Title: Amendment to the National Minimum Wage regulations 2013-increase in NMW rates **IA No:** **Lead department or agency:** Department for Business Innovation and Skills (BIS) **Other departments or agencies:**	**Impact Assessment (IA)** **Date:** 08/04/2013 **Stage:** Final **Source of intervention:** Domestic **Type of measure:** Secondary legislation **Contact for enquiries:** Ricardo Bowman: 0207 215 3945

Summary: Intervention and Options

RPC Opinion: GREEN

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, One-Out?**	**Measure qualifies as**
£0.0m	-£1.8m	-£1.5m	Yes	IN

What is the problem under consideration? Why is government intervention necessary?

If there is exploitation in the labour market, employers may abuse unequal bargaining power to pay unacceptably low wages, particularly where workers have a lack of experience, skills, mobility or opportunities. The aim of the government intervention is to prevent this. The National Minimum Wage (NMW) is a statutory pay floor that sets the minimum wage standards in the UK. This provides protection to low-paid workers by preventing potential exploitation; prevents businesses from being able to undercut by paying exploitatively low wages; and provides incentives to work. The NMW came into force in April 1999 and since then the NMW rates have been reviewed by the Low Pay Commission annually.

What are the policy objectives and the intended effects?

The objective of the NMW is to provide as much support as possible to the wages of the low paid without damaging their employment prospects by setting it too high. The NMW sets a wage floor below which pay cannot fall ensuring protection for low-paid workers, while also providing incentives to work.

The Government stated in the Coalition Programme for Government (p23): "We support the NMW because of the protection it gives low-income workers and the incentives to work it provides."

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

The independent Low Pay Commission (LPC) was set up in 1999 to make recommendations on the NMW to Government. **In making its recommendations to Government, the LPC has consulted extensively and undertaken substantial analysis. Details are contained in its 2013 report.**

The Government has two options to consider:

1. Agree with all the LPC recommendations on NMW rates and implement the new rates
2. Reject all, or some of the LPC rate recommendations

The Government has concluded that the LPC's recommendations for the adult rate; the Development rate and the 16-17 year old rate are appropriate. For apprentices it has concluded that it is appropriate to increase the apprentice NMW (ANMW) by 1% (to £2.68) as opposed to a freeze as suggested by the LPC, combined with measures to improve compliance. It has, therefore, accepted the LPC recommendation to improve compliance but not the rate recommendation.

Will the policy be reviewed? It will be reviewed. **If applicable, set review date:** 03/2014

Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** Yes	**< 20** Yes	**Small** Yes	**Medium** Yes	**Large** Yes
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** N/A	**Non-traded:** N/A	

I have read the Impact Assessment and I am satisfied that (a) it represents a fair and reasonable view of the expected costs, benefits and impact of the policy, and (b) that the benefits justify the costs.

Signed by the responsible SELECT SIGNATORY: Jo Swinson Date: 6 June 2013

Summary: Analysis & Evidence — Policy Option 1

Description: Option 1 - Agree with all the LPC recommendations on the NMW rates and implement the new rates.

FULL ECONOMIC ASSESSMENT

Price Base Year 2012	PV Base Year 2013	Time Period Years 1	Net Benefit (Present Value (PV)) (£m)		
			Low:	**High:**	**Best Estimate:** £0.0m

COSTS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low				
High				
Best Estimate			£226.4m	**£226.4m***

Description and scale of key monetised costs by 'main affected groups'

Employers – as a result of increases in the adult and youth NMW rates, the wage bill for employers will increase by £194.5m and an increase in non-wage labour costs of £31.9m (a total increase in labour costs of £226.4m). Over 95% of these costs are direct costs to business but are out of scope of OITO.

*This cost burden on employers is associated with the removal of exploitation and some employers paying unacceptably low wages.

Other key non-monetised costs by 'main affected groups'

The evidence from the LPC report suggests that the NMW rates recommended by the LPC will not have a negative employment impact. This is discussed further in the evidence section. The LPC concludes in its report that its recommended NMW rates will not have a negative employment impact. This is discussed further in the evidence section.

BENEFITS (£m)	Total Transition (Constant Price)	Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low				
High				
Best Estimate			£226.4m	**£226.4m**

Description and scale of key monetised benefits by 'main affected groups'

Employees – adults and young people benefit from higher wages (£194.5m) as a result of these rates being higher than our counterfactual assumption of a wage freeze.

Exchequer and employees - benefits from increased non-wage labour costs as a result of increase in adult and youth NMW rates (£31.9m).

Other key non-monetised benefits by 'main affected groups'

Apprentices - apprentices benefit from training and employment prospects being protected by the freezes in the 2013 apprentice NMW (ANMW) rate. Employers who provide accommodation benefit from an increased amount that can be offset against NMW pay.

Exchequer – there will be benefits to the Exchequer from increased tax and National Insurance (from employees) and reduced benefit and tax credit payments as a result of changes in the adult rate.

Key assumptions/sensitivities/risks — **Discount rate (%)** N/A

Main assumptions can be found in the impact assessment. We assume that in the absence of changes to last year's NMW rates, the wages of the lowest paid would remain the same for the year beginning 1 October 2013. The proposed 2013 NMW rates involve transfers from employers to employees and the Exchequer. As this impact assessment involves an annual uprating the time period is one year.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: £0m	**Benefits:** £0m	**Net:** £0m	No	NA

Summary: Analysis & Evidence — Policy Option 2

Description: Option 2 - Increase the apprentice NMW (ANMW) rate by 1% to £2.68 and agree with all other LPC recommendations

FULL ECONOMIC ASSESSMENT

Price Base Year 2012	PV Base Year 2013	Time Period Years 1	Net Benefit (Present Value (PV)) (£m)		
			Low: £0.0m	**High:**	**Best Estimate: £0.0m**

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low			£227.9m	**£227.9m**
High				
Best Estimate			£228.3m	**£228.3m***

Description and scale of key monetised costs by 'main affected groups'

Employers – as a result of increases in the adult, youth and ANMW rates, the wage bill for employers will increase by £196.4m and an increase in non-wage labour costs of £31.9m (a total increase in labour costs of £228.3m). Around 96% of these costs are direct costs to business. However, only the wage costs related to increasing the Apprentice NMW rate are in scope of OITO.

*This cost burden on employers is associated with the removal of exploitation and some employers paying unacceptably low wages.

Other key non-monetised costs by 'main affected groups'

The evidence from the LPC report suggests that the NMW rates recommended by the LPC will not have a negative employment impact. This is discussed further in the evidence section and includes consideration of the effect that a 1% increase in the ANMW rate will have, rather than the freeze recommended by the LPC. We concluded that there is unlikely to be a significant adverse effect on apprentice employment or training. However, given the lack of evidence in this area this conclusion is uncertain.

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low			£227.9m	**£227.9m**
High				
Best Estimate			£228.3m	**£228.3m**

Description and scale of key monetised benefits by 'main affected groups'

Employees – adults, young people and apprentices benefit from higher wages (£196.4m) as a result of these rates being higher than our counterfactual assumption of a wage freeze.

Exchequer and employees - benefits from increased non-wage labour costs as a result of increase in adult and youth NMW rates (£31.9m).

Other key non-monetised benefits by 'main affected groups'

Employers who provide accommodation benefit from an increased amount that can be offset against NMW pay.

Exchequer – there will be benefits to the Exchequer from increased tax and National Insurance (from employees) and reduced benefit and tax credit payments as a result of changes in the adult rate.

Key assumptions/sensitivities/risks — **Discount rate (%)** N/A

Main assumptions can be found in the impact assessment. We assume that in the absence of changes to last year's NMW rates, the wages of the lowest paid would remain the same for the year beginning 1 October 2013. The proposed 2013 NMW rates involve transfers from employers to employees and the Exchequer. As this impact assessment involves an annual uprating the time period is one year.

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			**In scope of OIOO?**	**Measure qualifies as**
Costs: 1.5m	**Benefits:** £0.0	**Net:** -£1.5m	Yes	IN

Evidence Base (for summary sheets)

Problem under consideration and rationale for intervention

The aim of the National Minimum Wage (NMW) is to provide protection to low-paid workers by avoiding potential exploitation by employers who, in the absence of government intervention, could undercut competitors by paying unacceptably low wages; and also to provide incentives to work. The NMW came into force in April 1999 and since then the NMW rates have been reviewed annually by the Low Pay Commission. The aim when setting the rates is to increase the wages of the low paid as much as possible, while making sure that their employment prospects are not damaged by setting it too high.

The Government commissions an independent body, the Low Pay Commission (LPC), annually to recommend the appropriate NMW rates. Decisions on the NMW rates are made by the Government following consideration of these recommendations. As the decision on the appropriate NMW rates is an empirical one, the LPC report contains a large body of evidence and analysis on the impact to date of the NMW. The LPC considers the prospects for the UK economy by considering the latest available forecasts for growth, average earnings, inflation, employment and unemployment from the Office for Budget Responsibility and the median of the HM Treasury panel of independent forecasters. The Government also provides evidence on the labour market and policy developments. The evidence and data collected and produced by the LPC have been used to inform this IA.

As young people face a comparative disadvantage when entering the labour market, the LPC recommends separate NMW rates by age band (16-17, 18-20 year olds, 21 years and older). This primarily reflects the vulnerable position of younger workers who tend to have less work experience, less knowledge of where to look for work and fewer in-work contacts. A minimum wage therefore has more potential for negative employment effects for young people associated with increases in labour costs (the evidence shows that young workers experience substantially worse unemployment and employment rates than adults). Further, evidence suggests that young people tend to be more susceptible to economic cycles than adults [1]. The Government's agrees with the LPC which has consistently argued that young workers should be treated differently from their older counterparts in order to protect employment and at the same time reflect the training element attached to younger workers. The NMW structure therefore provides for lower NMW rates for workers aged below 21.

In October 2010, the Government introduced a new apprentice national minimum wage (ANMW) which applies to those apprentices who were previously exempt from the NMW (that is, apprentices who are aged under 19, or aged 19 or over and in the first year of their apprenticeship). This was to ensure that these apprentices received the legal protection of the NMW. There are costs to the Apprenticeship provider (costs of the training, the lower productivity during training and the opportunity cost of managing the apprentice at the workplace); and considerable gains to the individual apprentices through higher future earnings and increased employment prospects. The level of the ANMW should provide a fair deal for apprentices which protects them from exploitation whilst at the same time not deterring businesses from taking them on and providing training.

The LPC also makes recommendations for the value of the Accommodation Offset. The Accommodation Offset was introduced in 1999 and provides a mechanism to offset the cost of providing accommodation for workers against the NMW. Accommodation is the only benefit-in-kind that can count towards the NMW. The offset arrangements provide protection to workers and give some recognition of the value of the benefit, but are not intended to reflect the actual costs of provision.

Consultation

Within government

BIS has worked closely with HM Treasury to provide oral and written evidence to the Low Pay Commission[2].

---

[1] National Minimum Wage Low Pay Commission Report 2013

[2] https://www.gov.uk/government/publications/national-minimum-wage-final-government-evidence-to-the-low-pay-commission-2012

Public consultation

The LPC consulted a range of stakeholders including employee and employer organisations to recommend the 2013 NMW rates. A full list of those consulted and a summary of responses can be found in Appendix 1 of the LPC report.

Policy objectives

The NMW sets a wage floor below which pay cannot fall ensuring protection for low-paid workers, raising wages while also providing incentives to work. The aim when setting the rates is to raise the wages of the low paid as much as possible, while making sure that their employment prospects are not damaged by setting it too high.

Options identification

Options:

Option 1) Agree with all the LPC recommendations on NMW rates and implement the new rates

Option 2) Reject all or some of the LPC recommendations

The LPC in its latest report to the Government have recommended the following NMW rates:

Table 1. NMW rates from October 2012

Age band	October 2012 rate	LPC recommended rate for October 2013	Percent increase
Adult rate (for workers aged 21+)	£6.19	£6.31	1.9 %
Development rate* (for workers aged 18-20)	£4.98	£5.03	1.0 %
16-17 year old rate	£3.68	£3.72	1.1 %
Apprentice rate	£2.65	£2.65	No change

Source: Low Pay Commission.

The LPC has recommended rates for October 2013 after a wide ranging consultation and careful consideration of economic evidence and the impact on the employment prospects of low paid workers. The LPC's analysis is set out in their report.

The Government's preferred option is to agree with the LPC recommendations for the adult, development and 16-17 NMW rates but to reject the recommended freeze in the ANMW rate and increase it by 1% to £2.68. The analysis contained within this impact assessment is based on option 2. The total costs for option 1 are also presented as these are a subset of those for option 2. This is because under our agreed counterfactual (discussed further below), a freeze in the ANMW rate would generate no additional costs to business over the year assessed in this impact assessment.

Rationale for the Government's decision

The adult NMW rate

The LPC concluded that the adult NMW rate should be increased by 12 pence (1.9%). The aim of the increase is to maintain the relative position of the lowest paid in the earnings distribution while recognising that many workers – low paid and otherwise - are likely see reductions in their real earnings.

The LPC has also noted that the macroeconomic conditions in the UK are not vastly different from last year which is another reason why the adult rate recommendation is similar to last year[3].

The youth NMW rates

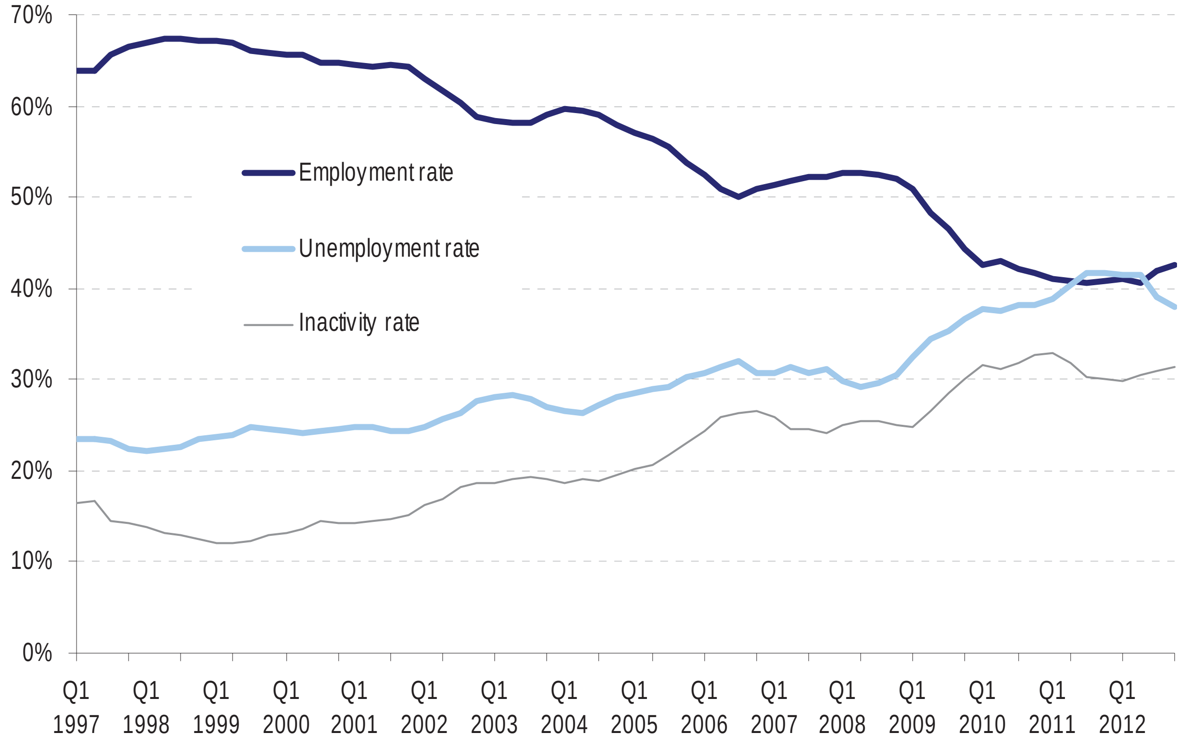
In the 2013 report, the LPC reiterates the findings from its 2012 report which suggested that the labour market position of young people had deteriorated over the recession. However, the 2013 report found that the labour market position of young people had stopped deteriorating and that there may have been some initial signs of improvement since 2012, although it is too early to tell whether this is the start of a long term trend. The LPC's view is that employment of young people is more sensitive than that of adults to the economic cycle which is one reason why the recommended increase of the youth rates is lower than that of the adult rate[4]. The LPC has recommended that the 16-17 year old rate should be increased by 4 pence (1.1%) and that the Development rate (18-20 year olds) should increase by 5 pence (1%) in October 2013.

Chart 1 and 2 below show the employment, unemployment and inactivity rates of young people excluding full-time students and graduates. Last year the LPC recommended a freeze in both the youth NMW rates due to the fact that the labour market position of young people had deteriorated. The charts below show that over 2012, the employment and unemployment rates may have begun to flatten out after having deteriorated during the recession.

The 1% increase in the youth rates is a moderate increase and is lower than the increase in recommended increase in the adult NMW rate of 1.9%.

Chart 1: **Employment, unemployment and inactivity rates of 16-17 year olds, excluding full time students and graduates**

Per cent of age group, four quarter moving average

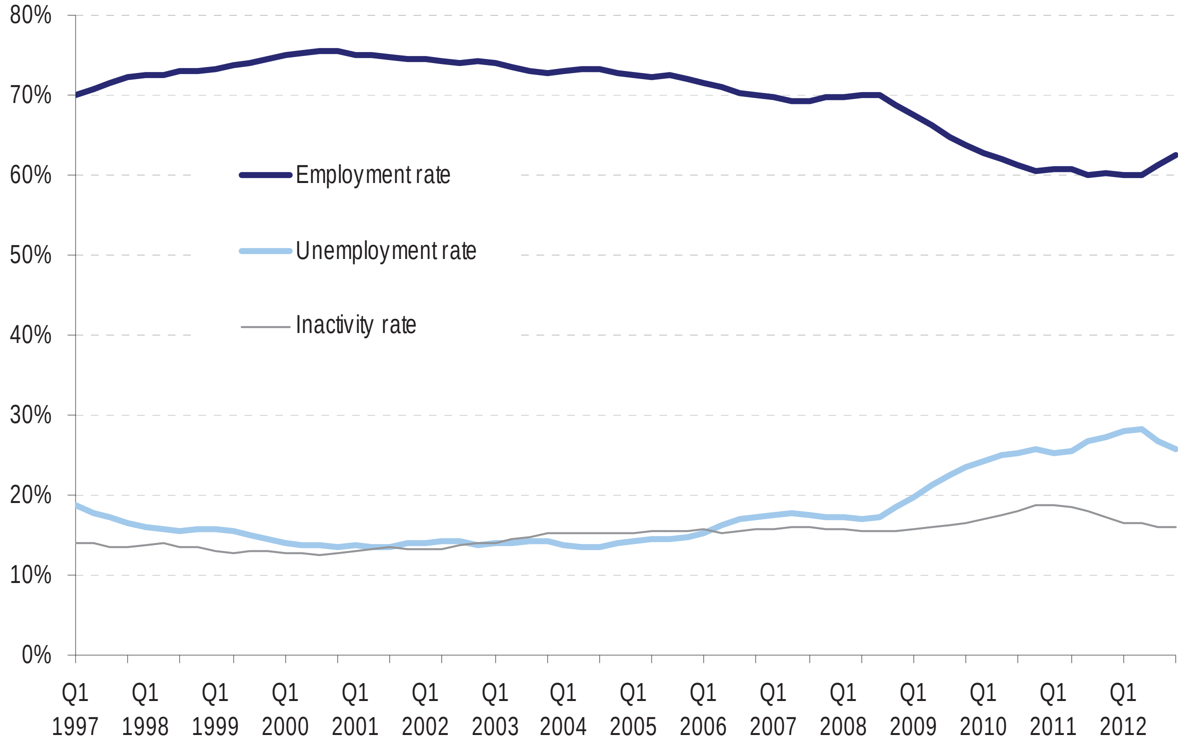


Source: BIS analysis of Office for National Statistics, Labour Force Survey. 4-quarter averages. Not seasonally adjusted.

[3] National Minimum Wage Low Pay Commission report 2013, page 166
[4] National Minimum Wage Low Pay Commission report 2013 page 166

Chart 2: **Employment, unemployment and inactivity rates of 18-20 year olds, excluding full time students and graduates**

Per cent of age group, four quarter moving average



Source: BIS analysis of Office for National Statistics, Labour Force Survey. 4-quarter averages. Not seasonally adjusted.

The Apprentice NMW (ANMW) rate

The LPC has recommended a freeze in the ANMW rate such that it should remain at £2.65[5] for two main reasons:

1. The LPC found that this year there has been a drop (of around 5,400) in under 19 Apprenticeship starts in England between 2010/11 and 2011/12. This is the first drop since 2008/09.

2. The LPC placed great weight on non-compliance with the ANMW in respect of young apprentices. Preliminary data from the 1st draft of the 2012 Apprentice Pay Survey (APS) for England and Wales (unpublished at time of their report) suggests that a relatively large proportion of young apprentices were being paid below the NMW rate - more than last year. The LPC notes that between 30 to 40% of apprentices aged 16-17 were estimated to be paid less than £2.65 per hour. For 18-20 year olds, the LPC notes that around 42% were estimated to be paid below their relevant NMW[6] rate (38% accounting for survey timing effects[7])[8]. The LPC notes that awareness of the ANMW and its annual review continues to be an issue for employers of apprentices as there is a suggestion that employers may have become non-compliant over time by not changing pay in line with NMW upratings or when apprentices progress on to the second year of their Apprenticeship[9]. The LPC also notes that non-compliance is more prevalent in certain sectors.

---

[5] National Minimum Wage Low Pay Commission report 2013 page 167

[6] Apprentices in this age group and not in their first year would be entitled to the Development NMW rate.

[7] The 2012 APS survey was conducted shortly after the 2012 NMW upratings occurred. It is therefore possible that the upratings were not registered by the respondents at this point. To compensate, hourly pay was also assessed against the 2011 NMW rates.

[8] National Minimum Wage Low Pay Commission report 2013 page 100

[9] National Minimum Wage Low Pay Commission report 2013 page 101

In their report, the LPC suggests that this level of non-compliance undermines the principle of the ANMW and that there is no point in raising the legal floor under apprentice pay if it is not in practice observed[10].

As well as the rate recommendation, the LPC has separately recommended that the Government should combine a communications campaign and a targeted enforcement initiative to ensure that the ANMW rate is known to employers and apprentices, and that infringers are caught, punished, and wherever appropriate, named[11].

The LPC also examined the effect of previous increases in the ANMW rate. The LPC noted that the ANMW rate has increased significantly since its introduction. However, it is important to note that there is some consensus that the ANMW rate was initially (in October 2010) set at a relatively low level. For instance the 2012 LPC report says: "…in 2010 we were prudent in our first recommendation for the Apprentice Rate…"[12].

It is also important to note that although there has been around a 4% decrease in Apprenticeship starts for 16-18 in England, this has not been the case for Apprenticeship starts for 19-24 year olds nor for Apprenticeship starts for ages 25+, which increased by 18,000 and 47,200 respectively over the same period[13]. The LPC report also shows that there were small increases in the number of under 19s starting Apprenticeships in Scotland and Northern Ireland in 2011/12[14].

After careful consideration, the Government's preferred option (option 2) is to reject the freeze of the ANMW rate and instead, increase it moderately by 1%, to £2.68 in October 2013.

The Government shares the LPC's concern about non-compliance with the apprentice minimum wage as employers must pay their staff at least the minimum wage. This is a key element to the Government's aim of making work pay and ensuring the success of the minimum wage. The Government has accepted the LPC's policy recommendation relating to enforcement of the ANMW and is stepping up compliance work in this area, including focused communications and targeted enforcement by HM Revenue & Customs.

As well as agreeing with the LPC recommendation that there needs to be a sustained effort on compliance with the ANMW, the Government agrees with the LPC's implicit view that there needs to be moderation on the ANMW rate.

Apprenticeships are central to the government's drive to raise skills and form part of the goal to support a stronger economy. The Government believes that our Apprenticeship programme delivers strong returns for the economy, employers and apprentices. The National Audit Office Report, published February 2012[15], demonstrates the very high level of return to investment delivered by the Apprenticeship programme, indicating that adult Apprenticeships deliver £18[16] of economic benefits for each pound of Government investment. The Department estimates that these returns are even higher, at £28 for each pound of Government investment. Because of this, it is important that Apprenticeships remain attractive to young people.

A freeze in the ANMW rate until at least October 2014 as recommended by the LPC could weaken the incentives for people who may be considering starting an Apprenticeship and for those already undertaking an Apprenticeship who are paid the ANMW rate. These people are more likely to be young

---

10 National Minimum Wage Low Pay Commission report 2013 page 167
11 National Minimum Wage Low Pay Commission report 2013 page 125
12 National Minimum Wage Low Pay Commission report 2012 page 149
13 Quarterly Statistical First Release, 31st January 2013: http://www.thedataservice.org.uk/statistics/statisticalfirstrelease/sfr_current/
14 National Minimum Wage Low Pay Commission report 2013 page 95
15 http://www.nao.org.uk/report/adult-apprenticeships/
16 This applies to 19+ apprentices – no figures available for 16-18 year olds, however we expect similar positive outcome for this age group

people as the Apprentice Pay Survey shows that young apprentices are paid less than older apprentices and further, that young apprentices are more likely to be on the ANMW than older apprentices.

The Government first announced in the Autumn Statement 2012 that it will increase most working age benefits by 1 per cent for three years from April 2013[17]. Therefore increasing the ANMW rate by 1% would approximately maintain its relationship with benefits as well as its relationship with both youth minimum wages (which would also be increasing by 1% under option 2)[18]. Such an increase in the ANMW rate would help to maintain the relative attractiveness of Apprenticeships to young people where the alternative is to seek normal employment or become unemployed and claim benefits.

As mentioned above, the LPC identified a fall in Apprenticeship starts in England for young people (under 19) for the first time since 2008/09. Table 2 below shows the proportion of Apprenticeship starts in England by age and data on vacancies and the proportion of applications for Apprenticeships by age from the National Apprenticeship Service (NAS) online vacancy matching service[19]. This service allows employers to advertise vacancies and individuals to register and apply for Apprenticeships online using the NAS's website. This online resource is one of a number of channels through which Apprenticeship vacancy matching can take place so does not capture the full picture and the results should be taken with caution. However, given the limited data in this area, this evidence is worth bearing in mind.

Looking at the number of under 19 Apprenticeship starts as a proportion of the total for all ages in England shows that this has decreased in 2010/11 and 2011/12 (see table 2 below). At the same time, the total annual number of vacancies[20] for Apprenticeships increased from around 43,000 to just over 100,000 in 2011/12. Furthermore, the proportion of candidate applications for Apprenticeships for under 19 year olds has decreased since 2009/10, while it has been increasing for over 19s.

This data may suggest that proportionately less younger apprentices have been applying for open Apprenticeship vacancies, despite the number of vacancies themselves increasing. One possible explanation for this could be that under 19s feel less incentivised to apply for Apprenticeships compared to older people and this could be driven by a low starting pay rate. An increase in the ANMW of 1% would help to maintain the relative attractiveness of the ANMW rate compared to benefits and the youth rates, especially for young people.

It is possible that an increase in the ANMW rate will reduce the demand for apprentices from employers, especially if this increase is above the competitive market price for apprentice labour. However, the increase in the ANM rate proposed for option 2 is moderate and although the evidence on the potential impact is unclear, we would expect any reduction in apprentice employment or training to be small. This is discussed further in the 'Costs and Benefits' section below.

It is important to consider this evidence in the wider context of the labour market and macro economy, especially since the evidence on apprentice pay and numbers is thinner than for the general economy.

---

[17] It is also important to note that public sector pay increases are capped at 1%

[18] Evidence in the LPC's report shows that the majority of apprentices paid on and just above the apprentice rate are young people

[19] https://apprenticeshipvacancymatchingservice.lsc.gov.uk/navms/Forms/Candidate/Apprenticeships.aspx

[20] Vacancies are not age specific

Table 2. Apprenticeship starts in England and vacancies and applications data for England from NAS online Apprenticeship vacancies service

Year**	2007/08	2008/09	2009/10	2010/11	2011/12
Apprenticeship starts	224,800	239,900	279,700	457,200	520,600
Under 19	47.9%	41.4%	41.8%	28.8%	25.0%
19-24	40.1%	35.3%	40.7%	31.4%	31.0%
25+	12.1%	23.3%	17.6%	39.8%	44.0%
Apprenticeship Vacancies	-	8,030*	43,010	70,880	100,970
Candidate applications for Apprenticeships	-	93,010*	292,090	477,430	513,790
Under 19	-	46.7%*	56.4%	54.4%	50.2%
19-24	-	35.2%*	31.1%	31.9%	35.4%
25+	-	18.0%*	12.6%	13.7%	14.4%

Sources: Quarterly Statistical First Release, FE and Skills: March 2013. And, Apprenticeship Vacancy Reports: http://mireportslibrary.thedataservice.org.uk/apprenticeships/apprenticeship_vacancy_reports/

* Only Dec 2008 – Jul 2009

** Year runs from August to July

The Accommodation Offset

The LPC reviewed the Accommodation Offset in their 2013 report. It found that the overall numbers and proportions in tied accommodation have decreased. However, the report concluded that there remains a strong rationale for an accommodation offset. The LPC recommended that the Accommodation Offset should remain as the only in-kind benefit that can count towards payment of the NMW and that there should only be one rate. The LPC recommended that the Accommodation Offset should increase from £4.82 to £4.91 in October 2013 (1.9%). This increase will maintain the Accommodation Offset's relative position to the adult NMW[21].

[21] National Minimum Wage Low Pay Commission report 2013 pages 121 and 166

Analysis of options

Table 3. NMW rates under option 2

Age band	LPC recommendations for October 2013	Option 2 NMW rates for October 2013	Difference
Adult rate (for workers aged 21+)	£6.31	£6.31	£0.00
Development rate* (for workers aged 18-20)	£5.03	£5.03	£0.00
16-17 year old rate	£3.72	£3.72	£0.00
Apprentice rate	£2.65	£2.68	£0.03

Costs and Benefits

In assessing the impact of the 2013 NMW rates, we need to establish what might have happened in the absence of government intervention. We make the counterfactual assumption that, in the absence of an increase in the NMW rates, wages for the lowest paid workers would remain unchanged. A fuller discussion of the counterfactual can be found below. **This counterfactual has been agreed within Government. It will be reviewed annually and agreed between BIS and the RPC in advance of the LPC making their NMW rate recommendations to assess if emerging evidence supports a different counterfactual.**

There will always be uncertainty surrounding the counterfactual as once policy intervention takes place we can never observe the outcome in the absence of Government intervention (we can only make inferences using appropriate evidence). It should be noted that the cost to employers is maximised by applying the rate freeze counterfactual. Therefore, the estimates provided in this IA represent an absolute upper bound estimate[22].

[22] Due to the evidence base and inability to observe the true counterfactual we take these estimates as our best estimate.

Box 1: real wage effects

The LPC has shown in their latest report that the real value of the NMW has fallen in recent years as the increase in the NMW rate has been lower than increases in CPI and RPI inflation. However, average earnings' growth has also been below inflation in recent years leading to a fall in real average earnings (see chart A1 in Annex 1).

Real wages combined with real non-wage labour costs is the real cost of labour that firms pay. When determining the balance of factors of production (capital and labour), a firm would tend to refer to real labour costs to determine how much labour they demand relative to capital. If real wages fall and real non-wage labour costs and the real cost of capital remain constant, in theory a firm would substitute away from capital and would employ more units of labour in its production process. This is because labour would have become relatively cheaper as a result of the real wage fall.

For 2013 the LPC has remained cautious, given that the economy is in a similar state to when it published its 2012 report – the recommended NMW rate increases for October 2013 are below the OBR's forecast rate of inflation. According to the OBR's forecasts, average earnings growth is set to remain below inflation until mid-2014, suggesting continued downward real wage pressures for the rest of the workforce.

The recommended increase in the NMW rate for adults for October 2013 is slightly below forecasts of average earnings annual growth to Q4 2013. However, the LPC notes that in the recent past, average earnings forecasts have tended to have been optimistic and that their previous rate recommendations have been more aligned with actual average earnings annual growth than the forecasts[23]. If it turns out that the 2013 rate recommendation is in line with actual average earnings over the same period, the rate increase would maintain the relative earnings of the lowest paid.

Since the introduction of the adult NMW in April 1999 and October 2012, the NMW rate has increased by more than average earnings, CPI and RPI inflation over the whole period. Between April 1999 and October 2012, the adult NMW rate has increased by around 72 per cent whereas growth in average earning over the same period was around 58.5 per cent[24].

It is important to note that the bite of the adult NMW (hourly minimum wage as a percentage of median hourly earnings) is currently higher than it has ever been. Therefore, although the recommended rise in the NMW rate is likely to lead to a small cut in the real wages of the lowest paid, it reflects what is happening to the broader labour market.

This impact assessment measures the costs and benefits in nominal terms.

The counterfactual

This impact assessment covers changes to the NMW regime through the proposed increases in the level of the NMW rates from 1 October 2013, as per option 2 outlined above. For the purposes of this impact assessment, the effect of the absence of government intervention would mean no changes to the existing NMW regime. There would still be a NMW (this impact assessment does not cover the overall policy of the NMW) but all the rates would remain at the level that is currently in force.

We assume that the lowest paid workers would have received a pay freeze in the absence of a NMW rate review. In terms of the remainder of the earnings distribution, we assume that workers who are paid above the statutory minimum will receive different wage increases in 2013.

The purpose of the NMW is to prevent the potential for abuse resulting from unequal bargaining power between employers and employees (for example, this could occur in uncompetitive labour market situations (of which one example is monopsony labour markets), which are discussed in more detail in Annex 5). We consider it is reasonable to assume that an employer who enjoys unequal bargaining

[23] National Minimum Wage Low Pay Commission report 2013 page 165
[24] National Minimum Wage Low Pay Commission report 2013 page 25

power would seek to maximise his profits and (in the absence of a statutory requirement to increase the wages of his employees), would not increase such wages.

Previous IAs have assumed that, in the absence of a NMW rate change, the lowest paid workers would have received an increase in wages in line with average earnings growth. The counterfactual used in this IA is the same as the one used last year for the October 2012 uprating of the NMW IA. There are a number of key reasons that support the use of this counterfactual. These are explored in more detail in Annex 1. However, the main arguments are briefly summarised below:

1. **The macroeconomy and the labour market** - The macroeconomic conditions in the UK are not significantly different to last year; price inflation is currently above average earnings growth and has been over the last few years; the NMW rate has increased faster than average earnings and inflation since its introduction.
2. **Evidence suggests that the NMW is binding on the labour market** – There is a spike in the earnings distribution at the NMW rate which moves to the new NMW rate each year; the 'bite' of the NMW has generally been increasing over time; NMW coverage has been increasing over time.
3. **The NMW is an established policy** - There is evidence that a number of employers track the NMW rate and may treat the NMW as the 'right' wage for the low paid; there is evidence that the NMW is influential in pay setting more generally.
4. **Uncompetitive labour markets** – The NMW aims to cover workers who could potentially be exploited through low wages by employers who have market power. In the absence of a wage floor in an uncompetitive labour market (for example a monopsony), employers would pay lower wages and employment would be lower. If there was a binding wage floor in a competitive labour market, there would be an increase in unemployment because employers would want to pay less for labour than the wage floor – the LPC has found no strong evidence of negative employment effects of the NMW.

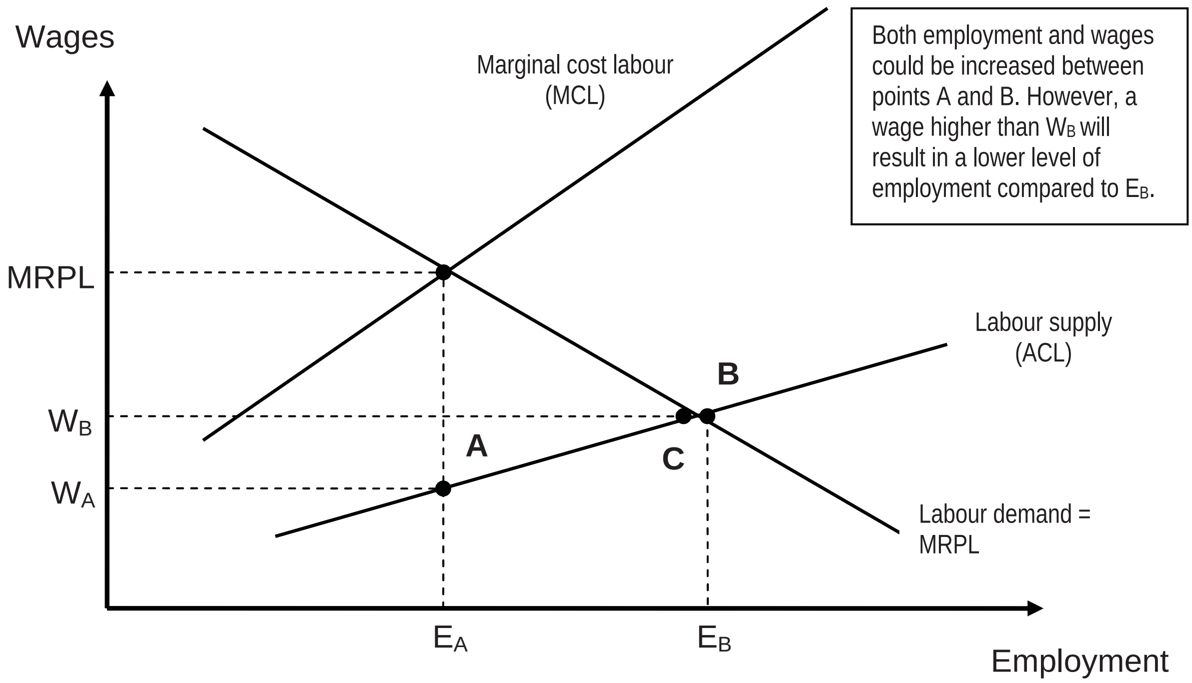
Costs and benefits

We assume that the lowest paid workers (NMW paid workers) have unequal bargaining power with their employer, and that without a NMW these workers would receive an unacceptable low wage. It is because of the NMW that these workers receive the NMW rates.

An increase in the NMW rate represents a transfer from employers (higher labour costs) to employees (higher wages). Leaving aside non-wage labour costs the wage element reflects a one-for-one transfer between employers and employees. This occurs because we assume no negative employment effects as a result of NMW policy decisions (this is discussed in more detail below). The transfer from employers to workers is as a result of mitigating potential exploitation of workers from low wages through a wage floor.

Adults – in the complete absence of a NMW workers would receive a wage of W_A (see figure 1 below). The introduction of the NMW and subsequent increases in the rate moves us to a point somewhere between A and B (for instance C). We don't know the precise location of C. The aim is for the NMW to get as close as possible to the market clearing wage for low paid workers and as this is achieved, point C will get closer to point B. The LPC's judgement is that we are now closer to B than we were in 1999. The LPC has taken a cautious approach during the economic downturn, attempting to mitigate negative employment effects and reduce the pressures on business. As a result, the LPC has recommended increases in the adult NMW rate that have turned out to be very close to actual average earnings growth. Forecasts for earnings growth have been optimistic over recent periods and the LPC recommendation for the adult rate for 2013 could be considered cautious in comparison to these.

Figure 1: A labour market characterised by market power for low paid workers



Young people – the argument is similar to adults although during the recession, it is more likely that the labour demand curve for young workers may have shifted inwards. If this happened to be the case, the distance between point C and B would become smaller. The LPC found that the labour market position of young people had stabilised over the last year. Further, the LPC concludes that in general the research that they commissioned demonstrated little effect of the NMW on young people. However, some evidence showed that NMW upratings had a negative impact on hours worked, particularly for young people during the recession[25]. Nevertheless, there is still uncertainty about the position of the NMW rate relative to point B, that is, whether a substantial NMW rate increase will result in a negative employment effect for young people.

Based on a counterfactual that wages of low paid workers would not increase without a rise in the NMW rates, there would be a cost to employers from the proposed increases in the adult and youth rates. This represents a transfer from employers to employees as the employees would gain an equivalent benefit of obtaining a wage increase which they would otherwise not have received.

Apprentices – Option 2 in this impact assessment is to increase the ANMW rate by 1% to £2.68 in October 2013. The LPC has recommended that there be no increase in the ANMW rate in October 2013 (option 1). As mentioned above, the LPC found that Apprenticeship starts in England had fallen in 2011/12 and further, that a significant number of young people in England and Wales were being paid below the ANMW rate. It is important to note that there were small increases in Apprenticeship starts for young people in Scotland and Northern Ireland and that there were significant increases in Apprenticeship starts for 19+ in England in 2011/12. Between its introduction in October 2010 and October 2013, the ANMW rate will have increased (under option 2) by 7.2 per cent (from £2.50 to £2.68). By comparison, the adult NMW rate will have increased by 6.4 per cent and the youth rates will have both increased by 2.2 per cent over the same period (including the 2013 uprating).

Based on a counterfactual that wages of low paid workers would not increase without a rise in the NMW rates, there would be a cost to employers from the proposed increases in the ANMW rate. This represents a transfer from employers to employees as the employees would gain an equivalent benefit of obtaining a wage increase which they would otherwise not have received.

[25] National Minimum Wage Low Pay Commission report 2013 page 104

An increase in the ANMW rate could also have an impact on the employment and/or the training prospects for apprentices. As mentioned above, a wage floor that imposes labour costs above the competitive market level can decrease employment. It is important to consider that for apprentices, another element of labour costs for employers is the provision of training and further, one of the key opportunity costs of employing an apprentice is the potential reduced productivity while they are training. With this in mind, an increase in labour costs due to an increase in the ANMW rate could mean that employers of apprentices reduce employment or hours worked of apprentices and/or reduce the quantity or quality of their training to offset the increased wage costs.

As mentioned above, the LPC identified a significant problem as regards non-compliance with the ANMW. This fact implies that there is a great deal of uncertainty around the scale of the potential employment and training impacts of increasing the ANMW rate. We estimate that the **additional** coverage of increasing the ANMW rate from £2.65 to £2.68 will be around 4,000[26]. The impact on employment and training will depend on the price elasticity of labour demand for apprentices. Although the own price elasticity of labour demand for apprentices is likely to be negative, it is likely to be relatively small, especially given that the LPC found in their 2013 report that pay is not the decisive factor in employers' decisions to take on apprentices[27]. Based on this, the number of people affected is highly uncertain but is likely to be small, given that the uprating only affects around 4,000 people. It is also important to consider that depending on the cross price elasticities of labour demand for apprentices with other forms of labour, there may be some substitution away from apprentices (in particular young apprentices) which may offset any reduction in labour demand of apprentices to some extent.

The Government has accepted the LPC's recommendation on compliance of the ANMW. The fact that compliance with the ANMW is likely to be improved over the course of the year means that estimates of the potential employment and training effects of an uprating are more uncertain. It is important to note that improving compliance could also lead to a decrease in employment and/or training.

The costs to individuals associated with reduced employment of apprentices include, decreased wages over the year and a reduction in human capital in the form of training relative to the counterfactual. A decrease in the employment of apprentices is unlikely to have any impact on the Exchequer as apprentices on the ANMW tend to earn less than the threshold for income tax and National Insurance Contributions (NICs).

The Apprentice Pay Survey is the main source of information on the degree of non-compliance. And it is likely that the scale of non-compliance is substantial. However, there is a great deal of uncertainty about the exact scale because of the nature and timing of the survey. In addition, there is little recent evidence on the adverse effect of the rate increase on employment and training of apprentices. Therefore, these impacts have not been quantified. However, given that our best estimate is that 4,000 people will be affected by the rate rise and real wage elasticities tend to be in the range of 0.5% to 3% it is unlikely that the effect will be large.

The NMW rates relative to median earnings

The aim of the LPC when recommending NMW rates is to have as high an increase in the minimum wage as possible without damaging low paid workers' employment prospects. When considering the impact on employment, the LPC considers the NMW rate as a proportion of median earnings or the "bite" of the NMW[28]. The adult bite has broadly been stable between 2007 and 2010 but has been increasing since then, reaching its highest level in April 2012. As mentioned above, research for, and analysis by, the LPC has not found significant evidence of negative employment effects as a result of the adult NMW. The LPC concluded that an increase which would roughly maintain the position of the lowest paid (although it would slightly lower the bite) is the largest increase that employers would pay without cutting jobs.

[26] From around 28,000 to 32,000. The increased coverage of the Apprentice NMW as a result of an uprating is discussed further below.

[27] National Minimum Wage Low Pay Commission report 2013 page 167

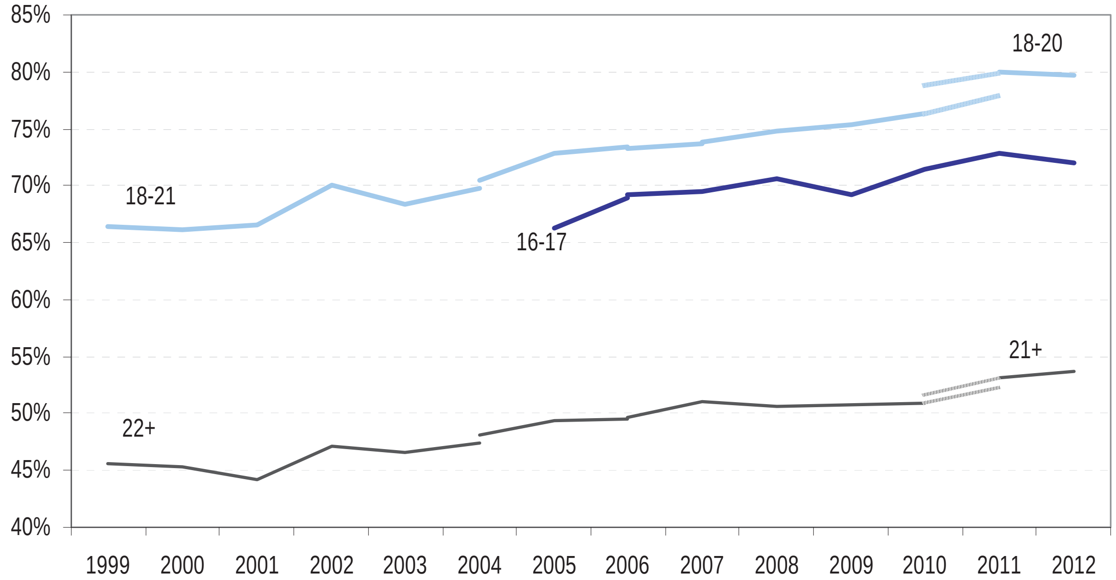
[28] The 'bite' of a minimum wage is a relative measure of its importance for a particular sector or demographic. For instance, a high minimum wage compared with the median wage in the UK is good for the relative position of minimum wage workers however it is more likely to affect their employment outcomes than a low bite

The bites of the youth rates relative to the median have been generally increasing over time, although in April 2012, the bite fell slightly due to relatively strong median earnings growth of young people. The labour market position of young people worsened over the recession, with employment of young people continuing to fall and unemployment to rise (although the extent to which pay is a factor is not clear). The LPC evidence suggests that the situation of young people may have stopped getting worse. However, the labour market position and the threat of unemployment is greater for younger workers than adults.

According to the initial findings from the first draft of the 2012 Apprentice Pay Survey, median hourly earnings of under 19 year old apprentices in England were £3.00. This means that the bite of the ANMW on this age group was 88.3%. The bite varied considerably by sector and was found to be 98.1% in hairdressing[29]. However, caution is needed in interpreting information from the survey and the results should be seen as indicative.

Chart 3: The bite of the NMW

Minimum wage as a per cent of median earnings



Source: Office for National Statistics, Annual Survey of Hours and Earnings. 1999-2004 ASHE data - excluding supplementary information 2004-2006 ASHE data - old methodology. 2006-2012 ASHE data - new methodology.

[29] Hairdressing is also found to have a high occurrence of non-compliance

Number of jobs covered by October 2013 NMW rates as at April 2014

In its 2012 report, the LPC estimated the coverage of the NMW upratings by deflating its recommended NMW rates for October 2012 to April 2011 (the reference month for ASHE 2011 data) using the OBR's average earnings growth forecasts. Using this deflated value, estimates were drawn from ASHE 2011 to give the coverage forecasts of the NMW rate recommendations at the time.

Due to the fact that the downrated value of the October 2013 rate recommendations are lower than the current value of the NMW when using the OBR's forecasts for average earnings, the LPC has not used the same methodology as last year to forecast the coverage of the recommended NMW rates. The table below presents the number of workers working at or below the NMW rates recommended for October 2013, in April 2012 from the LPC report[30]. These are based on ASHE 2012 data. Because of this change in the methodology, the estimates below are likely to be at the upper end of the range of coverage and may appear high compared to the estimated in last year's IA. Under this year's methodology, the coverage estimate for adults for last year's IA would have been 1.72 million people.

Table 4. Number of employees paid at or below the October 2013 National Minimum Wage by age (option 2)

Age group	October 2013 rates	Numbers covered
16-17 year old rate	£3.72	40,000
Development rate (for workers aged 18-20)	£5.03	173,000
Adult rate (for workers aged 21+)	£6.31	1,791,000
Total		2,003,000

Source: ONS' Annual survey of Hours and Earnings (ASHE). Figures have been rounded. Numbers may not sum to total due to rounding.

Because the LPC recommended uprating for the youth rates are lower than for the adult rate, the LPC does not expect a large increase in the coverage of the youth rates. The LPC expects it more likely that coverage for the youth and adult rates will decrease when compared to April 2012. Using ASHE 2012, the LPC has estimated that there are currently around 1.4 million NMW jobs.

It is not possible to distinguish between apprentices and non-apprentices from the ASHE data. Because of this, our methodology for estimating the coverage of apprentices for the ANMW uprating is to assume that all people earning at or below £2.68 from ASHE 2012 are people that will be covered by the ANMW uprating. Using this methodology BIS estimates that 32,000 people will be covered under option 2 – increase the ANMW rate to £2.68. Using the same method and assumption, according to ASHE 2012, there were around 28,000 people covered by the £2.65 ANMW rate in April 2012.

[30] National Minimum Wage Low Pay Commission report 2013 page 167

Cost and benefits of the proposed uprating of the Adult rate (21+)

The proposed changes to the October 2013 rates represent an increase of 1.9% on the current rate for adults.

Thus under our assumption that low pay wages would been frozen for low paid workers aged 21 and over in the absence of an uprating, the estimated cost impact of the 2013 adult rate is an increase in labour costs of **£212.6m for all employers (a direct impact on business of £203.6m).**

Adult employees benefit from increased wages (**£182.6m**). The Exchequer and employees will benefit from increased non-wage labour costs (**£30.0m**).

We have not monetised all the benefits to the Exchequer from increased tax and National Insurance revenues (from employees) and reduced benefit and tax credit payments as a result of changes in the adult rate.

We assume that there will be no negative employment effects from uprating the adult NMW rate as the aim of the LPC recommendations is to increase help as many low paid workers as possible, while making sure not to damage their employment prospects.

Methodology for estimating the cost to employers

The methodology for estimating the increased cost in the wage bill is as follows:

- We calculate the additional **weighted average**[31] hourly pay for those earning between the proposed rate and the rate that would have prevailed under the counterfactual. We multiply this average cost per hour by the average number of hours worked by those workers affected using the 2012 Annual Survey of Hours and Earnings (ASHE).

- Multiply by 52 weeks per year.

- Multiply by the number of potential workers between the proposed rate and the rate that would have prevailed under the counterfactual. We use 2012 ASHE[32] to estimate potential workers affected.

To go from the total wage bill to total labour costs, we add 16.4 per cent to take account of the cost to employers of National Insurance and any other non-wage labour costs (such as pension contributions)[33].

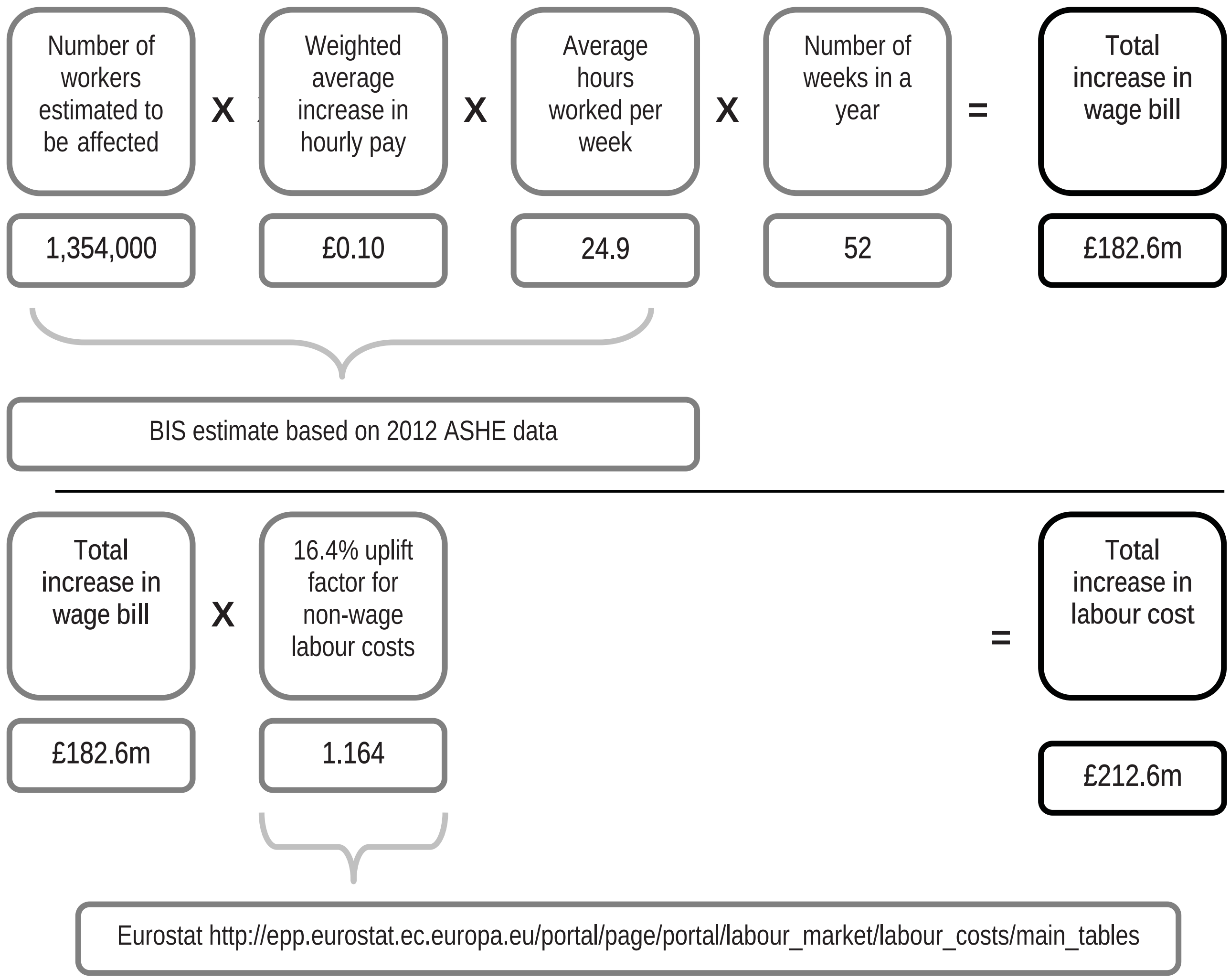
Our calculations for all rates can be found in figures 2-5 below.

[31] We use a weighted average as there will be some individuals that partially benefit by less than 12 pence (if they receive more than the old NMW rate but less than the forthcoming rate). Using a weighted average we estimate that on average individuals will benefit by 10 pence (this is lower than the 12 pence increase in the adult rate).

[32] The number earning at or below the proposed NMW in April 2012

[33] Source: Eurostat

Figure 2. Estimated increase in labour costs from increase in adult NMW rate from £6.19 to £6.31 (figures have been rounded*)



Source: BIS calculations. * Individual parts may not sum to total due to rounding. The estimated number of workers affected in figure 2 is a BIS estimate and this differs to table 2 which is a LPC estimate. Differences are due to slight variations in methodology.

Cost and benefits of the proposed uprating of 16-17 year old workers

The proposed changes to the October 2013 rates represent an increase of 1.1% on the current rate for 16-17 year olds.

Thus under our assumption that low pay wages would been frozen for low paid workers aged 16-17 in the absence of an uprating, the estimated cost impact of the 2013 16-17 rate is an increase in labour costs of **£2.3m for all employers (a direct impact on business of £2.2m).**

16-17 year old employees benefit from increased wages (**£2.0m**). The Exchequer and employees will benefit from increased non-wage labour costs (**£0.3m**).

We have not monetised all the benefits to the Exchequer from increased tax and National Insurance revenues (from employees) and reduced benefit and tax credit payments as a result of changes in the 16-17 year olds rate.

We agree with the LPC in assuming that there will be no negative employment effects from uprating the 16-17 NMW rate.

Figure 3. Estimated increase in labour costs from increase in 16-17 NMW rate from £3.68 to £3.72 (figures have been rounded*)

Number of workers estimated to be affected	X	Weighted average increase in hourly pay	X	Average hours worked per week	X	Number of weeks in a year	=	Total increase in wage bill
40,000		£0.04		25.7		52		£2.0m

Total increase in wage bill	X	16.4% uplift factor for non-wage labour costs	=	Total increase in labour cost
£2.0m		1.164		£2.3m

Source: BIS calculations. * Individual parts may not sum to total due to rounding. The estimated number of workers affected in figure 2 is a BIS estimate and this differs to table 2 which is a LPC estimate. Differences are due to slight variations in methodology.

Cost and benefits of the proposed uprating of 18-20 year old workers

The proposed changes to the October 2013 rates represent an increase of 1.0% on the current rate for 18-20 year olds.

Thus under our assumption that low pay wages would been frozen for low paid workers aged 18-20 in the absence of an uprating, the estimated cost impact of the 2013 18-20 rate is an increase in labour costs of **£11.5 for all employers (a direct impact on business of £11.1m).**

18-20 year old employees benefit from increased wages (**£9.9m**). The Exchequer and employees will benefit from increased non-wage labour costs (**£1.6m**).

We have not monetised all the benefits to the Exchequer from increased tax and National Insurance revenues (from employees) and reduced benefit and tax credit payments as a result of changes in the 18-20 year olds rate.

We agree with the LPC in assuming that there will be no negative employment effects from uprating the 18-20 NMW rate.

Figure 4. Estimated increase in labour costs from increase in 18-20 NMW rate from £4.98 to £5.03 (figures have been rounded*)

Number of workers estimated to be affected	X	Weighted average increase in hourly pay	X	Average hours worked per week	X	Number of weeks in a year	=	Total increase in wage bill
173,000		£0.05		24.3		52		£9.9m

Total increase in wage bill	X	16.4% uplift factor for non-wage labour costs	=	Total increase in labour cost
£9.9m		1.164		£11.5m

Source: BIS calculations. * Individual parts may not sum to total due to rounding. The estimated number of workers affected in figure 2 is a BIS estimate and this differs to table 2 which is a LPC estimate. Differences are due to slight variations in methodology.

Cost and benefits of the apprentice rate

An apprentice minimum wage of £2.50 was introduced 1st October 2010. This applies to apprentices aged under 19 and those aged 19 and over in their first six months of their Apprenticeship. This rate was increased to £2.60 in October 2011 and £2.65 in October 2012. Option 2 is to increase the ANMW rate by 1% to £2.68.

BIS estimates that around 32,000 apprentices stand to benefit from the increase in the ANMW rate and that it will **cost employers £1.9m (a direct impact on business of £1.8m)** in increased wage bills. This represents a transfer and will **benefit apprentices by £1.9m** in the form of increased wages.

The methodology for estimating the increased cost in the wage bill is as follows:

- Using ASHE 2012 data we estimate that around 32,000 individuals earn at or less than the £2.68 per hour ANMW rate proposed by option 2. We assume that all these people are apprentices. Given these small numbers we assume all of the apprentices affected will benefit from a 3p pay rise per hour.

- We multiply the above by **38 hours** worked per week (the average hours contracted to work by apprentices on the ANMW in 2011[34]).

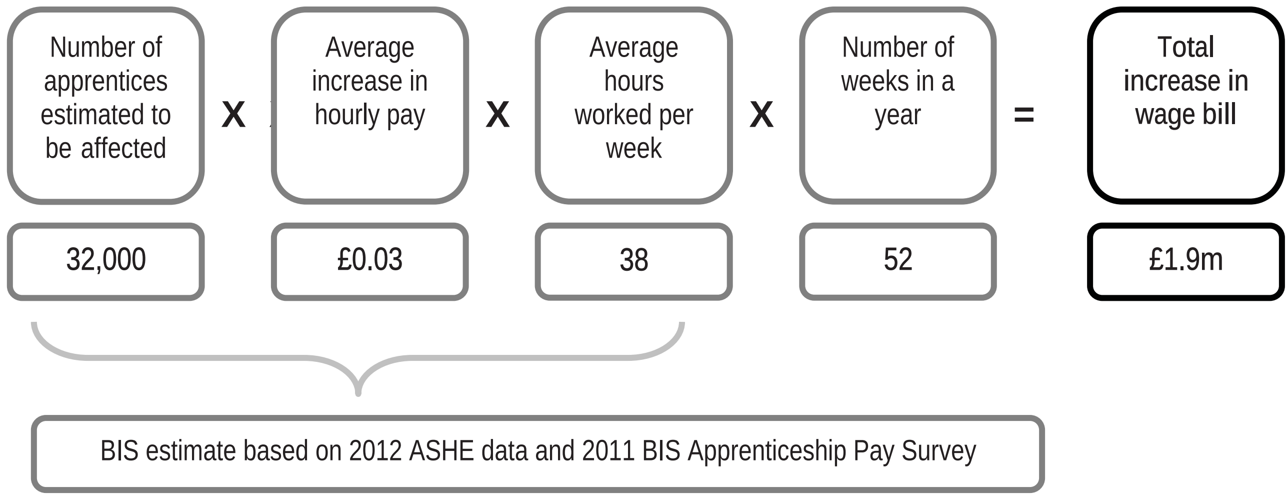
- Multiply by 52 weeks per year.

Unlike adults we assume no change in non-wage labour costs as the total apprentice weekly pay is tends to be below the point at which employers start paying National Insurance contributions.

Our calculations can be found in figure 5 below.

[34] Source: Apprenticeship pay survey 2011 data

Figure 5. Estimated increase in wage bill from increase in ANMW rate from £2.60 to £2.65



Source: BIS calculations. Figures have been rounded.

In order to make our coverage estimate of 32,000 we have assumed that all individuals counted by ASHE earning at or below £2.68 are apprentices. This is because, using ASHE, it is not possible to distinguish between whether an individual is an apprentice or not. Due to this assumption, there is less certainty around the coverage estimate for apprentices than for the other NMW rates. Because it is feasible that some of the people we have considered to be apprentices are not, we have assessed a sensitivity in which the coverage of the uprated ANMW is 20% below our best estimate. In this scenario, coverage is estimated at 25,600 and the total increase in labour costs as a result of the uprating of the ANMW rate is £1.5m. The net benefit of this scenario is the same as for our central estimate (zero).

As discussed above, there could be a decrease in the employment or hours worked of apprentices and/or a reduction in the quantity or quality of training as a result of uprating the ANMW rate. We expect the adverse impact on employment to be small. However, due to the uncertainty associated with these impacts, we have not monetised them.

Cost and benefits of the proposed uprating of the Accommodation Offset

Accommodation is the only benefit in kind that can count towards NMW pay and only up to the Accommodation Offset limit. The NMW Accommodation Offset was introduced with the intended purpose of protecting vulnerable workers whose employers might have sought to avoid paying their workers the NMW by levying excessive rent for their accommodation. The LPC found no reason this year to adjust the offset relative to the minimum wage.

The proposed change to the NMW Accommodation Offset is an increase from £4.82 in October 2012 to £4.91 in October 2013. This represents an increase of 1.9%. The Accommodation Offset is a benefit to employers as it allows them to offer a greater amount in benefits in kind to workers. We have not monetised this benefit as it is very uncertain how many employers offer accommodation to workers. An example of where the Accommodation Offset applies is where an individual works in a hospitality establishment such as a pub and lives above the commercial premises. If their accommodation is also owned by the same business that operates the pub the Accommodation Offset applies.

Risks and assumptions

This impact assessment is based on the best evidence base available and a set of necessary assumptions which are subject to uncertainty.

In assessing the impact of the 2013 NMW rates we have made the assumption that, in the absence of the uprating, wages for the lowest paid workers would not have changed in the year beginning 1 October 2013. However, if our counterfactual is incorrect – and the lowest paid workers would have received a wage increase in the absence of a statutory requirement to do so - this could lead to an overestimate of the costs and benefits. (The costs would never be underestimated as employers paying at the NMW could not reduce wages below the already existing NMW rates.)

We have not considered any potential displacement effects of possibly making younger workers relatively more attractive to adult workers given that the recommended increases in the youth NMW rates are smaller than that of the adult rate. With the current evidence base any estimate would be subject to great uncertainty. The LPC commissioned research for their 2013 report that looks at the substitution rate of young workers and adult workers. Lanot and Sousounis (2013) found some evidence that workers aged 18-21 years old were substantial, if not perfect complements to workers aged 55 or older. This suggested that the minor changes to the differences in the NMW between age groups since the introduction of the NMW had not affected the composition of the work force. Fidrmuc and Tena (2013) examined the impact of the NMW on employment and hours of young workers. They found some negative employment effects of the NMW for young men, a year before they became entitled to the adult rate[35].

We have assumed that there are no negative employment effects of uprating the adult and youth NMW rates. The 2013 LPC report concluded that, given the strong labour market performance of low paying sectors and the findings from their commissioned research, on balance there is no strong evidence of negative employment effects of the NMW. The LPC's remit is to recommend NMW rates such that the employment prospects of low-paid workers are not damaged and their recommendations are based on a thorough body of evidence. Therefore, we believe that making such an assumption is justified. If there were to be negative employment effects of uprating the NMW, the quantified impacts would be uncertain. We have not made the same assumption for the uprating of the ANMW rate in option 2.

Due to lack of available data that precisely estimates the number of apprentices covered by the October 2013 rate under option 2 or option 1, we have had to make a simplifying assumption. Using April 2012 ASHE data we make the assumption that everyone earning at or below the October 2013 ANMW rate is an apprentice. We have also tested scenarios in which the coverage is 20% below our central estimate.

With employment levels unaffected by the adult minimum wage uprating, any knock on savings to the exchequer via increased tax take and/or reduced support benefits would be transfers and will not affect the NPV. Therefore, we have not fully monetised all the impacts on the exchequer. For further info, please see LPC Report 2013[36].

Enforcement

The NMW is enforced by HM Revenue and Customs (HMRC). HMRC respond to complaints about workers not be being paid the NMW. They also visit employers identified through risk assessment. Individuals may also make a complaint to an Employment Tribunal that their employer has not paid them the NMW. Employers found to have underpaid their workers NMW are required to pay arrears (at the current NMW rates) to their workers and may be subject to a penalty. The Government accepts the LPC's recommendation that the Government should combine a communications campaign and a targeted enforcement initiative to ensure that the ANMW rate is known to employers and apprentices, and that infringers are caught, punished, and wherever appropriate, named[37].

---

[35] National Minimum Wage Low Pay Commission report 2013 page 91
[36] National Minimum Wage Low Pay Commission report 2013 page 169
[37] National Minimum Wage Low Pay Commission report 2013 page xvii

There is no change in the cost to the Exchequer of enforcement due to the upratings of the various NMW rates.

Summary of preferred option

Table 4 represents a summary of option 2 (agree with the LPC recommendations on the adult and youth NMW rates; reject the LPC recommendation on the ANMW rate and instead increase this by 1%).

Table 5. Summary costs and benefits of option 1*

Age band	October 2013 rate	Employers	Employees
Adult rate (aged 21+)	£6.31	Higher labour costs	Higher wages for employees (benefit)
Development rate (aged 18-20)	£5.03	Higher labour costs	Higher wages for employees (benefit)
16-17 year old rate	£3.72	Higher labour costs	Higher wages for employees (benefit)
Apprentice rate	£2.68	Higher labour costs	Higher wages for apprentices (benefit)

Source: BIS. *Exchequer benefits from some of the increase in non-wage labour costs from employers (some of the non-wage labour costs will be accrued by the employee), increased tax and National Insurance revenue (from employees) and reduction in benefits and tax credits as a result of changes in the adult NMW rate.

Implementation

The changes to the NMW regulations would be made by secondary legislation and would be expected to come into force on 1 October 2013.

"One in, two out" rule

Implementation by the Government of LPC rate recommendations falls out of scope of the 'one-in two-out' (OITO) rule whereby no new regulation can be brought in without other regulation being removed. Therefore, under option 1 all direct costs to business are exempt from OITO. Under option 2, the direct costs to business associated with the uprating of the adult NMW, the 18-20 NMW and the 16-17 NMW are exempt from OITO. However, the direct cost to business of rejecting the LPC recommendation to freeze the ANMW rate and instead increase it to £2.68 falls within the OITO rule.

In order to calculate the direct costs to business, using 2012 ASHE data, 95.8% of low paid workers (earning at or below the NMW) worked in the private sector. We take 95.8% as the percentage impact on business. The appraisal period has been set at one year as the NMW is reviewed annually and we have used 2012 prices.

The table below shows the calculations for the additional costs to business of increasing the ANMW rate. These are the total costs which fall within the scope of OITO. All of our workings to calculate the full costs to business (including those exempt from OITO) and net present values can be found in Annex 6.

The corresponding 'out' of twice the value of this 'in' that we have identified is 'collective redundancies: changes to the rules'.

Table 6: Costs and benefits in scope of OITO of preferred option

Impact on business (%)	Direct impact on business	In scope of OITO?	Cost or benefit	Year 0 total	Nominal total	Present value total	Business Net Present Value (OITO)
			<u>Costs</u>				
96%	YES	YES	Wage bill apprentice rate (employer)	£1.9m	£1.9m	£1.9m	£1.8m
96%	YES	YES	Non-wage labour cost apprentice rate (employer)	£0.0	£0.0	£0.0	£0.0
			<u>Benefits</u>				
0%	NO	YES	Wage bill apprentice rate (apprentices)	£1.9m	£1.9m	£1.9m	£0.0
0%	NO	YES	Non-wage labour cost apprentice rate (Exchequer and apprentices)	£0.0	£0.0	£0.0	£0.0
			<u>Totals</u>				
			Total cost	£1.9m			
			Present value total cost			£1.9m	
			OITO present value total cost				£1.8m
			Total benefit	£1.9m			
			Present value total benefit			£1.9m	
			OITO present value total benefit				£0.0

Source: BIS estimates. We have used the share of employees working in the private sector from ASHE 2012 to estimate percentage impact on business for costs and benefits.

Annexes

Annex 2 should be used to set out the Post Implementation Review Plan as detailed below. Further annexes may be added where the Specific Impact Tests yield information relevant to an overall understanding of policy options.

Annex 1: Counterfactual discussion

Below are further details of the main arguments for selecting the counterfactual for this IA referred to on page 6.

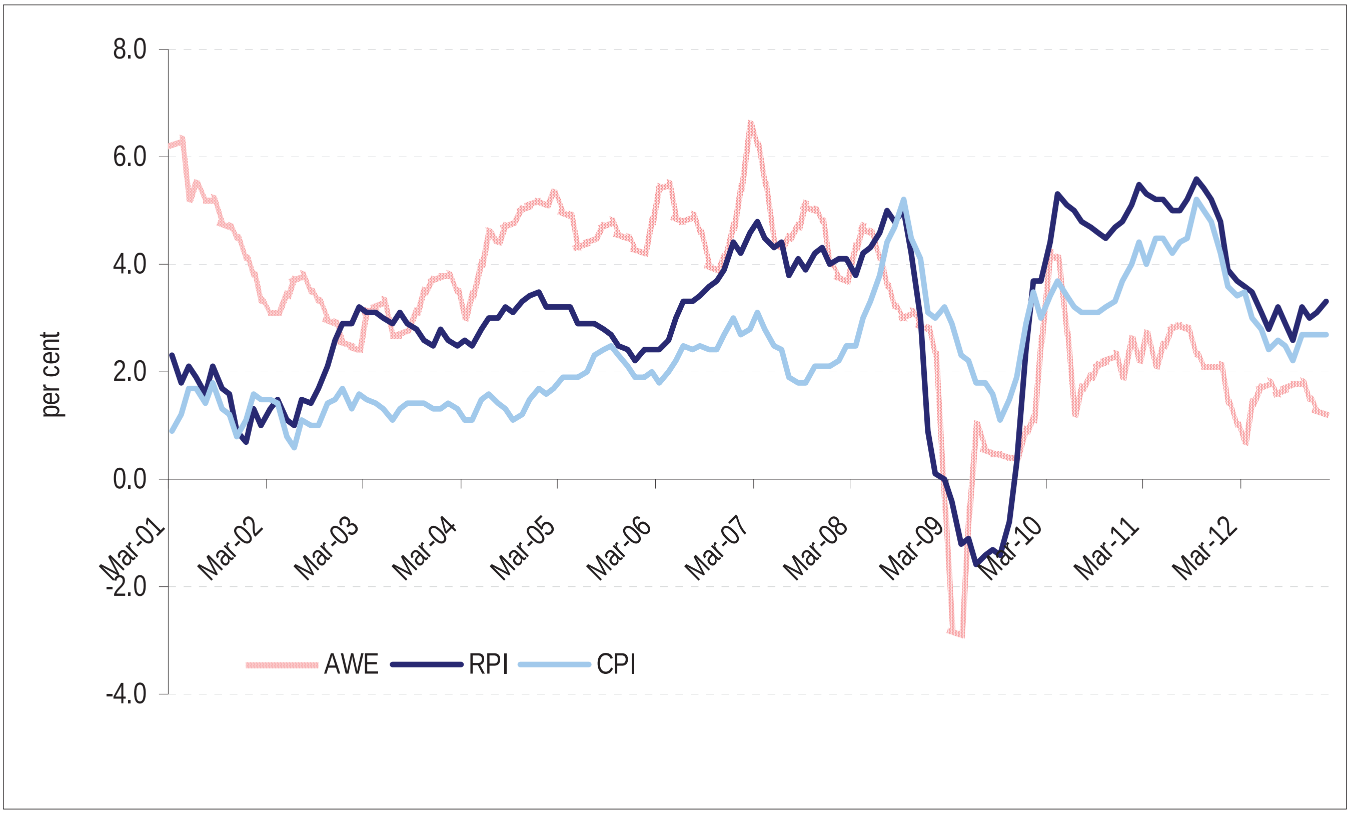
1) The macroeconomy and labour market

Since last reviewing the counterfactual, there have been no significant developments in the macroeconomic conditions experienced by the UK economy. It is also important to note that the state of the macroeconomy and labour market remains very different compared to the years that followed the introduction of the NMW. GDP was estimated to have decreased by 0.3 per cent in Q4 2012 compared to the previous quarter and GDP was estimated to have been relatively flat between 2011 and 2012 with estimated growth of 0.2 per cent[38]. The Office for Budget Responsibility (OBR) forecasts that the UK economy will recover slowly with 1.2 per cent growth in 2013 and 2 per cent growth in 2014[39]. The most recent HMT comparison of independent forecasts suggests that the recovery may be slower with an average of forecasts showing 1 per cent GDP growth for 2013 and 1.6 per cent for 2014[40].

Post recession average earnings growth has fluctuated around 2% and annual growth in total pay[41] across the whole economy was 1.2 per cent in the three months to January 2013. In comparison, pre-recession average earnings growth was above 4% since the start of 2004. Also, pre-recession average earnings growth has tended to be above consumer and retail price inflation. Post-recession this has reversed with price inflation outstripping average earnings growth (see chart A1 below). With both average earnings growth being shocked downwards post recession and price inflation higher than wage growth; this casts some doubt over whether the very lowest paid workers in the economy would have received average earnings pay settlements in the absence of a NMW rate increase.

[38] Second Estimate of GDP, Q4 2012: www.ons.gov.uk/ons/dcp171778_296602.pdf
[39] OBR Economic and Fiscal Outlook, December 2012: http://cdn.budgetresponsibility.independent.gov.uk/December-2012-Economic-and-fiscal-outlook23423423.pdf
[40] HMT Forecasts for the Economy: a comparison of independent forecasts, Feb 2013: http://www.hm-treasury.gov.uk/d/201302forecomp.pdf
[41] Including bonus payments

Chart A1. Annual growth in average weekly earnings, consumer price inflation and retail price inflation



Source: National Statistics. Average weekly earnings (KAC3), CPI (D7G7), RPI (CZBH)

Prior to the introduction of the NMW, wages for the lowest paid grew at around the same rate as the CPI with those just above getting increases in line with RPI. However, these increases were considerably below average earnings increases.

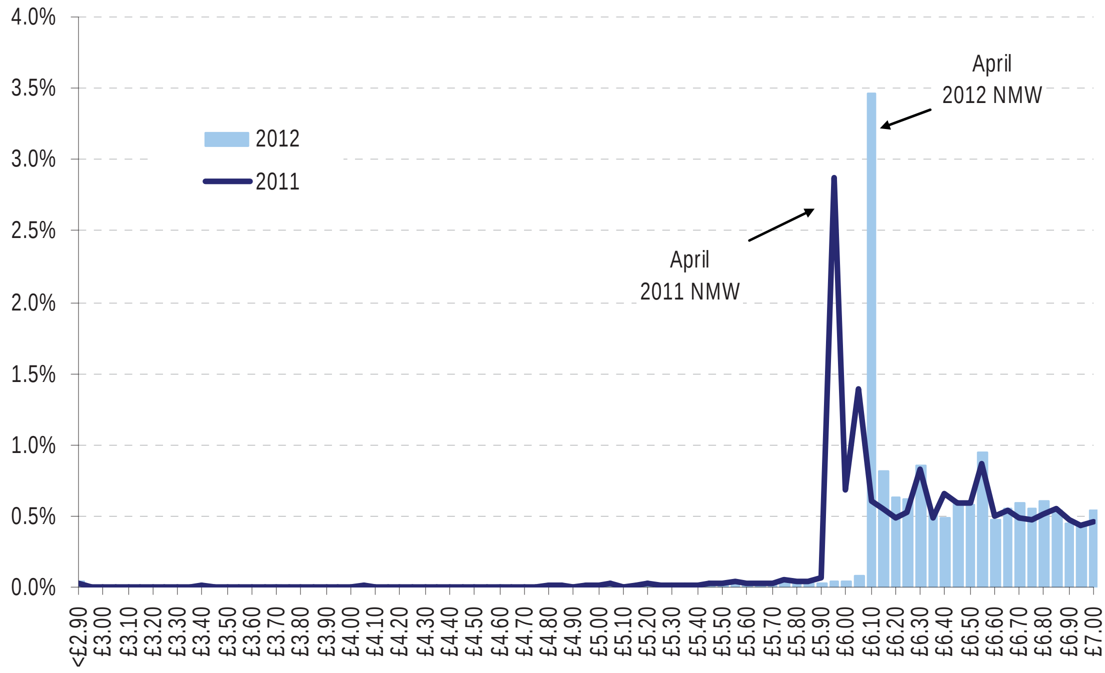
Since its introduction, the adult NMW rate has risen faster than average earnings and price inflation over time (see box 1) and therefore the scope to increase it any further without incurring job losses is now more limited. Because of the limited scope to further substantially increase wages without the shedding of labour we strongly believe the appropriate counterfactual is a wage freeze.

2) Evidence suggests that the NMW is binding on the labour market

According to evidence from ASHE 2012, the 2.5 per cent uprating of the NMW in October 2011 increased the spike in the low paid earnings distribution (see chart A2 below). The distribution just above the spike remained largely unchanged. The 2012 and the recommended 2013 NMW upratings are slightly lower at 1.8 per cent and 1.9 per cent respectively however, we will not be able to assess their impact on the low pay distribution until further data is released.

Chart A2: Adult low-pay distribution, April 2012

Per cent of adult jobs (21 years or older)



Source: Office for National Statistics, Annual Survey of Hours and Earnings

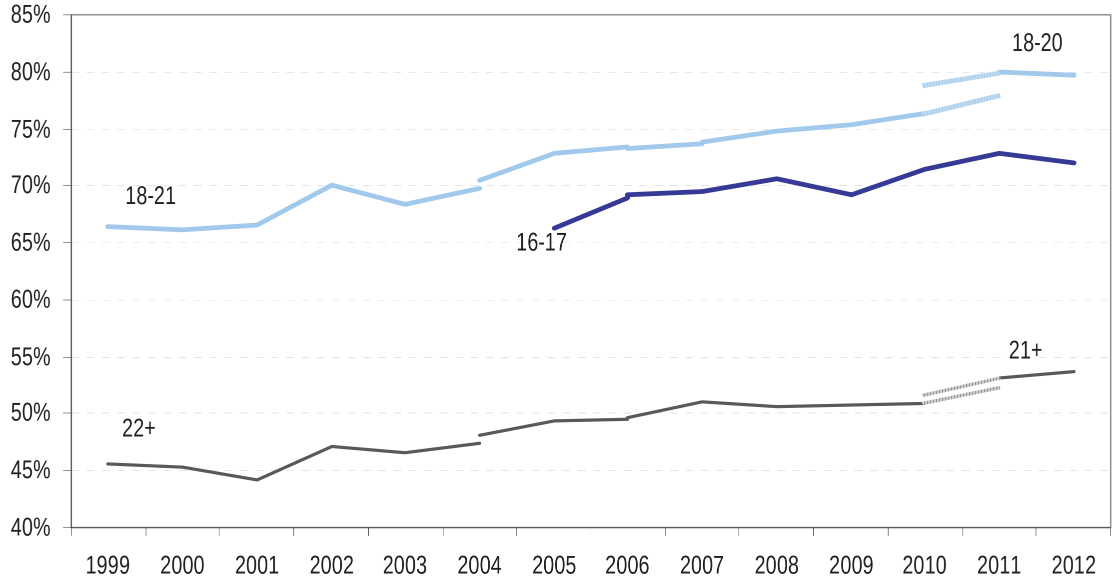
We can also look at the NMW as a proportion of median earnings, or the 'bite' (see chart A3 below). Between April 2011 and April 2012, the bite for adults has increased from 53.1 per cent to 53.7 per cent. Furthermore, the 'bite' is currently at its highest level. The 'bite' for both youth rates decreased for both youth rates between April 2011 and April 2012. However, they are both higher than in other previous years. According to LPC analysis, the bite is higher in low paying sectors than for the whole economy average. Although the adult bite remained broadly flat for the whole economy between 2007 and 2010, the bite increased for low paying sectors over this time, and has continued to increase since then. This is mainly due to lower than average earnings growth in these sectors since 2007 (1.4 percentage points lower than the NMW upratings)[42].

This argument is further supported by the fact that the NMW coverage estimates have increased from last year.

[42] National Minimum Wage Low Pay Commission report 2013 page 30

Chart A3: The bite of the NMW

Minimum wage as a per cent of median earnings



Source: Office for National Statistics, Annual Survey of Hours and Earnings. 1999-2004 ASHE data - excluding supplementary information 2004-2006 ASHE data - old methodology. 2006-2012 ASHE data - new methodology.

3) The NMW has been established for fourteen years

In addition to the arguments above, it should also be noted that the adult NMW rate was introduced 14 years ago. The LPC has received evidence that some employers have tended to track the NMW rate each year[43]. For these employers if the NMW rates were not reviewed and were frozen they would be highly likely to freeze rates. It is also possible that over time, the NMW may have had an impact on the business behaviour of low paying firms such that these businesses may interpret the NMW rate as the 'appropriate' wage for the low paid. Low paying employers thus may interpret a wage freeze (achieved through no government intervention to review the rates) as a signal that the most appropriate wage settlement is a freeze.

Chart A2, based on ASHE 2012 shows that for workers on the adult NMW there is a 'spike' in the earnings distribution at the 2011 NMW rate in 2011. In 2012 this 'spike' moves to the 2012 minimum wage rate. This trend of employers closely tracking the NMW rate has also been present in previous years. Based on this evidence, we assume that if NMW rates were not reviewed, employers would track this wage freeze.

The 2013 LPC report suggests that there is further evidence of the NMW having an influence on pay setting, citing the Workplace Employment Relations Study (WERS) 2013[44] which found that 31 per cent of private sector employers considered the NMW as an influence on pay settlements. Also, CIPD (2012) found that 7 per cent regarded the NMW as the most influential influence on increasing salaries[45]. Furthermore, research commissioned by the LPC found that there is clear evidence that the NMW has affected the timing of pay reviews in the low paying sectors[46].

[43] There is evidence that there is a spike in the earnings distribution at the NMW rates and that this spike jumps to the new NMW rate on an annual basis (see chart A2).

[44] https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/68684/13-535-the-2011-workplace-employment-relations-study-first-findings.pdf

[45] National Minimum Wage Low Pay Commission report 2013 page 41

[46] National Minimum Wage Low Pay Commission report 2013 page 43

4) Uncompetitive labour markets

For the purpose of this analysis, workers in the labour market can be broadly split into two groups – workers that have unequal bargaining power with their employer and could be exploited through low wages (for example uncompetitive labour markets) and workers employed in the competitive labour market (who are paid at the competitive labour market rate). Where there is presence of unequal bargaining power and potential exploitation of workers, both wages and employment can rise together. In a competitive labour market, employers are faced with a downward sloping demand curve and increases in wages correspond with less employment – assuming no change to the labour supply curve.

The NMW rates cover workers who could potentially be exploited by their employers (who have some form of labour market power) but are set at a level that is approaching the competitive labour market wage. Beyond this wage, the NMW will start affecting the competitive labour market and a further rise in the NMW would be followed by a fall in employment.

In the 2013 LPC report, the LPC concludes that, given the strong labour market performance of low paying sectors and the findings from their commissioned research, on balance there is no strong evidence of negative employment effects of the NMW. For young people, there may be a greater risk that their NMW rate is very close to the competitive labour market wage given their poor labour market performance over the recession. The labour demand curve for young low paid workers may have shifted inwards (a fall in demand) and there is greater uncertainty over the level of the competitive labour market wage for young people. On balance, we have concluded that the current NMW rates are not yet greater than the competitive labour market wage although we recognise that there is great uncertainty.

With this discussion in mind, we consider it is reasonable to assume that an employer who enjoys unequal bargaining power would seek to maximise his profits and, in the absence of a statutory requirement to increase the wages of his employees, would not increase such wages. Furthermore, if hypothetically the NMW was a binding wage floor in a competitive labour market (above the market clearing level), as discussed above, this would be expected to reduce labour demand compared to a situation in which the market clearing wage prevailed – and thus reduce employment (given an unchanging labour supply curve). In addition, businesses would not increase wages in the absence of a wage floor, but reduce them, as there would be enough people willing to work at a lower wage to fill the number of positions that businesses wish to fill.

It is important to also note that the Low Pay Commission (LPC) provides NMW rate recommendations such that low paid workers are helped as much as possible, while making sure that their employment prospects are not damaged by setting it too high. The LPC monitors the level of the NMW and its employment effects primarily through examining the NMW bite (NMW as a percentage of hourly median earnings) and monitoring of employee jobs in low paid sectors. The LPC makes its recommendations based on the best available economic evidence as well as oral and written evidence from Government and other stakeholders.

Annex 2: Post Implementation Review (PIR) Plan

A PIR should be undertaken, usually three to five years after implementation of the policy, but exceptionally a longer period may be more appropriate. If the policy is subject to a sunset clause, the review should be carried out sufficiently early that any renewal or amendment to legislation can be enacted before the expiry date. A PIR should examine the extent to which the implemented regulations have achieved their objectives, assess their costs and benefits and identify whether they are having any unintended consequences. Please set out the PIR Plan as detailed below. If there is no plan to do a PIR please provide reasons below.

Basis of the review: [The basis of the review could be statutory (forming part of the legislation), i.e. a sunset clause or a duty to review , or there could be a political commitment to review (PIR)];

Review objective: [Is it intended as a proportionate check that regulation is operating as expected to tackle the problem of concern?; or as a wider exploration of the policy approach taken?; or as a link from policy objective to outcome?]

Review approach and rationale: [e.g. describe here the review approach (in-depth evaluation, scope review of monitoring data, scan of stakeholder views, etc.) and the rationale that made choosing such an approach]

Baseline: [The current (baseline) position against which the change introduced by the legislation can be measured]

Success criteria: [Criteria showing achievement of the policy objectives as set out in the final impact assessment; criteria for modifying or replacing the policy if it does not achieve its objectives]

Monitoring information arrangements: [Provide further details of the planned/existing arrangements in place that will allow a systematic collection systematic collection of monitoring information for future policy review]

Reasons for not planning a review: [If there is no plan to do a PIR please provide reasons here]

BIS will not be planning a PIR for the amendments to the NMW regulations as the LPC extensively monitors and evaluates the NMW each year. The Government's remit to the LPC includes monitoring, evaluating and reviewing the NMW and its impact, with particular reference to the effect on pay, employment and competitiveness in the low paying sectors; the effect on different groups of workers, including different age groups, ethnic minorities, women and people with disabilities and migrant workers and the effect on pay structures.

Annex 3: Specific impact tests

Competition Assessment

The NMW provides a floor for wages and therefore ensures that firms cannot compete against each other by driving down wages to unacceptable low rates. Most of the sectors where the impact of the NMW is felt are characterised by large numbers of relatively small firms. To the extent that the NMW affects labour costs, these are borne by all employers in a sector. It is therefore unlikely that the NMW creates significant barriers to entry.

We have fully considered the questions posed in The Office of Fair Trading competition assessment test[47] and conclude that the 2013 NMW rates are unlikely to hinder the number or range of suppliers or the ability and incentive for businesses to compete.

Table A1. Competition assessment.

Question: *In any affected market, would the proposal..*	Answer
..directly limit the number or range of suppliers?	No
..indirectly limit the number or range of suppliers?	No
..limit the ability of suppliers to compete?	No
..reduce suppliers' incentives to compete vigorously?	No

Source: BIS

Small firms impact test

The LPC's remit required them to consider the impact of the NMW on small firms. Their recommendations were based upon extensive analysis and gathering of evidence, including evidence received from, and discussion with, small businesses and their representatives.

The LPC noted in their report that workers in large firms (250+ employees) are less likely to be paid at or below the minimum wage than those in small firms (less than 50 employees), especially micro firms (those with 1-9 employees). Over 10 per cent of jobs in micro firms are paid at the minimum wage compared with around 3 per cent in large firms. The proportion of people earning at or below the minimum wage has increased for firms of all sizes since last year, although the increases have been bigger for the smallest firms[48]. Nevertheless, according to the Annual Survey of Hours and Earnings (ASHE), the majority of minimum wage workers (in terms of numbers rather than percentages) work in large firms.

In the LPC report they found the bite of the NMW (the adult NMW as a percentage of median earnings) is much greater across the earnings distribution for smaller firms. For example the bite for small firms is 59.4 per cent compared to medium sized firms at 54.4 per cent. Furthermore, between 2007 and 2010, the bite for medium and large sized firms remained broadly constant whereas the bite for micro and other small firms has generally been increasing since the early 2000s[49].

[47] http://www.oft.gov.uk/shared_oft/reports/comp_policy/oft876.pdf
[48] National Minimum Wage Low Pay Commission report 2013 page 38
[49] National Minimum Wage Low Pay Commission report 2013 pages 32-33

Micro-business Exemption Rule

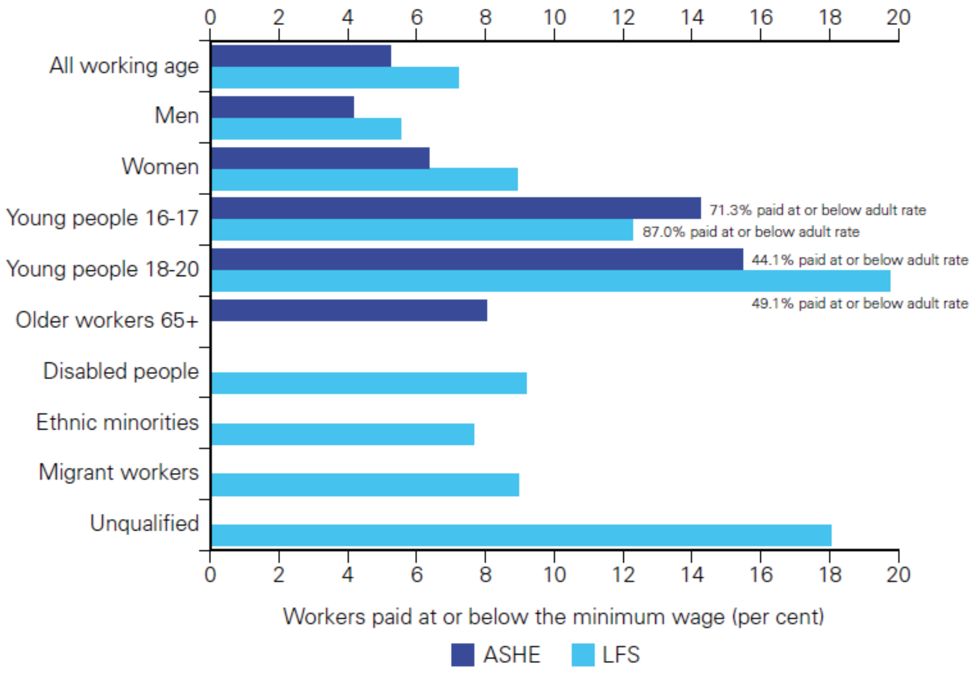
The micro-business exemption rule for organisations of 10 or fewer employees and start-ups does not apply to the National Minimum Wage.

Equality impact assessment

The Department for Business, Innovation and Skills (BIS) is subject to the public sector duties set out in the Equality Act 2010. Equality Impact Assessments are an important mechanism for ensuring that we gather data to enable us to identify the likely positive and negative impacts that policy proposals may have on certain groups and to estimate whether such impacts disproportionately affect such groups. This assessment considers the impact of the NMW uprating.

The focus of part of the LPC analysis is on groups that contain high proportions of minimum wage workers. In the 2013 report, these groups include women, young workers, older workers, people with disabilities, ethnic minorities, migrant workers, and those with no qualifications[50]. Chart A4 below shows the proportions of minimum wage workers of each of these groups compared to the general population.

Chart A4: Minimum Wage Workers, UK, 2012[51]



Source: LPC estimates based on ASHE 2010 methodology, low-pay weights, including those not on adult rates of pay, UK, April 2012 and LFS Microdata, income weights, quarterly, not seasonally adjusted, UK, Q2 2012.
Note: Minimum wage jobs defined as adults (aged 21 and over) earning less than £6.13, youths (aged 18-20) earning less than £5.03, and 16-17 year olds earning less than £3.73 in April 2012.

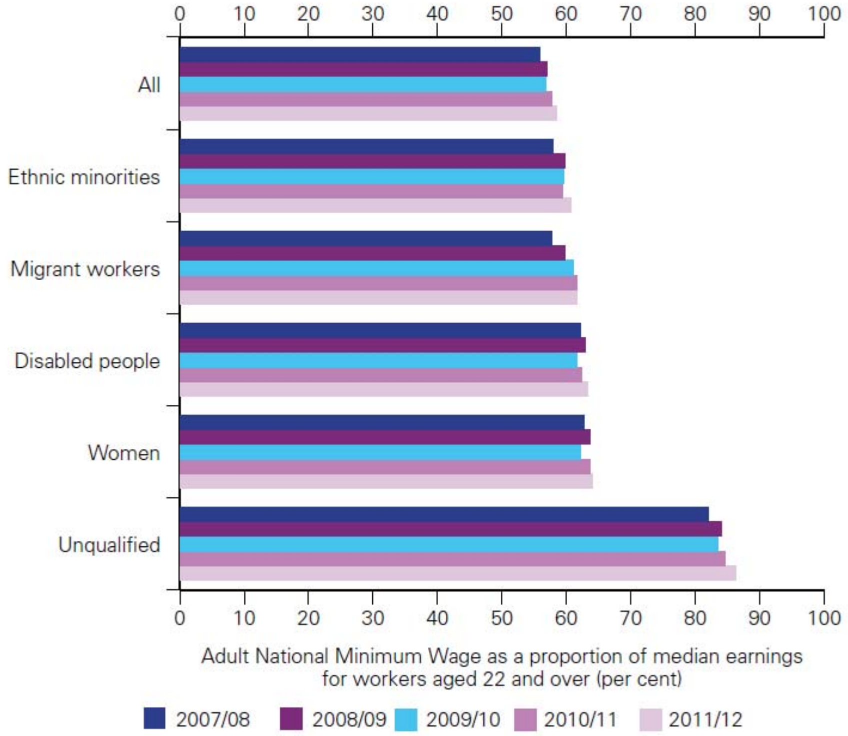
Gender
Chart A4 shows that a higher proportion of women than men were minimum wage workers in 2012. This is also reflected in the coverage estimates by gender of the October 2013 NMW rates presented in Annex 4. These coverage estimates suggest a relatively even distribution of coverage as a result of the

50 National Minimum Wage Low Pay Commission report 2013 page 23
51 National Minimum Wage Low Pay Commission report 2013 page 24

uprating of the youth rates. However, this is less true for adult workers. The LPC has also identified that 'bite[52]' of the adult NMW for women is slightly higher than for the general population (see chart A5).

The LPC notes that the median gender pay gap has fallen over the last year from 9.6 per cent to 8.6 per cent. This continues a trend that began at a similar time to the introduction of the NMW. However, the gender pay gap at the lowest decile of the pay distribution increased from 5 per cent to 5.6 per cent between 2011 and 2012, despite more than halving from the introduction of the NMW to 2011[53]. Given that more adult women have been identified as minimum wage workers than men, an increase in the adult NMW rate could reduce the gender pay gap at the lower end of the earnings distribution[54].

Chart A5: Bite of the adult NMW at the median for those aged 22 and over, by groups of workers[55]



Source: LPC estimates based on LFS Microdata, income weights, quarterly, four-quarter averages, UK, Q4 2007-Q3 2012.
Note: Due to changes in the data series, the estimates for 2011/12 are not directly comparable with estimates for earlier years.

Age
The LPC identified that a higher proportion of young workers and older workers are minimum wage workers. They also note that a relatively high proportion of young workers are paid above the youth rates but at or below the adult NMW rate.

Ethnicity
The proportion of workers of ethnic minorities that are minimum wage workers is shown in chart A4 to be relatively similar to the overall population (according to the LFS figures). However, it is important to note that this category is made up of many different ethnicities, masking some of the variability between more detailed groups. For example, the proportions of black workers and Indian workers in minimum wage jobs (5.1 per cent and 6.7 per cent respectively) were lower than that of white workers (7.2 per cent). In contrast, 12.3 per cent of Pakistani and Bangladeshi workers earned the minimum wage[56].

52 NMW as a proportion of median earnings
53 National Minimum Wage Low Pay Commission report 2013 page 39-40
54 Assuming no decrease in employment or substitution between men and women
55 National Minimum Wage Low Pay Commission report 2013 page 34
56 National Minimum Wage Low Pay Commission report 2013 page 24

Chart A5 shows the bite of the adult NMW over time on ethnic minorities. Since 2008, the bite has generally increased for white people (from 55.7 per cent to 58.3 per cent) and those from ethnic minorities as a whole (from 57.9 per cent to 60.8 per cent). But the bite for ethnic minorities disguises variations among different ethnic groups. The bite at the median for Indian workers is lower than that for white workers, and has increased from 50.3 per cent in 2007/08 to 51.8 per cent in 2011/12. The increase in the bite for Bangladeshi people was similar albeit at a much higher level (from 74.0 to 76.0 per cent). The increase in the bite for black workers over the same period, from 56.9 per cent to 63.7 per cent, was much larger. In contrast, the bite has fallen considerably for people of Pakistani origin from 73.5 per cent to 65.0 per cent. Over the last year, there was a fall in the bite for all three Asian ethnicities but increases in the bite for other ethnic groups, including white people[57].

Disability
Chart A4 shows that the proportion of people with disabilities that are minimum wage workers is higher than for the overall population.

Removal of barriers which hinder equality

The NMW policy is a broad policy and is designed to have a positive impact on all workers in low paid sectors regardless of their characteristics. Therefore the 2013 NMW rates are unlikely to create any barriers to equality with regards to the protected groups.

[57] National Minimum Wage Low Pay Commission report 2013 page 34

Annex 4: Coverage estimates

As discussed above, the LPC has not made comprehensive forecasts of future coverage of their October 2013 NMW rate recommendations. In the same way that we have provided aggregate figures in table 2 using ASHE 2012 data, below are estimates of the number of people earning at or below the LPC's recommended NMW rates for October 2013. These estimates do not include apprentices because data is not reliable enough to do so.

Table A2. Estimated number of workers (excluding apprentices) that are covered by the October 2013 National Minimum Wage rates by age and sex

	Male	Female	Total
16-17	19,000	20,000	40,000
18-20	83,000	90,000	173,000
21 and over	665,000	1,125,000	1,790,000
Total	767,000	1,235,000	2,003,000

Source: BIS estimates based on ONS' Annual Survey of Hours and Earnings (ASHE) 2012. Figures have been rounded so totals may not sum up to individual parts.

Table A3. Estimated number of workers (excluding apprentices) that are covered by the October 2013 National Minimum Wage rates by country and government office region

Country or region	Coverage estimate
Wales	116,000
Scotland	171,000
Northern Ireland	92,000
England	
North-East	100,000
North-West and Merseyside	245,000
Yorkshire & Humberside	198,000
East Midlands	169,000
West Midlands	213,000
Eastern	182,000
London	150,000
South East	195,000
South West	172,000
United Kingdom	2,003,000

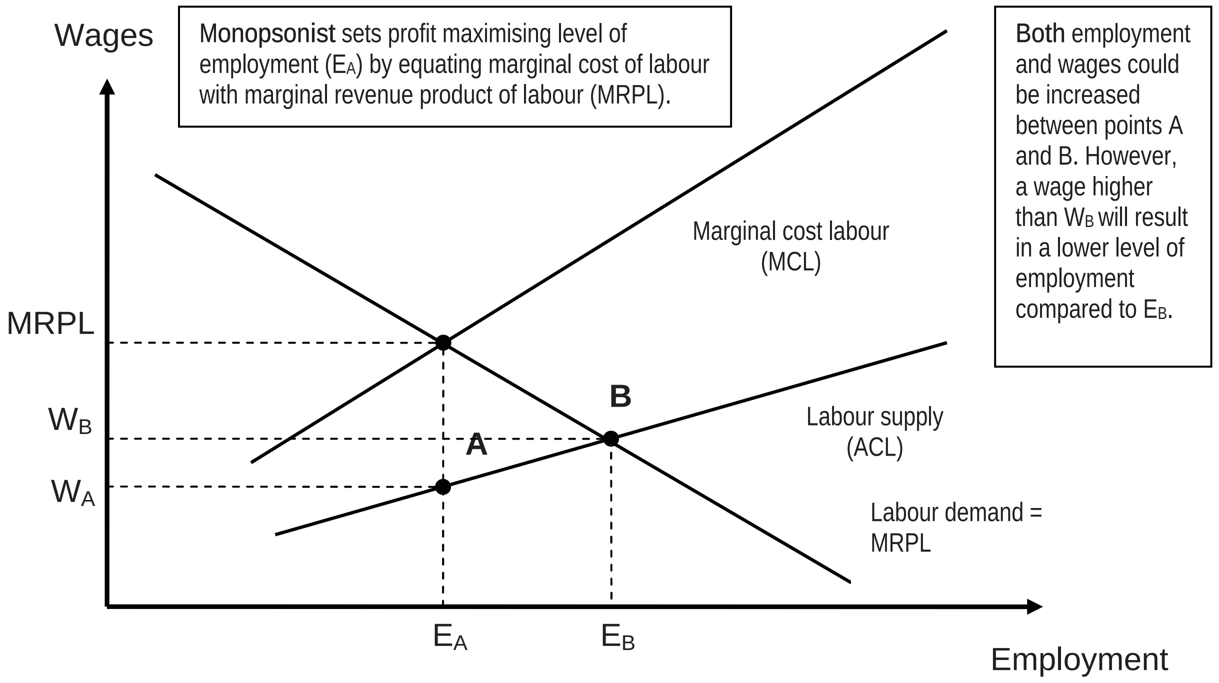
Source: A BIS breakdown of estimates based on ONS' Annual Survey of Hours and Earnings (ASHE) 2012. Figures have been rounded so totals may not sum up to individual parts.

Annex 5: Uncompetitive labour markets monopsony example

A monopsony is a market dominated by a single buyer. A monopsonist has the market power to set the price of whatever it is buying (from raw materials to labour inputs). In a monopsony labour market a monopsonist sets profit maximising employment at the point which the marginal cost of labour is equal to the marginal revenue product of labour. A monopsonist faces an upward sloping marginal cost curve (it typically has to offer higher wages to the next marginal worker). However, wages are offered at the average cost of labour which is below the marginal cost of labour.

Figure 4 below shows that a monopsonist would set employment at E_A and offer wages W_A (point A). Point B represents the perfectly competitive labour market outcome where demand and supply equate. Between points A and B a higher wage can be associated with higher employment. However, a wage higher than W_B will result in a lower level of employment compared to E_B.

Figure A1: A monopsony labour market



Annex 6: Net Present Value and direct cost to business calculations

The table below explain the costs and benefits that were fed into the Better Regulation Executive (BRE) IA calculator to calculate the net present values and Equivalent Annual Net cost to Business (EANCB) scores for option 1.

Table A4: Costs and benefits of option 1: agree with all the LPC recommendations on the NMW rates and implement the new rates. All figures in £m. Best estimates.

Impact on business (%)	Direct impact on business	In scope of OITO?	Cost or benefit	Year 0	Nominal total	Present value total	Business Net Present Value (OITO)
			Costs				
96%	YES	No	Wage bill adult rate (employer)	182.6	182.6	182.6	N/A
96%	YES	No	Non-wage labour cost adult rate (employer)	30.0	30.0	30.0	N/A
96%	YES	No	Wage bill 18-20 rate (employer)	9.9	9.9	9.9	N/A
96%	YES	No	Non-wage labour cost 18-20 (employer)	1.6	1.6	1.6	N/A
96%	YES	No	Wage bill 16-17 rate (employer)	2.0	2.0	2.0	N/A
96%	YES	No	Non-wage labour cost 16-17 (employer)	0.3	0.3	0.3	N/A
96%	YES	YES	Wage bill apprentices (employer)	1.9	1.9	1.9	1.8
96%	YES	YES	Non-wage labour cost apprentices (employer)	0.0	0.0	0.0	0.0
			Benefits				
0%	NO	NO	Wages adult rate (employee)	182.6	182.6	182.6	N/A
0%	NO	NO	Non-wage labour cost adult rate (Exchequer and employee)	30.0	30.0	30.0	N/A
0%	NO	NO	Wages 18-20 rate (employee)	9.9	9.9	9.9	N/A
0%	NO	NO	Non-wage labour cost 18-20 (Exchequer and employee)	1.6	1.6	1.6	N/A
0%	NO	NO	Wages 16-17 rate (employee)	2.0	2.0	2.0	N/A
0%	NO	NO	Non-wage labour cost 16-17 (Exchequer and employee)	0.3	0.3	0.3	N/A
0%	NO	YES	Wages apprentices (employee)	1.9	1.9	1.9	0.0
0%	NO	YES	Non-wage labour cost apprentices (Exchequer and employee)	0.0	0.0	0.0	0.0
			Totals				
			Total cost	228.3			
			Present value total cost			228.3	
			OITO present value total cost				1.8
			Total benefit	228.3			
			Present value total benefit			228.3	
			OITO present value total benefit				0.0

Source: BIS estimates. For the purposes of OITO, net cost to business on the front page are presented in 2009 prices. This IA has a 2012 price base year and the EANCB figures have been adjusted accordingly using HMT's GDP deflator. We have used the share of employees working in the private sector from ASHE 2012 to estimate percentage impact on business for costs and benefits.