion of individuals stuck in the low pay trap.[132]

Targeting these localities with place-specific growth policies that incentivise higher paying employers to locate in these regions could result in better-paid job opportunities for low-paid workers in these areas. It is important to ensure that the entry of higher paying employers into an area translates into improved job opportunities for those living in an area, including through the provision of training and advice schemes which enable individuals to access better-paying jobs.

Another consideration is the need to ensure that new employers entering an area bring benefits to existing firms in the area – for example through purchasing local goods and services, and collaboration. International evidence suggests that, often, multinational firms incentivised to move to an area do not collaborate with local firms[133]. Such challenges could potentially be overcome through ensuring appropriate incentives are in place – for example through making tax breaks contingent on supporting the wider local economy.

A recent example of regional interventions is the reintroduction of Enterprise Zones (EZs) in England in 2012. The aim of this policy was to help rebalance the English economy. EZs offer a range of tax incentives (and other benefits) to encourage businesses to relocate or start up a business in a specific locality. Under the current policy the location of EZs were chosen based on nominations from Local Enterprise Partnerships, prioritising areas with little or no existing business occupancy.

Benefits include business rate reduction worth up to £275,000 over a 5-year period, 100% enhanced capital allowances (tax relief) to businesses making large investments in plant and machinery and simplified local authority planning, such as granting automatic planning permission for certain developments.[134]

Enterprise Zones in California

Enterprise Zones were introduced in California; however, they have since been repealed by legislation and replaced with a state-wide incentives programme. The EZs were created in areas of economic distress throughout the state and used special incentives to promote investment and the creation of new jobs within specific localities.

One of the most generous tax benefits associated with the Californian EZs is the ‘Hiring Credit’. The hiring credit is available for employers who hire workers with certain characteristics including, but not limited to, residents of targeted employment areas, welfare recipients, veterans and an ex-offender. A qualified business is able to reduce their state income tax by £7,440 per qualified worker over a five-year period.[135]

Very little evaluation of the scheme has occurred due to a lack of requirements on the state or its local zones. **Estimates suggest that the enterprise zone designation raises employment growth** by approximately **3 percent each year during the first six years after designation, but this effect does not persist in later years.** One study found that the number of employees at each business in an enterprise zone also rises more than employment at businesses that do not have the same tax incentives.[136]

Evidence from the 1980s suggests that EZs have positive outcomes for job growth and private investment. However, there is a considerable risk that EZs simply displace activity from one area to another. An evaluation of the UK's EZ policy from 2006 to 2011 suggests that employment increased within the zone but this came at the cost of comparable employment losses on the other side of the zone boundary.[137] Evidence from the French Empowerment Zones suggests that employment gains associated with area based initiatives are often only experienced within the short-run.[138]

Displacing activity from one geographical area to another is a clear risk with EZ policies. This can include displacement from localities nearby just outside the tax-advantaged boundary.[139] However, policy design can help mitigate this. There is evidence to suggest that the risk of displacement can be reduced by targeting the schemes to focus on tradeable sectors.[140] Meanwhile, locations may have to be chosen carefully. For instance, an area which had few high-paying firms just outside its boundary would be better protected against any damaging displacement activity in the policy we are considering.

A new regional tax incentive programme could be designed to build upon previous uses of employment and economic growth incentives. Through the establishment of Economic Growth Areas (EGA), businesses would be encouraged to relocate or start their business in areas where low pay is pervasive. It would be possible to require firms to train and hire local workers to benefit from tax incentives, and there is some evidence from France that local labour requirements can be effective[141]. This would help to ensure that the wages and opportunities available to local people are influenced through the establishment of the EGA. Under this scenario the burden of training would fall upon the employer, however this may work as a disincentive to relocate and hence the government may consider providing or subsidising the training of local workers.

We note that tax incentives, such as those provided in Enterprise Zones, are just one of a range of options for improving growth in a specific area. In some instances, alternative growth strategies – such as public sector investment in infrastructure – might yield greater benefits, highlighting the need to assess the relative merits of tax incentives versus other growth policies on a case-by-case basis.

Policy area 4: Tax incentives for employers in high paid sectors to locate in areas dominated by low-paying jobs

Our analysis suggests that there is an important geographic dimension to low pay that often gets overlooked: namely that opportunities for low-paid workers to progress their earnings and their careers may be particularly limited in some localities where the labour market is dominated by sectors that offer low-paid work and typically weak wage and career progression opportunities.

Introducing into the locality a wider range of better paid jobs could offer opportunities for both wage increases and career progression (by individuals moving into sectors that on average have better occupational mobility).

The report discusses the concept of 'Economic Growth Areas', which could be piloted by local authorities, city governments or national government. These would offer tax incentives to firms in higher paying sectors to relocate or start a business in an area where there is poor industry mix and where the economy is dominated by low paying sectors.

It may be beneficial to complement any such policies with additional training opportunities and advice opportunities for low-paid workers in these localities. It may also be beneficial to complement such policies with public investment programmes – such as investment in digital and transport infrastructure.

As a starting point, we suggest that MHCLG commissions exploratory analysis to determine whether it would be possible to carry out a convincing study into the impact of the concentration locally of specific sectors on the wage progression outcomes for low-paid workers.

ENDNOTES

[1] https://www.jrf.org.uk/report/uk-poverty-2017
[2] Resolution Foundation (2018), Low Pay Britain 2018
[3] Resolution Foundation (2017), "The Great Escape? Low pay and progression in the UK's labour market"
[4]https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/790910/20_years_of_the_National_Minimum_Wage_-_a_history_of_the_UK_minimum_wage_and_its_effects.pdf
[5] https://www.theguardian.com/society/2019/may/05/hammond-increase-minimum-wage-low-pay
[6] https://www.oecd.org/eco/outlook/Decoupling-of-wages-from-productivity-november-2018-OECD-economic-outlook-chapter.pdf
[7]https://www.google.com/search?q=donal+trump+tax+cut+swages&rlz=1C1GCEU_en-GBGB819GB819&oq=donal+trump+tax+cut+swages&aqs=chrome..69i57.34480j0j7&sourceid=chrome&ie=UTF-8
[8] See, for example, Resolution Foundation (2015), "Analysing the National Living Wage: impact and implications for Britain's low pay challenge"
[9] See, for example, http://www.ifn.se/wfiles/wp/Wp1105.pdf
[10] http://highpaycentre.org/blog/ftse-100-bosses-now-paid-an-average-143-times-as-much-as-their-employees
[11] Social Mobility Commission/Resolution Foundation (2014), "Escape Plan. Understanding who progresses from low pay and who gets stuck"
[12] IPPR (2015), "Employee Progression in European Labour Markets"
[13] Abel, Tenreyro and Thwaites (2018), "Monopsony in the UK"
[14] Benmelech, Bergman and Kim (2018), "Strong Employers and Weak Employees: How does Employer Concentration Affect Wages?"
[15] Krueger (2018), "Reflections on Dwindling Worker Bargaining Power and Monetary Policy"
[16] Krueger and Posner (2018), "A proposal for protecting low-income workers from monopsony and collusion"
[17] Shelkova (2014), "Low-Wage Labor Markets and the Power of Sugestion"
[18] Resolution Foundation (2018). "Is everybody concentrating? Recent trends in product and labour market concentration in the UK."
[19] Song et al (2016), "Firming Up Inequality"
[20] Aghion et al (2017), "Innovation, Firms and Wage Inequality"
[21] Schaefer and Singleton (2018), "Recent changes in British wage inequality: Evidence from firms and occupations"
[22] https://www.ft.com/content/2ea375d2-8c98-11e7-a352-e46f43c5825d
[23]https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/earningsandworkinghours/adhocs/004960annualsurveyofhoursandearningsashe2003to2015estimatesofweeklygrossearningsbyemployersizebanduk
[24]https://www.ons.gov.uk/economy/economicoutputandproductivity/productivitymeasures/articles/understandingfirmsinthebottom10ofthelabourproductivitydistributioningreatbritain/jantomar2017
[25] See, for example, https://europa.eu/sinapse/webservices/dsp_export_attachement.cfm?CMTY_ID=0C46BEEC-C689-9F80-54C7DD45358D29FB&OBJECT_ID=8FC3370C-9BF7-17EE-A62A0B68CADD629B&DOC_ID=C04B4D21-0381-B4F0-3494F9845049CFF4&type=CMTY_CAL
[26] Resolution Foundation (2018), *Low Pay Britain 2018*
[27] https://www.jrf.org.uk/report/uk-poverty-2018
[28] LPC, *National Minimum Wage Report* (2018)
[29] LPC, *National Minimum Wage Report* (2018)
[30] Social Mobility Commission and Resolution Foundation, *Escape Plan: Understanding who progresses from low pay and who gets stuck*, (2014)
[31] SMF (2017) "Living on the Edge: Britain's Coastal Communities"
[32] For more discussion of these factors see, SMF, *Back on Track* (2018)
[33] Resolution Foundation (2018), "Low Pay Britain 2018"
[34] Resolution Foundation (2017), "The Great Escape? Low pay and progression in the UK's labour market"
[35] https://www.resolutionfoundation.org/app/uploads/2017/10/Great-Escape-final-report.pdf
[36]https://www.ons.gov.uk/employmentandlabourmarket/peopleinwork/employmentandemployeetypes/articles/qualificationsandlabourmarketparticipationinenglandandwales/2014-06-18
[37] House of Commons, Women and the Economy (2019); https://www.ifs.org.uk/uploads/publications/bns/BN223.pdf
[38] SMF, *Back on Track* (2018)
[39] Resolution Foundation (2018), "Low Pay Britain 2018"
[40] https://www.resolutionfoundation.org/app/uploads/2017/10/Great-Escape-final-report.pdf
[41] https://www.disabilityrightsuk.org/news/2018/may/disability-pay-gap-increases-highest-level-2013
[42] https://www.resolutionfoundation.org/media/blog/the-3-2bn-pay-penalty-facing-black-and-ethnic-minority-workers/
[43] Hudson, M. and Radu, D. (2011) The Role of Employer Attitudes and Behaviour. York: Joseph Rowntree Foundation
[44] See, for example, Hudson et al. (2017), "Ethnicity and low wage traps: favouritism, homosocial reproduction and economic marginalization"
[45] SMF, *Making Progress* (2014)
[46] SMF, *Making Progress* (2014)

[47] SMF, *Making Progress* (2014); https://dera.ioe.ac.uk/14577/1/evidence-report-43-engaging-low-skilled-employees-in-workplace-learning.pdf
[48]S. Avram, S. Harkness, *The NMW/NLW and progression out of minimum wage jobs in the UK* (2018)
[49] House of Commons, *National Minimum Wage Statistics* (2018)
[50] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/785217/nmw-nlw-lpc-remit-2019.pdf
[51] Riley and Bondibene, *Raising the Standard: Minimum Wages and Firm Productivity* (2015)
[52] Croucher and Rizov (2012)
[53] Resolution Foundation, *Low Pay Britain* (2018)
[54] IPPR, *The missing pieces: Solving the UK's productivity puzzle*, (2015); John Forth and Ana Rincon Aznar, *Productivity in the UK's low-wage industries* (JRF, 2018)
[55]https://minimumwage.blog.gov.uk/2016/09/30/new-minimum-wage-rates-for-under-25s-why-are-they-different/
[56] Rani, Belser, and Ranjbari 2013
[57] LPC, *Report on the sub-minima rates of the national minimum wage* (2017)
[58] http://eprints.whiterose.ac.uk/93598/1/Harald%20Conrad%2C%20From%20Seniority%20to%20Performance%20Principle.pdf
[59] OECD, *Working better with age: Japan* (2018)
[60] https://www.ft.com/content/87586772-a600-11e4-abe9-00144feab7de
[61] Miyamoto and Higuchi (2007)
[62] https://www.gov.uk/agricultural-workers-rights/grades-and-categories
[63] Thomson Reuters report for the LPC, *The implications for the National Minimum Wage of the abolition of the Agricultural Wages Board in England and Wales*, (2011)
[64] http://www.oecd.org/employment/emp/Minimum%20wages.pdf
[65] https://www.minimum-wage.org/international/bolivia
[66]https://minimumwage.blog.gov.uk/2015/10/13/the-minimum-wage-for-younger-workers-why-is-the-level-different/
[67] Incomes Data Research, *The National Living Wage: employers' responses to the 2017 increase* (2017)
[68] LPC, *National Minimum Wage Report* (2018)
[69]LPC, *The National Minimum Wage, first report of the Low Pay Commission* (1998)
[70]LPC, *National Minimum Wage Report* (2006)
[71] LPC, *Report on the sub-minima rates of the National Minimum Wage* (2017)
[72] Low Pay Commission, *Non-compliance and enforcement of the National Minimum Wage*, September 2017
[73] Low Pay Commission, *Non-compliance and enforcement of the National Minimum Wage*, September 2017
[74] Low Pay Commission, *Non-compliance and enforcement of the National Minimum Wage*, September 2017
[75] See https://www.theguardian.com/politics/2018/sep/23/labour-private-sector-employee-ownership-plan-john-mcdonnell https://www.ft.com/content/4cad1c50-bf59-11e8-8d55-54197280d3f7
[76] Harvard Business Review, *Research: How Incentive Pay Affects Employee Engagement, Satisfaction, and Trust* (2017) https://hbr.org/2017/03/research-how-incentive-pay-affects-employee-engagement-satisfaction-and-trust
[77] https://www.managementtoday.co.uk/uk-prp-plus-turns-minus/article/410830
[78] Bell & Hanson 1984; Wadhwani & Wall (1990)
[79] Alex Bryson & Richard Freeman, *Doing the right thing? Does fair share capitalism improve workplace performance?*, Employment Relations Research Series No. 81 (2007)
[80] Ibid
[81] Harvard Business Review, *Research: How Incentive Pay Affects Employee Engagement, Satisfaction, and Trust* (2017) https://hbr.org/2017/03/research-how-incentive-pay-affects-employee-engagement-satisfaction-and-trust
[82] For a discussion of this literature see: Nigel Keohane, *Mutually Assured Growth: Employee ownership and the UK economy* (2013)
[83] John Forth and Ana Rincon Aznar, *Productivity in the UK's low-wage industries* (2018)
[84] Resolution Foundation, Low Pay Britain (2012)
[85] https://www.managementtoday.co.uk/uk-taxman-rescue-profit-related-pay/article/408985
[86] Martin Conyon & Richard Freeman, *Shared Modes of Compensation and Firm Performance: UK Evidence*, NBER Working paper No.8448 (2001)
[87] Penny Ciancanelli, Sonja Gallhofer, Jim Haslam & Robert Watson, *Profit Related Pay and the UK Small Firm Labour Market*, Small Business Economics Vol. 9, No. 3, pp. 225-238 (1997)
[88] As cited in https://www.accountancyage.com/aa/news/1752592/profit-related-pay-the-fatal-hour
[89] Ibid
[90] Ibid
[91] Penny Ciancanelli, Sonja Gallhofer, Jim Haslam & Robert Watson, *Profit Related Pay and the UK Small Firm Labour Market*, Small Business Economics Vol. 9, No. 3, pp. 225-238 (1997)
[92] https://www.managementtoday.co.uk/uk-prp-plus-turns-minus/article/410830
[93] https://www.managementtoday.co.uk/uk-prp-plus-turns-minus/article/410830
[94] BEIS, *The 2011 Workplace Employment Relations Study: first findings (fourth edition)* (2013)
[95] https://www.worker-participation.eu/National-Industrial-Relations/Countries/France/Financial-Participation/Basic-Data-on-Profit-Sharing-Employee-Share-Ownership#note2

[96]https://www.eurofound.europa.eu/publications/article/2014/france-study-finds-bonus-payments-have-no-effect-on-total-employee-remuneration
[97] http://www.afigec.com/data/en/pdf/24/profit-sharing-plan-in-france.pdf
[98] Noélie Delahaie & Richard Duhautois, 2015. "Profit-Sharing and Wages: An Empirical Analysis Using French Data Between 2000 and 2007," TEPP Working Paper 2015-03, TEPP
[99] Noélie Delahaie & Richard Duhautois, 2015. "Profit-Sharing and Wages: An Empirical Analysis Using French Data Between 2000 and 2007," TEPP Working Paper 2015-03, TEPP
[100] https://www.worker-participation.eu/National-Industrial-Relations/Countries/Germany/Financial-Participation
[101] https://www.eurofound.europa.eu/publications/article/2008/employee-financial-participation-in-companies
[102] https://www.eurofound.europa.eu/publications/article/2008/employee-financial-participation-in-companies
[103] https://www.eurofound.europa.eu/publications/article/2008/employee-financial-participation-in-companies
[104] Kornelius Kraft & Marija Ygarović, *Profit-sharing and the financial performance of firms: Evidence from Germany*, Economics Letters, Volume 92, Issue 3 (2006)
[105] Kris Aerts, Kornelius Kraft & Julia Lang, *Profit-Sharing and Innovation*, Centre for European Economic Research Discussion Paper No. 13-114 (2013)
[106] https://www.bls.gov/opub/ted/2017/38-percent-of-private-industry-workers-had-access-to-nonproduction-bonuses-in-2017.htm
[107] https://www.bls.gov/opub/ted/2016/74-percent-of-private-industry-workers-participated-in-saving-and-thrift-plans-in-2015.htm
[108] https://media.nesta.org.uk/documents/the_impact_and_effectiveness_of_fiscal_incentives.pdf; European Commission, *R&D tax incentives: How to make them most effective? Working Paper Series* (September 2017)
[109] Department for Business, Energy and Industrial Strategy, *Longitudinal small business survey 2017: SME employers* (2018)
[110] https://www.gov.uk/corporation-tax-rates
[111]https://theconversation.com/there-isnt-solid-research-or-theory-to-support-cutting-corporate-taxes-to-boost-wages-92031
[112]https://www.reuters.com/article/us-japan-economy-spending/japan-wage-growth-hits-21-year-high-signals-pickup-in-household-spending-idUSKBN1KR2GY
[113] HMRC, *Corporation Tax Statistics 2018* (2018)
[114] Department for Business, Energy and Industrial Strategy, *Longitudinal small business survey 2017: SME employers* (2018)
[115] https://www.livingwage.org.uk/news/brent-council-first-country-approve-new-business-rate-incentives-pay-living-wage
[116] https://www.brent.gov.uk/business/business-rates/how-to-reduce-your-business-rates/; http://brent.gov.uk/livingwage
[117] https://www.dundeecity.gov.uk/news/article?article_ref=3367
[118]http://democracy.brent.gov.uk/documents/s78440/15.%20Business%20Rates%20Relief%20Scheme%20for%20Businesses%20accredited%20with%20LWF.pdf
[119] Centre for Cities, *What do the coming business rates changes mean for cities?* (2017)
[120]https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/385150/TIIN_2143.pdf
[121] Resolution Foundation (2018), Low Pay Britain 2018
[122] Social Market Foundation, *Making apprenticeships work* (2019)
[123] SMF, *Making Progress* (2014)
[124] Department for Education, *Adult Education Survey 2016: research report* (2018)
[125] Department for Education, *Adult Participation in Learning Survey 2017* (2018)
[126] Social Mobility Commission, *The adult skills gap: is falling investment in UK adults stalling social mobility?* (2019)
[127] National Audit Office, *Train to Gain: Developing the skills of the workforce* (2009)
[128] SMF, *Making Apprenticeships Work* (2019)
[129] Enterprise and Skills Research Group, *Engaging small employers in continuing training: An international review of policies and initiatives* (2008)
[130] Ian Stone, *Encouraging small firms to invest in training: learning from overseas* (UK Commission for Employment and Skills) (2010)
[131] SMF, *Making Apprenticeships Work* (2019)
[132] Resolution Foundation, *The great escape? Low pay progression in the UK's labour market* (2017)
[133] https://blogs.lse.ac.uk/gild/2019/02/21/what-policies-work-for-fdi/
[134] https://enterprisezones.communities.gov.uk/about-enterprise-zones/
[135] https://www.foxconsultinggroupllc.com/services/ez/
[136] Suzanne O'Keefe, *Job creation in California's enterprise zones: a comparison using a propensity score matching model* (2003)
[137] https://voxeu.org/article/effectiveness-place-based-policies-uk-evidence
[138] IRES, *The efficiency of enterprise zone programs: some conflicting results?* (2013)
[139] https://voxeu.org/article/effectiveness-place-based-policies-uk-evidence
[140] https://whatworksgrowth.org/policy-reviews/area-based-initiatives/evidence-review/
[141] https://whatworksgrowth.org/public/files/Policy_Reviews/16-01-04-Area-based-initiatives-EZ.pdf