

Productivity Commission's Draft Inquiry Report on Paid Parental Leave



Submission by Ai Group

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Productivity Commission’s Draft Inquiry Report on “Paid Parental Leave”

Submission by Ai Group

1. Introduction

Ai Group welcomes the opportunity to comment on the Productivity Commission’s Draft Inquiry Report on *Paid Parental Leave*.

Ai Group commends the Commission on its responsiveness to stakeholders’ views and concerns raised to date. The Commission’s report, and its proposed model, shows that the Commission has genuinely considered and sought to balance the many issues and interests relevant to this important and complex area of public policy. The Commission has clearly been cognisant of the need to take into account:

- The practical operation of any scheme, including in particular, its interaction with existing workplace rights and obligations and integration within the industrial relations framework; and
- The business impacts of any scheme, both direct and indirect, and the importance of employer acceptance in ensuring the scheme’s effectiveness.

The Commission’s model contains many of the elements proposed by Ai Group in its previous written and oral submissions, including the concept of government (taxpayer) funding for the weekly payments to working mothers at the level of the Federal Minimum Wage (FMW). It is particularly welcome that the Commission has rejected proposals for employers to fund the weekly payments or top up payments. Such funding would create substantial risks of discrimination against women of child-bearing age.


However, the proposed scheme would entail some costs for employers, most notably through the payment of superannuation contributions while employees are absent on parental leave and the requirement for employers to make parental leave payments and seek reimbursement from the Government. The impact of these costs requires careful consideration.

Ai Group agrees with the Commission's finding that the introduction of an appropriately designed paid parental leave scheme would provide many benefits to the community and, of course, for the children themselves. Importantly, it would also help keep women linked to the workforce and increase participation rates, both before and after the birth. Facilitating workforce participation is a key element in addressing the challenges of an ageing workforce.

In this submission, we address each of the key elements of the Commission's proposed model, as well as some important issues on which the Commission has invited comments.

Ai Group is one of the largest national industry bodies in Australia representing employers in manufacturing, construction, automotive, food, transport, information technology, telecommunications, call centres, labour hire, printing, airlines and other industries.

This submission is made by Ai Group and on behalf of its affiliated organisation, the Engineering Employers' Association, South Australia (EEASA).



Heather Ridout

CHIEF EXECUTIVE

2. Source of funding

Perhaps the most fundamental element of any scheme is by whom it is to be funded. Ai Group has continued to express strong support for a scheme which is wholly publicly funded and strongly supports the Commission's findings that such an approach would:

- Be the most efficient and easiest to manage administratively;
- Be most equitable in spreading the cost of the scheme across the community;
- Avoid the negative impacts associated with employer-financing;
- Avoid the costs and complexities associated with other options.

Ai Group also welcomes the Commission's conclusion that employer 'top up' payments should be entirely voluntary and an issue for workplace bargaining.

Ai Group also supports the Commission's view (Draft Report, 7.12-7.13) that the introduction of a government funded scheme is unlikely to have undesirable effects on existing paid schemes. The Commission's findings in this regard reflect a number of points made in Ai Group's submissions about the likely response of employers. In particular, the Commission acknowledges that while some employers may decide to substitute or redesign an existing scheme, or pursue different initiatives in response to the introduction of a government funded scheme, this could well lead to positive outcomes overall.

The Commission notes (at p.8.6) Ai Group's comments regarding the problems associated with pooled levy arrangements for funding a scheme. The Commission accurately describes such levy arrangements as a "hypothecated payroll tax". In effect, the imposition of a levy would amount to a tax on employment.

3. Financing of the scheme

In its previous submissions, Ai Group identified fiscal responsibility as a key principle which needs to inform the design of the scheme, given that it will be publicly funded. This is a particularly important issue in the current economic and budget context.

Ideally, a paid parental leave scheme would be financed, so far as possible, by reconfiguring existing family and welfare payments. Any additional spending should be limited to what is necessary to achieve the objectives of the scheme.

The Commission's report considers the interaction between existing welfare and family payments, particularly Family Tax Benefits A and B and the Baby Bonus. The Commission proposes that:

- Those receiving paid parental leave would not be eligible for Family Tax Benefit B or the Baby Bonus;
- Those not receiving or not eligible for paid parental leave receive the Baby Bonus;
- The Baby Bonus (renamed the maternity allowance) remain at the same level (ie \$5,000) and not be means tested (noting that a means test will operate from 1 January 2009).

The rationale advanced by the Commission for these proposals is that the Baby Bonus currently exists and there is a community desire to support all parents of newborn children (page XXVII). On the other hand, the Commission considered and rejected proposals that a paid parental leave scheme apply to all parents regardless of work status (draft report, p XXVII).

The Commission considered the interaction between paid parental leave and the Baby Bonus if they were to exist alongside each other, concluding that paid parental leave would need to be set at a higher amount than the Baby Bonus to present an adequate incentive to meet the eligibility requirements for paid parental leave. The

Commission concluded that part-time employees earning less than the FMW should receive the flat rate rather than pre-birth income. The Commission states that its “flat rate proposal means that the labour supply effects are greatest for lower income, less skilled women – precisely those who are most responsive to wage subsidies” (Draft Report, p XXVI).

Ai Group has some reservations about these aspects of the Commission’s model and the implications for the cost effectiveness of the scheme. In principle, Ai Group submits that it would be more logical and consistent with the objectives of the scheme for those receiving a wage less than the FMW prior to going on leave to receive the same wage on paid parental leave under the scheme and indeed would be more likely to reinforce the connection with paid employment as opposed to the perception of a welfare payment.

While acknowledging the importance of providing sufficient incentives for low wage earners to be in work rather than receiving welfare payments outside the labour force, it is not clear that the flat rate proposal (at the level of the FMW) is necessary to achieve this.

Under the Commission’s model, those receiving as little as \$143.10 per week for 52 weeks (ie. 10 hours per week at the FMW hourly rate) would be entitled to the full payment of \$9,788.04 (18 weeks at the FMW of \$543.18). For an employee earning \$143.10 per week, this is equivalent to over 68 weeks at full replacement income.

The treatment of those earning less than the FMW is of significance due to the number of women who are in low paid, part-time employment. From ABS data, the average female part-time employee receives \$413.10¹. The recommendation that payments be made at a flat rate of the FMW therefore has cost implications for the scheme.

¹ ABS, Employee Earnings and Hours, 6306.0, May 2006 (reissue April 2007). The current Federal Minimum Wage is \$543.78 and a lower FMW was applicable to the source data.

Putting to one side the issue of the interaction with the Baby Bonus, consideration could be given to setting a “floor” on payments where an employee’s pre-birth income is lower than the FMW, if it is considered necessary to ensure an adequate incentive to meet the eligibility criteria. For example, a payment “floor” of 50% of the FMW would still be substantially more than what is in effect the minimum qualifying rate of \$143.10 per week (ie. a person with pre-birth income of \$143.10 per week would receive weekly payments of \$272, half the FMW). 18 weekly payments of \$272 would work out at about the level of the current Baby Bonus (although it would be taxable).

Ai Group encourages the Commission to give further consideration to the design of its maternity allowance (if the recommendation regarding such a payment is retained), in order to limit the additional cost that the scheme would entail and to ensure its objectives are clear. Two points in particular should be borne in mind:

1. The current level of the Baby Bonus, and the substantial increase in the amount over recent years, has been heavily influenced by the absence of a paid parental leave scheme in Australia. Where such a scheme is introduced, there is cause to consider whether the payment should be set at a more moderate level;
2. The Government has only recently made a policy decision (yet to take effect) to exclude higher income families, to address community views about appropriate recipients of welfare payments. If the amount of the payment is set at a level akin to the Baby Bonus, the argument in favour of a means test is particularly strong.

4. Payment rate

The Commission has proposed:

- That payments be made at the level of the FMW;
- In some limited cases such as juniors, where actual wages are below the FMW, payments would be made at a lower rate;
- Payments would be taxable.

Under the model advocated by Ai Group in its previous submissions, payments were capped at the level of the FMW and were taxable as income. Ai Group continues to support these features of the scheme as being appropriate in terms of:

- Limiting the overall cost of the scheme;
- Introducing a measure of equity, given that the scheme is publicly funded;
- By treating the payments as taxable income, reinforcing the perception of the payments as income replacement rather than welfare payments.

The Commission has identified some specific issues for junior employees, in that a young person might be tempted to make short-sighted decisions if the payment rate for paid parental leave was well in excess of the employee's pre-birth wage. Ai Group's view is that the scheme should not enable any eligible employee to receive payments well in excess of pre-birth income as this is not necessary or cost effective.

If Ai Group's suggestion that part-time employees earning less than the FMW be paid at replacement rate (possibly subject to a payment "floor"), the same rule should be adopted in respect of juniors. Alternatively, a lower payment floor could be set for junior employees, more closely reflecting wages.

There are already a number of elements of the scheme that remove the potential for “short-sighted” decisions, including the requirement to be employed for the 12 months prior to the birth, the fact that payments would be made in instalments, and that payments would be taxable.

5. Eligibility

Under the Commission’s model, the main eligibility criteria for paid parental leave are:

- 12 months’ service, with any number of employers;
- An average of at least 10 hours per week in that period;
- The person must be the child’s primary carer.

The Commission has proposed that an employee who meets the criteria for unpaid parental leave would also be entitled:

- To receive superannuation contributions during a period of paid parental leave (capped at 9% of the FMW);
- To be paid directly by an employer as part of the normal pay cycle.

A number of the proposed eligibility criteria reflect the principles identified by Ai Group as appropriate in influencing the design of the scheme:

- It should be an employment-based entitlement, rather than a universal payment on childbirth;
- Parental leave payments should not be means tested, since all women in paid work face an opportunity cost associated with childbearing;
- The scheme should focus on women due to their intrinsic childbearing role.

While the Commission’s model does not confine paid parental leave to women, its design clearly recognises, for practical reasons, the utility of centring the eligibility requirements on the mother.

Ai Group, in its previous submissions, advocated that the scheme should be integrated closely with existing parental leave entitlements and that eligibility be confined to employees entitled to unpaid parental leave (to which a return to work guarantee is attached). Ai Group continues to support this integrated approach.

While the Commission's model does not fully adopt this principle, its recommendations show that it has carefully considered how the scheme might best be designed to facilitate workforce participation and minimise the burden on business.

6. Duration

Paid parental leave

The Commission has proposed paid parental leave of a duration of 18 weeks, which it states is influenced primarily by considerations of maternal and child health and development and the view that between six to nine months of leave is desirable. The Commission acknowledges however that the entire period of leave need not be financed under the scheme and some contribution by the parents could be expected.

In its earlier submissions, Ai Group nominated an appropriate duration as being 14 weeks (at the FMW). While Ai Group appreciates that the appropriate duration of a scheme is influenced by a number of factors, it expresses some reservations about the necessity and cost of the Commission's proposed duration. The Commission notes research from the Longitudinal Study of Australian Children indicating that mothers who did take leave around the time of childbirth took an average of 37 weeks (over 9 months) (Draft Report, pages 3.19-3.20). Only 29% of mothers in paid work prior to leave returned to work within six months, and only 20% of all women regardless of whether they were in paid employment prior to childbirth returned to work within six months of childbirth. On the basis of this research, it is not clear why the Commission considers 18 weeks' paid leave necessary. The reasons

for those who returned to work within six months of the birth should be carefully considered in order to determine their likely responsiveness to the scheme.

As discussed in section 2 – Financing of the scheme, Ai Group is conscious of the need to minimise the additional cost of the scheme on top of budget savings which may be achieved. The Commission indicates that, with Baby Bonus savings plus tax and budget savings, the additional (new) cost equates to around five weeks' paid leave, ie. the savings would finance nearly 13 weeks' of paid leave. In Ai Group's view, this highlights the need to ensure there is a sound basis for recommending the 'additional' weeks which represent an additional cost to government.

Paid paternity leave

The Commission has proposed two weeks' paid paternity leave be available to fathers or the supporting parent which would be quarantined and could not be transferred to the primary care giver. Eligibility would not depend upon the other parent being eligible for paid parental leave. The leave could be taken concurrently with paid parental leave and would need to be taken within the six months after birth.

The Commission has assessed that 225,000 fathers will be eligible for paid paternity leave, whereas only 140,000 mothers would be eligible for paid parental leave. Hence, the cost of including paid paternity leave in the scheme is substantial.

As the Commission has noted, "its actual effects on fathers' behaviour are likely to be modest" (Draft Report, p XXIII) and that although the reaction is hard to assess, "UK experience suggests that initially a relatively small share will use it" (p 5.34).

Including paid paternity leave as an element of the scheme could conceivably encourage the view that paid parental leave is appropriately the domain of women, whereas the (much shorter) paid paternity leave is the part carved out for men. The existence of a separate paid paternity leave component may also encourage the

perception that paid parental leave is not in fact available to fathers who are the primary care giver.

Currently, the average period of leave taken by men upon the birth of a child is two weeks, with only 15% of men taking more than two weeks' leave (cited in the Draft Report, p. 3.19-3.21). The duration of fathers' leave would appear to be influenced by financial pressures as well as societal (and workplace) norms and cultural factors, although it is not the subject of research considered by the Commission. In any event, to the extent that it is a factor of financial pressure, the existence of a paid parental leave scheme would already assist in alleviating this pressure.

In Ai Group's view, a likely outcome of paid paternity leave is that fathers who take the paid leave will not increase their period of leave and will merely receive the additional income (by way of paid paternity leave payments) on top of what they would otherwise have received (noting that fathers typically take paid leave at this time in any event). This would not advance the goals sought to be achieved by paid paternity leave.

Ai Group does not support the paid paternity leave element of the proposed scheme.

To the extent that societal and cultural factors influence fathers' leave, educational and information initiatives promoting the role and value of fathers may be more cost effective in achieving change.

7. Rules on taking paid parental leave

The Commission's model contemplates a number of rules about taking leave including that:

- Paid parental leave could not be taken concurrently by both partners (but paid paternity leave could overlap with the mother's leave);
- Leave would have to be taken in a single continuous block;

- Leave would need to commence at birth or after a period of other continuous leave commencing at birth;
- An employee could choose to take less than 18 weeks' paid parental leave but would only receive payment for the period of leave actually taken;
- A 'keep in touch' arrangement, allowing an employee on paid parental leave to attend the workplace for up to ten days if the employer and employee mutually consent strengthens the connection to the workplace;
- It would not be possible to take the paid leave on a part-time basis;
- An employee would be required to give six weeks' notice of an intention to extend the period of parental leave (which would require amendment of the NES).

Ai Group generally supports the above recommendations as practical and sensible and as reflecting a reasonable balance between the benefits of flexibility with the need to avoid unwarranted complexities. The rules also go some way towards enabling the scheme to be integrated in a practical way with the existing parental leave provisions which is important in ensuring the scheme operates effectively.

On the issue of whether paid leave should be able to be taken on a part-time, Ai Group cannot see sufficient merit in including this element within the statutory scheme. In summary:

- There is unlikely to be great demand for such arrangements in the 18 weeks following the birth of a child; (Indeed, where the decision to return to work is financially motivated, the scheme would alleviate this pressure);
- There is uncertain and potentially problematic interaction with existing unpaid parental leave entitlements and the right to request flexible working arrangements under the NES; and
- The ability to take leave part-time could also be seen as undermining the objective of the scheme of enhancing maternal and child health and development.

Ai Group supports the principle behind a ‘keep in touch’ arrangement (Draft Report, p 2.30-2.31), allowing employees to participate in training or planning and strategy days. The recommendations of the Commission in this regard would appear to advance important objectives of the scheme without undermining the objectives associated with maternal and child health and wellbeing.

7. Delivery of payments

As set out in its earlier submissions, Ai Group submits that payments should be paid directly to employees by the Government unless the employer and employee agreed to the employer acting as paymaster (which might well be common in practice, at least for larger firms). This would avoid the difficulties associated with cases where an employer is an unwilling paymaster, as well as cases where an employee would prefer not to receive the payments from the employer for a range of reasons. Complications would also arise where an employer was making the payments to an employee and where the employee decided during that period not to return to the same employer – the employee might have an incentive not to inform the employer in order to avoid any disruption in payments.

The Commission has recommended that the employer be responsible for delivering the payment to employees as part of the normal pay cycle where the employee is entitled to unpaid parental leave. The Commission’s has qualified this recommendation by stating that the obligation would only arise where there is an efficient and timely way for government to fully reimburse that employer, preferably through a credit to ‘pay as you go’ withholding payments to the ATO for employers making at least monthly repayments. The Commission estimated the cost of deferred reimbursement as \$7 million in aggregate each year (or around \$5 per relevant employee per month) (Draft Report, 2.13).

Ai Group recognises that in making these recommendations, the Commission has sought to balance the compliance and administrative burden on business. Reimbursement through a credit to ‘pay as you go’ withholdings would be greatly preferable to a system of cash reimbursement, which in practice could take many

months. A requirement that only those businesses making at least monthly repayments would also lessen the cash flow implications of being required to act as paymaster.

8. Superannuation

The Commission has proposed that where an employee who takes paid parental leave or paid paternity leave is eligible to take unpaid parental leave, and where the employer is already making super contributions for that employee, an employer would be required to make superannuation contributions on behalf of that employee at 9% on the FMW. The contributions would not be reimbursed.

The rationale behind this recommendation appears at page XXX of the Draft Report:

“Employers would participate in the scheme by providing superannuation contributions to relevant employees, but would otherwise have few obligations beyond those already applying under the National Employment Standards. Providing super contributions would be a quid pro quo for the retention gains that business could expect, and from a practical perspective, payment of such entitlements but the government would entail many complexities (as shown below this employer contribution represents a relatively small share of the total package of costs.)”

Ai Group is not supportive of placing this obligation on employers which is clearly a direct cost on business.

However, Ai Group recognises that the Commission has given consideration to the impact on business, and has alleviated the burden to some extent, in recommending that:

- The payments would only be required where the employee is entitled to unpaid parental leave under the NES and is entitled to these benefits before going on leave;
- The contributions would be capped at 9%, where the employer contributions are normally above that level;
- The contributions would also be paid on the FMW or lesser, depending on pre-birth income.

As a result of the above, the maximum contribution for an employee taking 18 weeks' paid parental leave would be \$881 (or \$98 for an employee taking two weeks' paid paternity leave). For an employee on the FMW, this amount would represent around 3% of annual salary.

In general, the rationale for requiring superannuation contributions to be made would appear to be two-fold:

1. Addressing the inequity in women's retirement savings due in part to characteristic absences from the workforce due to caring responsibilities;
2. Reinforcing the concept of paid parental leave as a work-entitlement.

While the above are both relevant goals of a scheme, it is not clear that placing a requirement on employers to make superannuation contributions in this way is a necessary or cost effective means of achieving them.

Keeping women linked to the workforce and facilitating workforce participation would tend to have a far greater role in the long term in reducing the disparity between men and women in retirement savings. As to the concept of the paid leave as a work-related entitlement, as the Commission notes in its report, there is no one way of treating work-related payments for superannuation purposes. For example, annual leave payments are treated as ordinary time earnings on which superannuation is payable, but annual leave loading is not. Nor is it payable on other work-related

entitlements such as redundancy pay or payment in lieu of notice (under Superannuation Guarantee Ruling 94/4). Currently, as the Commission notes, superannuation is not payable on paid parental leave, on the basis that it is an entitlement related to employment and parenthood and not in respect of ordinary hours of work (also according to SGR 94/4).

As Ai Group pointed out in its previous submissions, employers will need to adjust to a new system of obligations and rules under the NES, including some which are highly relevant to this area (eg. the right to request flexible working arrangements and to extend the parental leave period by an additional 12 months). Introducing additional obligations on employers, especially those involving a direct cost, is not warranted.

9. Accrual of entitlements during paid parental leave

The Commission's report canvasses the issue of whether time spent on paid parental leave under the scheme should count as service for the purpose of accruing other entitlements such as annual leave, personal/carer's leave and long service leave. The Commission has specifically sought feedback on this issue.

The Commission states (Draft Report, 8.31):

The Commission recognises the value of paid parental leave being seen as being like other leave. However, there is no single set of commercial and legislative requirements for entitlements on current forms of leave – so that it is not easy to gauge what is 'normal'. And, particularly with respect to mandating the accrual of leave entitlements while on parental leave, there would be a significant financial and (ongoing) compliance cost imposed on employers and legislative burden placed on Governments in order to amend the relevant industrial relations legislation (potentially with other broader

consequences). In the Commission's view, this would preclude leave accrual being considered a practical component of the scheme it is proposing. However, if evidence emerged that obstacles could be overcome in a cost-effective manner, the Commission would have cause to reconsider this conclusion.

In Ai Group's view, the practical difficulties are significant and a requirement to treat the period of paid parental leave as service for the purposes of other paid leave would impose a substantial and unreasonable cost burden. Ai Group opposes any requirement that unpaid or paid parental leave be treated as service over and above what is required under the NES (or in a contract of employment or a modern award).

A requirement to treat paid parental leave as service would impose a direct cost on employers, risking an adverse response from employers. The additional financial burden would be imposed on employers at a time when they are already required to adjust to the employee's absence and, (under the Commission's model), act as paymasters and make superannuation contributions.

The direct cost implication is most evident in the case of annual leave. For example, if a period of 18 weeks' of paid parental leave was treated as service for the purpose of accruing annual leave, an employee would accrue an additional one and a half weeks of annual leave. Many employees taking parental leave could be expected to want to use that annual leave accrued during unpaid parental leave to extend their absence from work. (It may be noted in this respect that under the NES, an employer must not unreasonably refuse to agree to an employee's request to take annual leave). Seen in this way, the requirement to treat unpaid parental leave as service for the purpose of other leave entitlements (and for annual leave in particular) is really an indirect means of achieving a partly employer-funded paid paternity leave model. Ai Group opposes such a model for the reasons expressed above and in its previous submissions.

The Commission appears to contemplate that if paid parental leave was to be treated as service, it would be consistent with other elements of the Commission's model that accrual or payment of the other entitlements be "capped" at the level of the FMW (draft report, 8.30). However, as the Commission recognises, leave entitlements typically accrue based on the employee's hours of work and payment is linked to the rate the employee was receiving prior to commencing leave or which the employee would have received in the leave period had he or she not been on leave. Imposing a payment rule based on the FMW for the period of leave accrued during paid parental leave would be problematic and confusing. It would introduce unwarranted complexity into the accrual and payments rules for other types of leave and, as the Commission notes, would require amendment of the NES. These new complexities would come at a time when employers and employees will be adjusting to a range of new entitlements and rules under the NES.

On the one hand, it is true that forms of paid leave are generally treated as service for the purposes of accruing other leave entitlements. However, no other form of paid leave is for such an extended period as well as being characteristically taken by an identifiable group of employees (ie. women of childbearing age, in the case of paid parental leave). For these reasons, any requirement to treat paid parental leave as service would present difficulties and dangers. Because of the particular nature of parental leave, it is best treated as suspending the period of employment, as has historically been the case.

In Ai Group's view, treating paid parental leave as service is unlikely to be a cost effective means of signalling that the leave is a work-related benefit.

Summary of how unpaid parental leave is treated

Currently under the *Workplace Relations Act 1996* (Cth), unpaid parental leave does not break continuity of service but does not count as service for the purposes of accruing annual leave or personal/carer's leave under the Act. A period of unpaid parental leave only counts as service for the purpose of determining an entitlement to subsequent unpaid parental leave. A period of parental leave does however count as service where expressly provided in an employee's contract of employment, any award or agreement which applies to the employee, or under another law.

Under the NES, unpaid parental leave will count as service for limited purposes, that is, in determining eligibility for flexible work arrangements, notice of termination and later periods of parental leave. It will not count as service for the purposes of annual leave, personal/carer's leave or redundancy pay.

The NES does not currently contain a stand-alone entitlement to long service leave (beyond giving effect to a separate pre-existing entitlement). The Government is currently developing a long service leave standard in consultation with the states and territories. However, it could be expected that unpaid parental leave will not count as service for the purpose of any long service leave standard, consistent with its treatment for most other purposes under the NES and with existing long service leave legislation.

Under both the WR Act and the NES, entitlement to compassionate leave is not based on service but rather the occurrence of a specified event and hence is not relevant in this respect.