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The Rt Hon Andrea Leadsom MP
Department for Business, Energy and Industrial Strategy

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Dear Andrea,

I would like to congratulate you on your recent appointment as Secretary of State for Business, Energy and Industrial Strategy. At the Low Pay Commission (LPC), our role is to advise the Government on the appropriate levels of the different rates of the National Minimum Wage (NMW), including the National Living Wage (NLW). Over 20 years, the LPC's consensus-based social partnership model has ensured the NMW's success in raising pay for the lowest paid without harming employment, as well as building strong credibility with workers and employers alike. We look forward to working with you on this important agenda, in particular on the future of the NLW beyond 2020.

I am writing now to set out our recommendations on the age structure of the NMW, which we have reviewed over the past year. These recommendations will underpin further advice in the autumn on the future of the NLW. These two questions are closely linked, as changing the structure of the youth rates will directly affect the NLW's future trajectory. Because of this, we are writing now with our recommendations on this issue, to make clear the basis for our advice on the post-2020 remit later in the year. In short, **we believe there is a strong case for lowering the age of eligibility for the NLW from 25 to 21. We recommend a two-step approach, with Government announcing this autumn that the age of eligibility for the NLW will be 23 from April 2021, along with a commitment to reduce the threshold to 21 at a later date. The LPC will then review the evidence and advise Government in October 2022 on the appropriate timetable for the next step.** Making these changes in two stages represents a pragmatic approach, balancing ambition for 21-24 year olds with caution towards the impacts on businesses and the most vulnerable workers in this group.

We are not proposing any changes to the structure of the rates for those aged between 16 and 20, but will continue to consider the differentials between these rates and the NLW as part of our usual rate recommendations. We are also reviewing the Apprentice Rate of the NMW and will notify the Government of our

recommendations on this in the autumn, alongside our recommendations on the NLW and NMW rates to come into effect in April 2020.

Lowering the NLW threshold age

Our argument for lowering the NLW age threshold is based on several pieces of evidence. Firstly, the number of 21 to 24 year old workers paid at the rate for their age has fallen substantially. In 2014, 12 per cent of 21-24 year olds were paid the NMW, which was the prevailing adult rate for those aged 21 and over. But since the introduction of the NLW this has halved to 6 per cent, as many employers have chosen to pay the NLW to all workers aged 21 and over.

We have also considered the 'bite' of the NLW for these age groups – the ratio of the NMW rate to the median wage, and a key measure of pressure arising from minimum wage rates. While moving 22 to 24 year olds onto the NLW would increase their bites, they would remain at reasonable levels. However, 21 year olds have the highest bite of any age group currently, and moving them up to the NLW would increase this further – this finding is a contributory factor behind our more cautious approach for this age group.

For 16-20 year olds a move up to the next rate could result in substantial bite increases, of over 20 percentage points in most cases, indicating a significant impact on their position in the labour market. This is a key reason why we are not proposing a change in the NMW structure for these workers.

On most measures, including educational participation, employment and unemployment rates, as well as where – and how – they work, 23, 24 and 25 year olds are very similar. There is, on these measures, little basis for treating them differently in the minimum wage structure. The evidence base for extending the NLW to 21 and 22 year olds is less clear-cut; on many measures, they are more different to 25 year olds than 23 and 24 year olds. But in making this decision, we also considered the views of employers and other stakeholders.

Although there was not unanimous support for this proposal, the majority of employers in low-paying sectors told us they would support extending the NLW to 21 year olds. One important reason was fairness: 21-24 year old workers generally do the same work as older workers, with minimal differences in experience and productivity, particularly in low-paying sectors. Another reason was to reduce complexity, an important element in improving compliance. Employers noted that this would be the right move provided there was sufficient notice, so that small firms and others with tight margins could prepare. Their view was that 21 is a more 'natural' cut-off point. This was an important reason why the LPC previously argued throughout the 2000s for lowering the starting age of the NMW from 22 to 21.

When that change was made in 2010, it led to a 20 per cent increase in the wage floor for 21 year olds. But despite the large size of that increase – and the timing of implementation, two years into the financial crisis – research has shown no negative effects on employment for 21 year olds; indeed, there was some evidence that the higher wage floor stimulated movements into employment for some young people. In part this was because the change was well managed – employers were given 18 months' notice to prepare.

Finally, demographics are a key part of our rationale. Population projections suggest that the number of 21 to 24 year olds in the population will fall over the next five years. While they are projected to rise again subsequently, this reduction in numbers will provide further employment protection for this group over the period of transition that we are proposing.

Making the change in two stages

Overall, we think the evidence supports an extension of the NLW to workers aged 21-24 and that current economic conditions, of record high employment and a tightening labour market, are likely to offer protection to young workers. We believe this can be achieved without harming their employment prospects, provided that employers are given sufficient notice. And we think it is important to signal clearly to employers our intention to recommend bringing the age of eligibility down to 21, to give them a long lead-in time to prepare.

However, the evidence does indicate a difference in the labour market position of 21 to 22 year olds and those aged 23 and over. In addition, moving the age of eligibility to 21 in a single step would be a substantial change and affect a larger cohort than that in 2010. For these reasons, we recommend a cautious approach to this change, lowering the age of eligibility first to 23 and then to 21. This will provide us with an opportunity to review the evidence again and maintain flexibility over when to move to 21.

We therefore recommend that the lowering of the age of eligibility for the NLW to 23 from April 2021 is announced in the autumn of 2019, along with the commitment to reduce the threshold to 21. This will give employers 18 months' notice in which to prepare for the initial change. By October 2022, the LPC will have sufficient evidence to assess the impact of this change and the circumstances of 21 and 22 year olds, and therefore will be in a position to make a recommendation on the timetable for lowering the eligibility age further to 21.

It is possible, indeed likely, that when they hear this announcement some employers will chose to move their 21 to 24 year old workers onto the NLW sooner than is required. We will continue to monitor the evidence and, if this happens, it may provide scope to lower the age of eligibility more quickly.

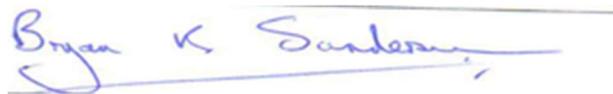
Implications for the NLW after 2020

We look forward to providing you with further advice on our future remit later this year and will do so on the basis of the age thresholds we have set out in this letter. However, there is one final point of relevance to the Government's ambitions post-2020.

The changes we propose here will have a direct impact on the Government's ambitions for the minimum wage post-2020. The inclusion of younger workers in the NLW population will lower the median wage on which any target is based and therefore the nominal values of the NLW rates in the future. This means there are some clear trade-offs: younger workers benefit in the form of higher pay, but older NLW workers will receive lower rates of increase than they otherwise would have. At the same time, the overall risk of job loss for those aged over 25 will be lower than it otherwise would have been, and higher for 21 to 24 year olds. The Commission has considered these trade-offs and discussed them with employer and employee stakeholders. Our view is that this change is the right choice: it will make the system fairer and bring it back into line with understood business practices.

Once again, I look forward to working with you on this important agenda. If you would like to meet to discuss this or our work more generally, I would be more than happy to do so.

Yours sincerely,



Bryan Sanderson
Chair, Low Pay Commission

Letter copied to the Chancellor of the Exchequer, the Chief Secretary to the Treasury and the Minister for Small Business, Consumers and Corporate Responsibility