Non-compliance and enforcement of the Minimum Wage

Low Pay Commission

September 2017

About this report

Traditionally each Low Pay Commission annual report contains a chapter looking at enforcement and non-compliance with the National Minimum Wage (NMW), which is where workers are paid below the legal minimum.

However, instead we are publishing a separate report, which this slide pack summarises, that considers the nature and extent of non-compliance, reflects on the current policy response and makes policy recommendations where necessary.

It was prompted by the introduction of the National Living Wage (NLW) in April 2016, a higher rate for workers aged 25 and over, which raised the numbers covered by the minimum wage sharply and had implications for compliance and enforcement.

In this report we estimate the number of workers affected by underpayment – though this is challenging, look at the policy response to underpayment and make a series of recommendations

For the full report, sources of evidence and recommendations please go to www.gov.uk/government/publication/non-compliance-and-enforcement-of-the-national-minimum-wage-september-2017

For more information and research about minimum wages:

Website: www.lowpay.gov.uk

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If you are worried you aren't being paid the minimum wage, contact the Acas helpline on **0300 123 1100**

How the LPC works

The Low Pay Commission is the independent body tasked with advising the Government each year on the rates of the minimum wage – including the NLW.

For the NLW, we are required each year to recommend the pace of increases to a 2020 target of 60% of median earnings 'subject to sustained economic growth'. For younger workers and apprentices, we recommend increases to help as many low-paid workers as possible 'without damaging their employment prospects'.

The rates of the National Minimum Wages, including the National Living Wage, are shown below.

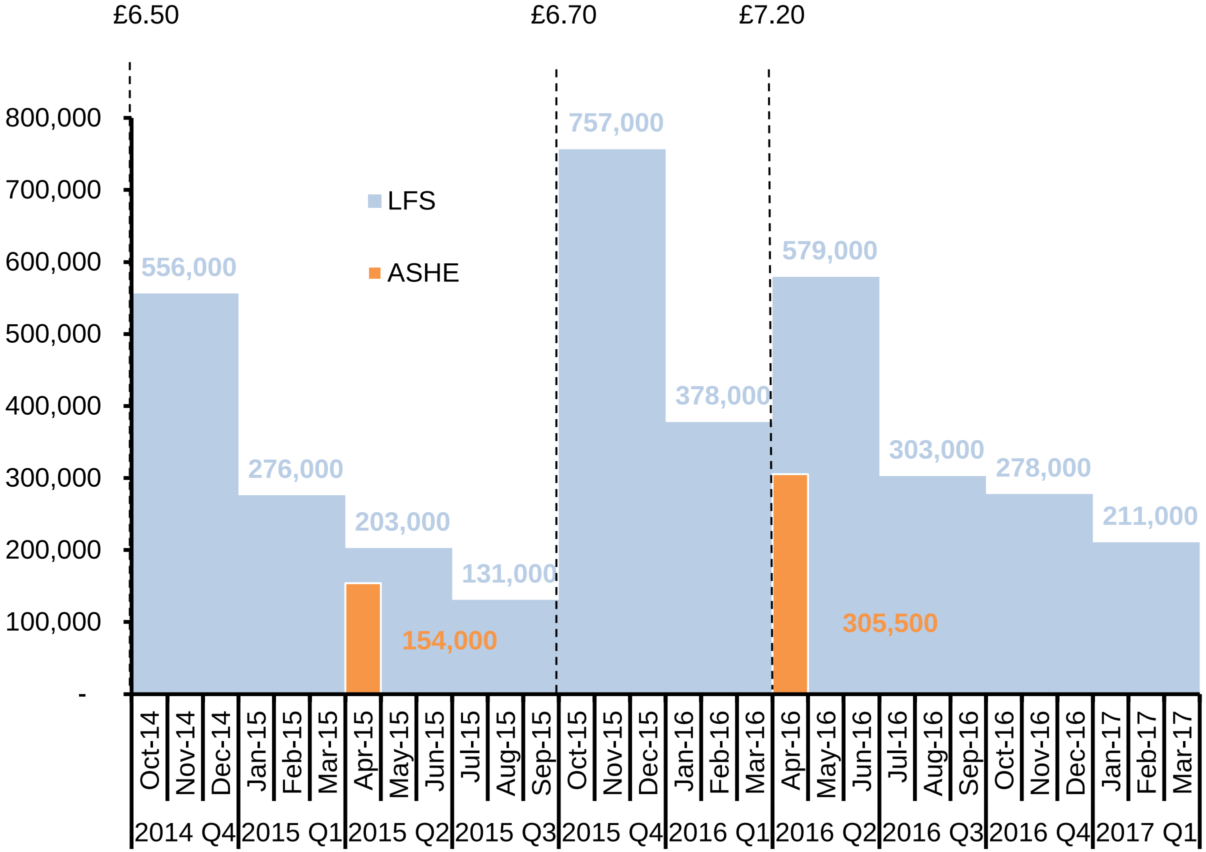
Minimum Wage Rates	Current From 1 April 2017
National Living Wage (25+)	**£7.50**
21-24	**£7.05**
18-20	**£5.60**
16-17	**£4.05**
Apprentice Rate*	**£3.50**
Accommodation Offset**	**£6.40/day**

*Applicable to apprentices in their first year or aged 16-18

**Deductible where accommodation is provided

Estimates of the number of underpaid workers did not rise significantly following the introduction of the National Living Wage, but it is highly seasonal throughout the year

Figure 2: Estimates of the number of underpaid workers aged 25 and over



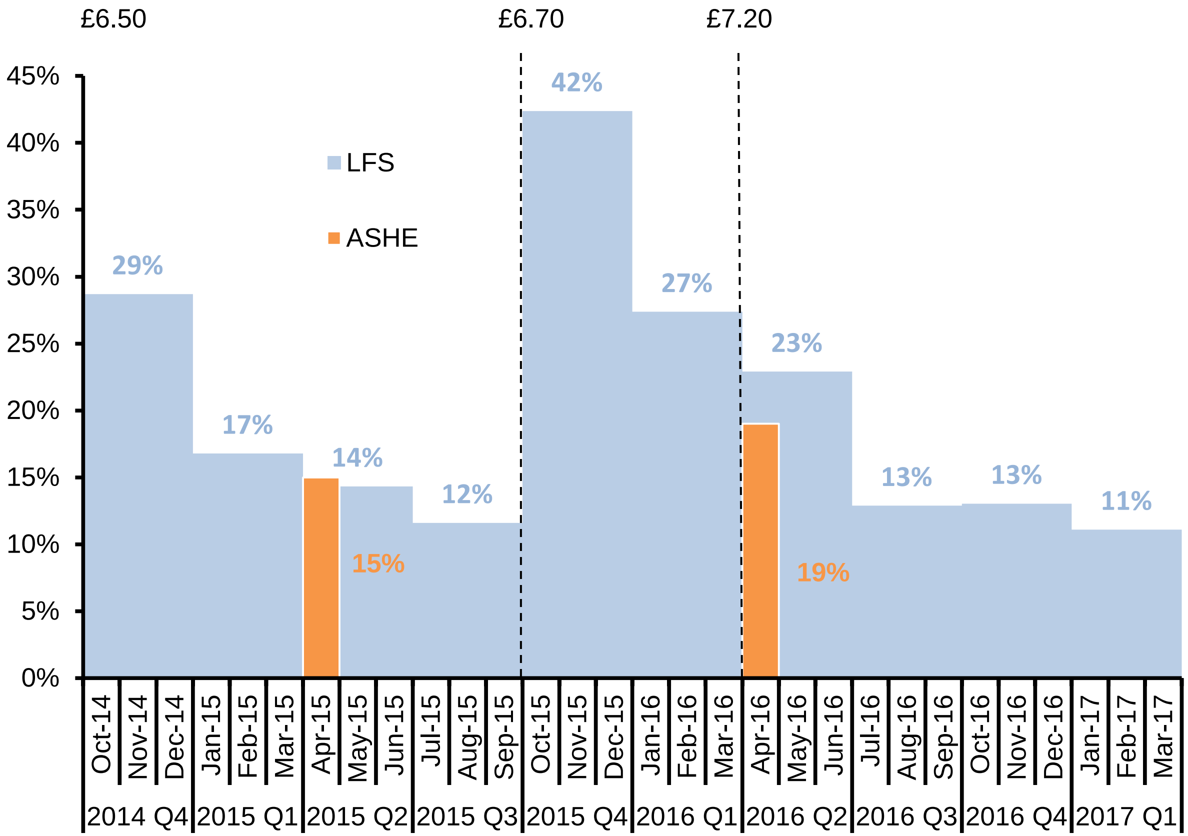
Source: LPC estimates using:
a) Annual Survey of Hours and Earnings (ASHE), data excludes first year apprentices, UK
b) Labour Force Survey Microdata, income weights, quarterly, not seasonally adjusted, UK

Accurately measuring underpayment is challenging. This chart compares two estimates of the number of underpaid workers derived from the Annual Survey of Hours and Earnings (ASHE) in orange, and the Labour Force Survey (LFS) in blue. Both sources have their flaws, the details of which can be found in the full report.

- The LFS data illustrates the strong frictional nature of underpayment: the number of workers affected is at its highest immediately following each uprating, but then falls by around half in the six to nine months that follow.
- This frictional pattern explains the large rise in the ASHE measure of underpayment following the introduction of the NLW. The change in the NLW timetable – with upratings taking effect from April instead of October – meant that the 2016 ASHE measured underpayment immediately after its introduction and therefore the peak in the year.
- The LFS measure of underpayment was actually higher immediately following the October 2015 uprating to £6.70 (2015 Q4) than it was following the introduction of the NLW. This may be because the NLW was extremely high profile in nature and was accompanied by the Government's communications campaign, driving awareness and therefore compliance
- Comparing LFS data from the fourth quarter of 2016 with the second quarter of 2015 gives an indication of the change over time, as these both take place two quarters after an uprating. On this measure the number of underpaid workers aged 25 and over appears to have increased by around a third from 203,000 to 278,000.

As a share of coverage (workers paid at or below the NMW/NLW) underpayment appears to have fallen slightly

Figure 2: Estimates of underpayment as share of low-paid workers for workers aged 25 and over

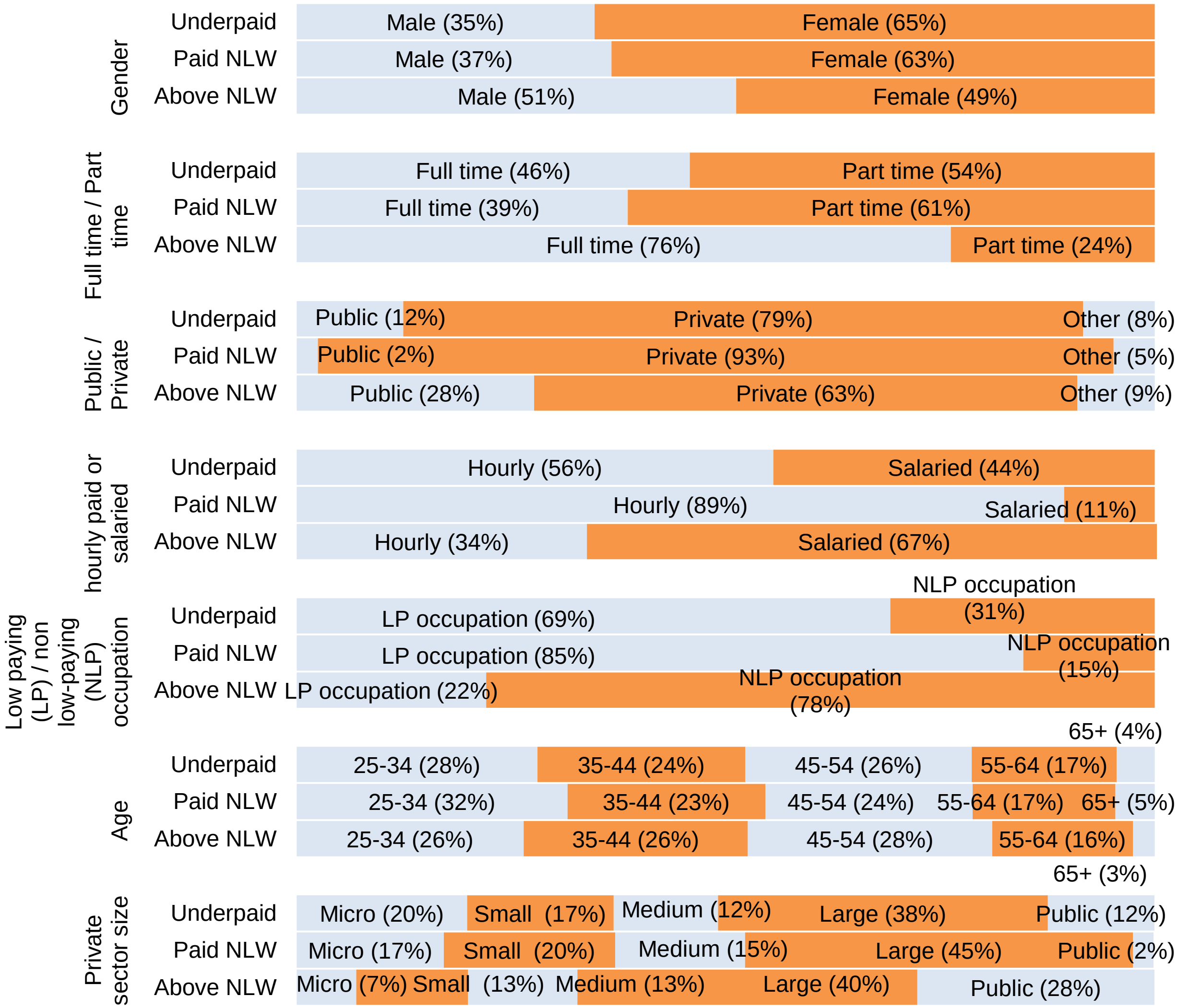


Source: LPC estimates using:
a) Annual Survey of Hours and Earnings (ASHE), data excludes first year apprentices, UK
b) Labour Force Survey Microdata, income weights, quarterly, not seasonally adjusted, UK

- This chart shows the share of low-paid workers (those paid within 5p of the NLW or below), which we refer to as coverage, who appear to be underpaid.
- As a share of coverage underpayment was between 19 and 23 per cent immediately after the NLW uprating in April 2016.
- The previous slide showed an increase in the estimates of the number of underpaid workers following the NLW's introduction from 203,000 to 278,000. However, because the NLW resulted in a significant increase in coverage underpayment as a percentage of coverage appears to have fallen very slightly from 14 to 13 per cent between 2015 Q2 and 2016 Q4 (which both occur two quarters after an uprating).

Underpaid workers tend to be female, part-time and hourly paid, but salaried and public sector workers appear over-represented

Figure 3: Breakdown of underpaid workers aged 25 and over (ASHE, 2016)



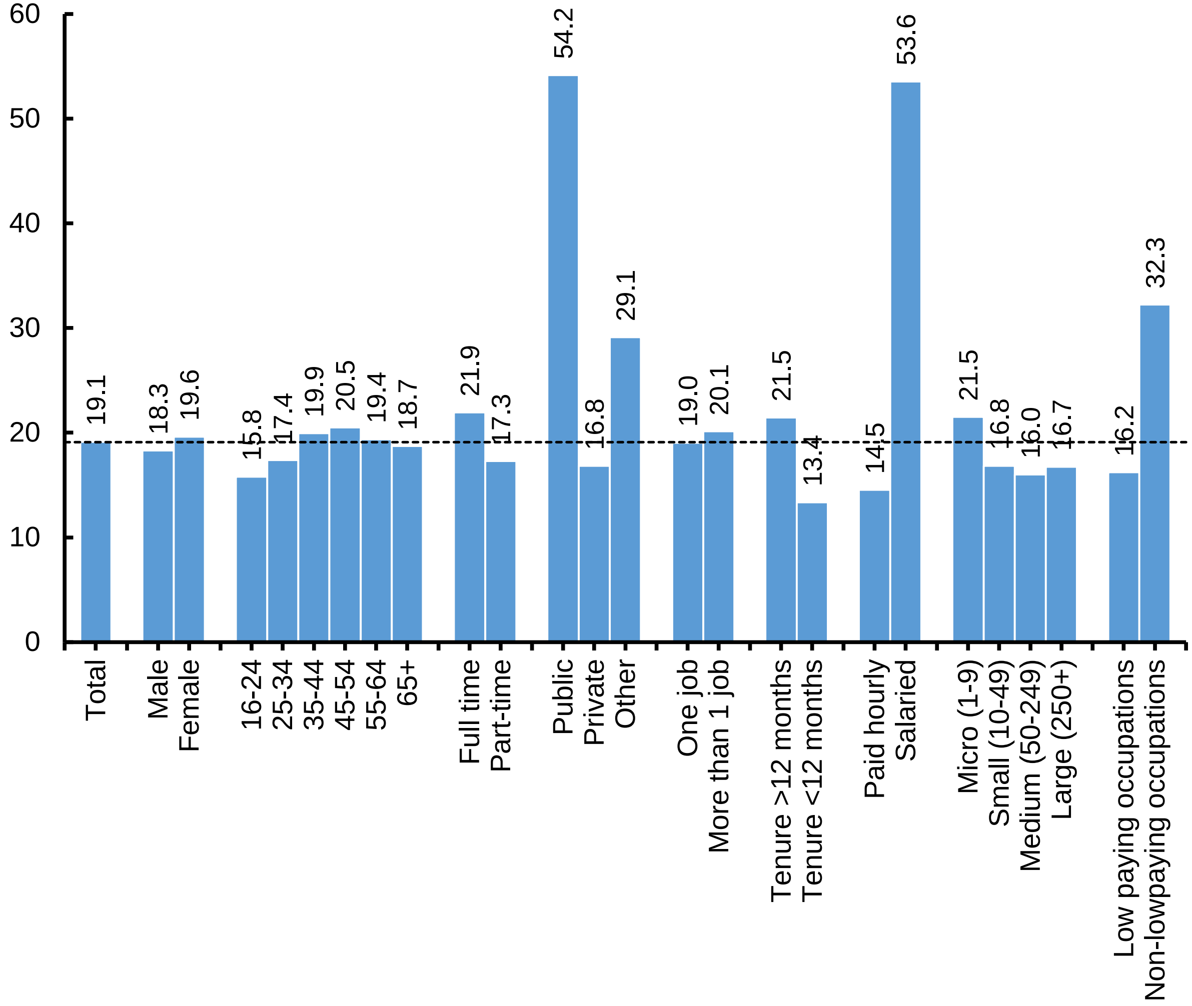
Source: LPC estimates using Annual Survey of Hours and Earnings (ASHE), data excludes first year apprentices, UK

This chart breaks down all underpaid workers identified in the ASHE in April 2016 by a range of different personal and work related characteristics and compares them to NLW workers (i.e. those paid within 5p of the NLW) and all workers paid above the NLW i.e the rest of the employed workforce. A number of things are apparent.

- Underpaid workers are more likely to be female, reflecting the fact that the majority of low-paid workers are also female.
- Slightly more underpaid workers are part-time than full-time but slightly less than low-paid workers as a whole and significantly less than those paid above the NLW
- The vast bulk of underpaid workers are in the private sector but, in comparison to low-paid workers more generally, there is a larger share are in the public sector
- The vast majority of NLW workers are paid hourly. By comparison salaried workers are over-represented amongst the underpaid. In many cases neither salaried workers nor their managers are keeping track of their hours those at the lower paid end risk falling into non-compliance.
- The age profile across the three groups doesn't vary significantly
- The majority of underpaid workers tend to work in small or medium sized businesses, but just under two fifths work for larger private sector employers.

Underpayment as a share of low-paid workers varies across a range of job and personal characteristics – the public sector and salaried workers stand out

Figure 4: Percentage of low-paid workers who are underpaid for various types of worker aged 25 and above (2016)

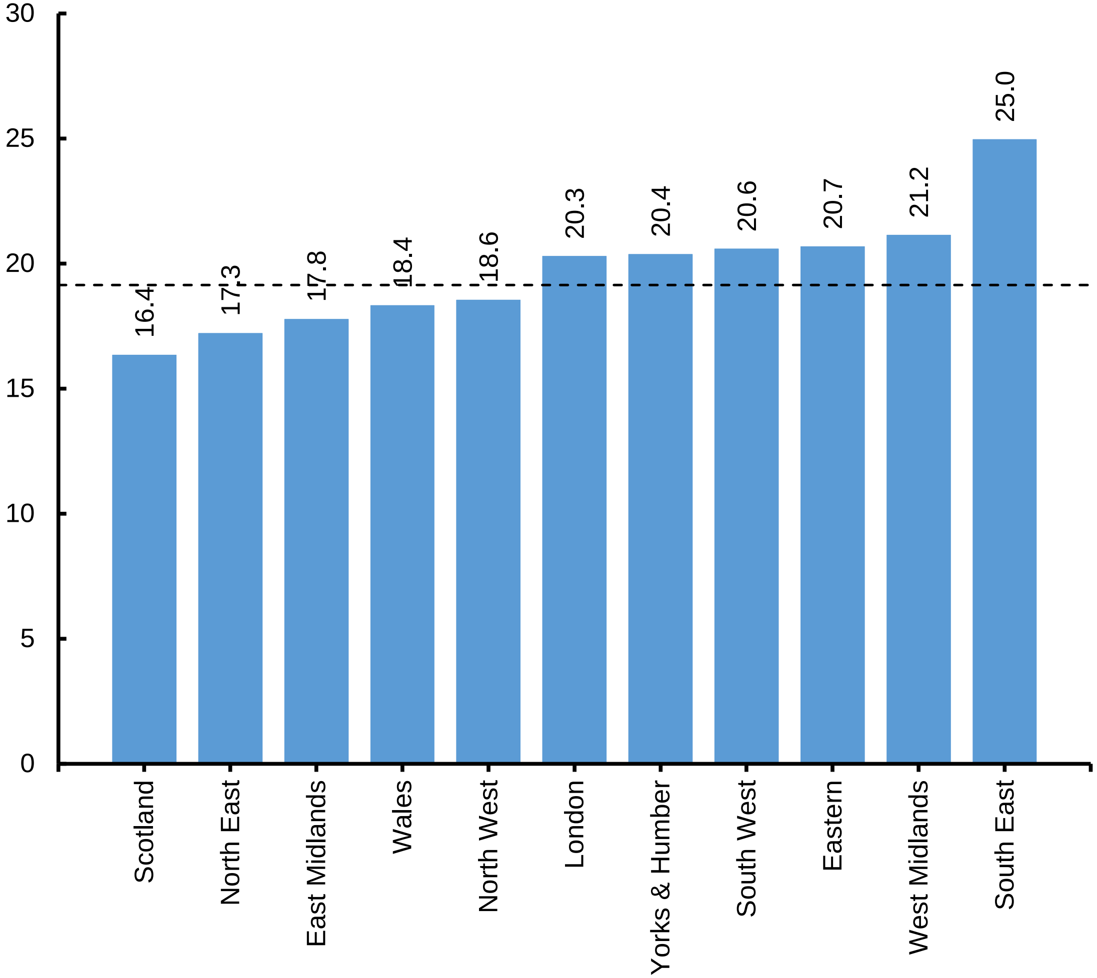


Source: LPC estimates using Annual Survey of Hours and Earnings (ASHE), data excludes first year apprentices, UK

- Figure 4 shows the share of low-paid workers in each group who are underpaid for a range of different characteristics.
- Overall almost 1 in 5 low-paid workers aged 25 and over were underpaid in the ASHE survey in 2016. There is little difference in the rates between men and women or between different age groups. There is also little difference across different sized firms, although workers for the smallest have an above average chance of being underpaid.
- The underpayment rates that stand out are those for the public sector, salaried workers and, again perhaps counter-intuitively, for those working in non-low paying occupations.
- Perhaps because in some cases neither salaried workers nor their managers are keeping track of the hours they work and their hourly rate of pay, those at the lower paid end risk falling into non-compliance.
- The high rate in the public sector is harder to explain. Although it is important to remember that these workers tend to be better paid and so coverage is very low. Just 1 per cent of public sector workers are paid the NLW, compared to 9 per cent in the private sector. So underpayment as a share of coverage is a relatively high percentage of a very small group.

Underpayment as a share of low-paid workers varies across different nations and regions of the UK

Figure 5: Underpayment rates by nation and region of the UK (workers aged 25 and above)



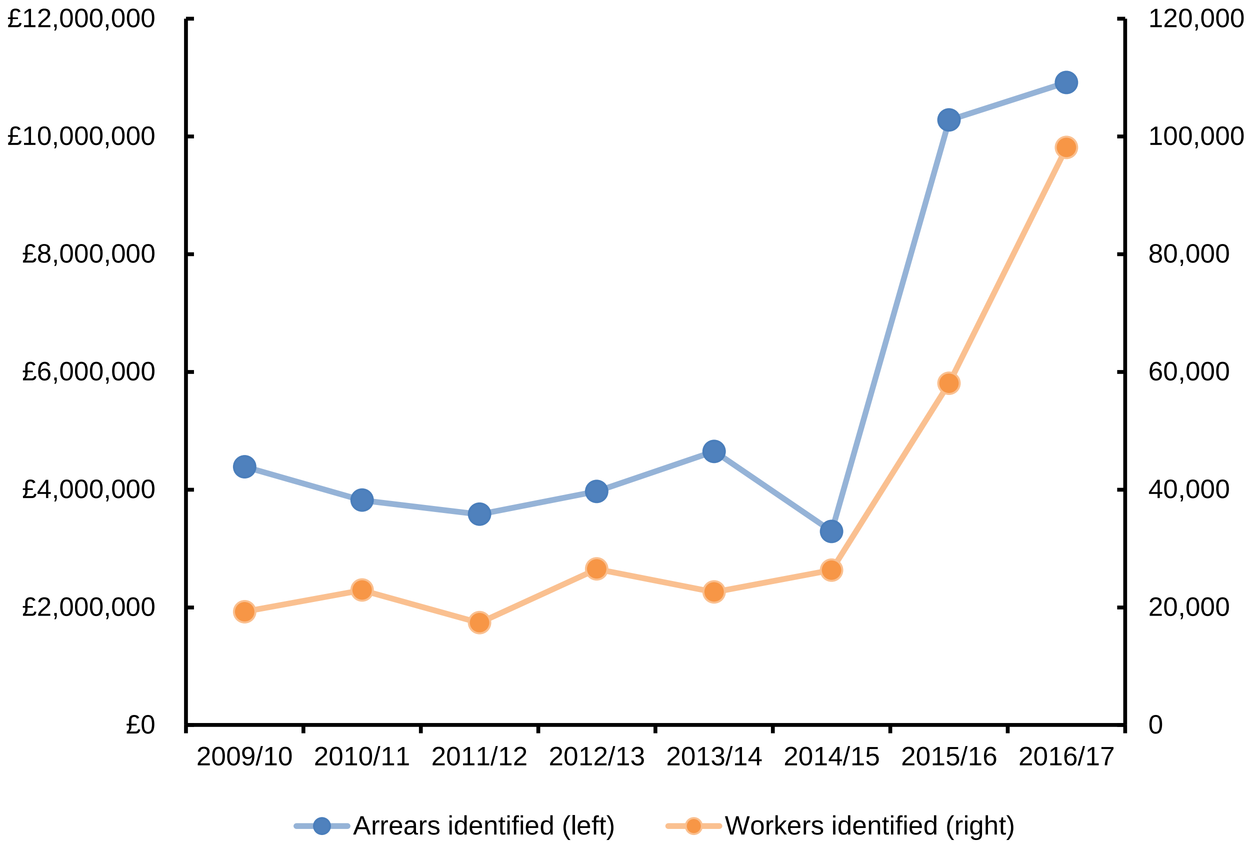
- In geographical terms underpayment as a share of low-paid workers tends to be lower in areas where coverage is highest, for example the North East, East Midlands and Wales. This may be down to the fact that high coverage brings and greater levels of high awareness with it, perhaps because more low-paid workers are paid hourly, making the appropriate pay levels more visible.

- This may explain the high levels in the South East – because coverage is lower there are lower levels of awareness. The part of the UK that stands out is Scotland which has both low coverage and the lowest underpayment rate.

Source: LPC estimates using Annual Survey of Hours and Earnings (ASHE), data excludes first year apprentices, UK

There have been large increases in the level of arrears and the number of workers found to be underpaid in HMRC's investigations

Figure 10: Total arrears identified and total workers identified in HMRC enforcement

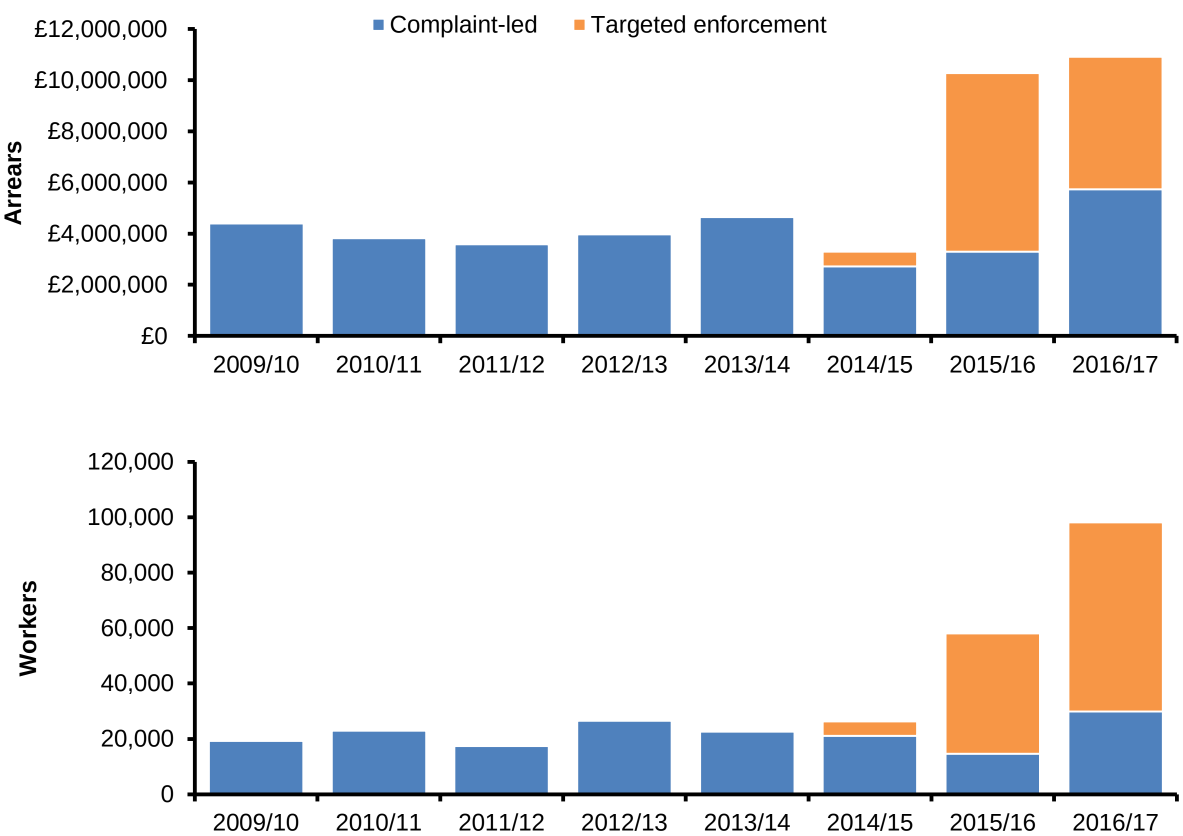


- HM Revenue and Customs (HMRC) is the government department responsible for enforcing compliance with the NMW/NLW on behalf of BEIS, the Department for Business, Energy and Industrial Strategy.
- This chart shows the number of workers and arrears identified in HMRC's investigations
- The number of workers for whom HMRC have found arrears more than doubled in 2015/16 to 58,000 and increased again to a record 98,000 in 2016/17 from an average of around 25,000 workers per year over the preceding six years.
- Arrears increased by a similar margin, from around £4 million per year over 2009/10 to 2014/15 to just over £10 million in 2015/16 and 2016/17

Source: LPC analysis using BEIS data from "National Minimum Wage: Government evidence to the LPC"
https://www.gov.uk/government/collections/national-minimum-wage#government-evidence-to-the-lpc

HMRC has shifted its approach to more targeted enforcement and this, alongside self-correction, accounts for the increase in arrears and workers

Figure 8: Total arrears and workers identified in cases by complaint led and targeted enforcement cases

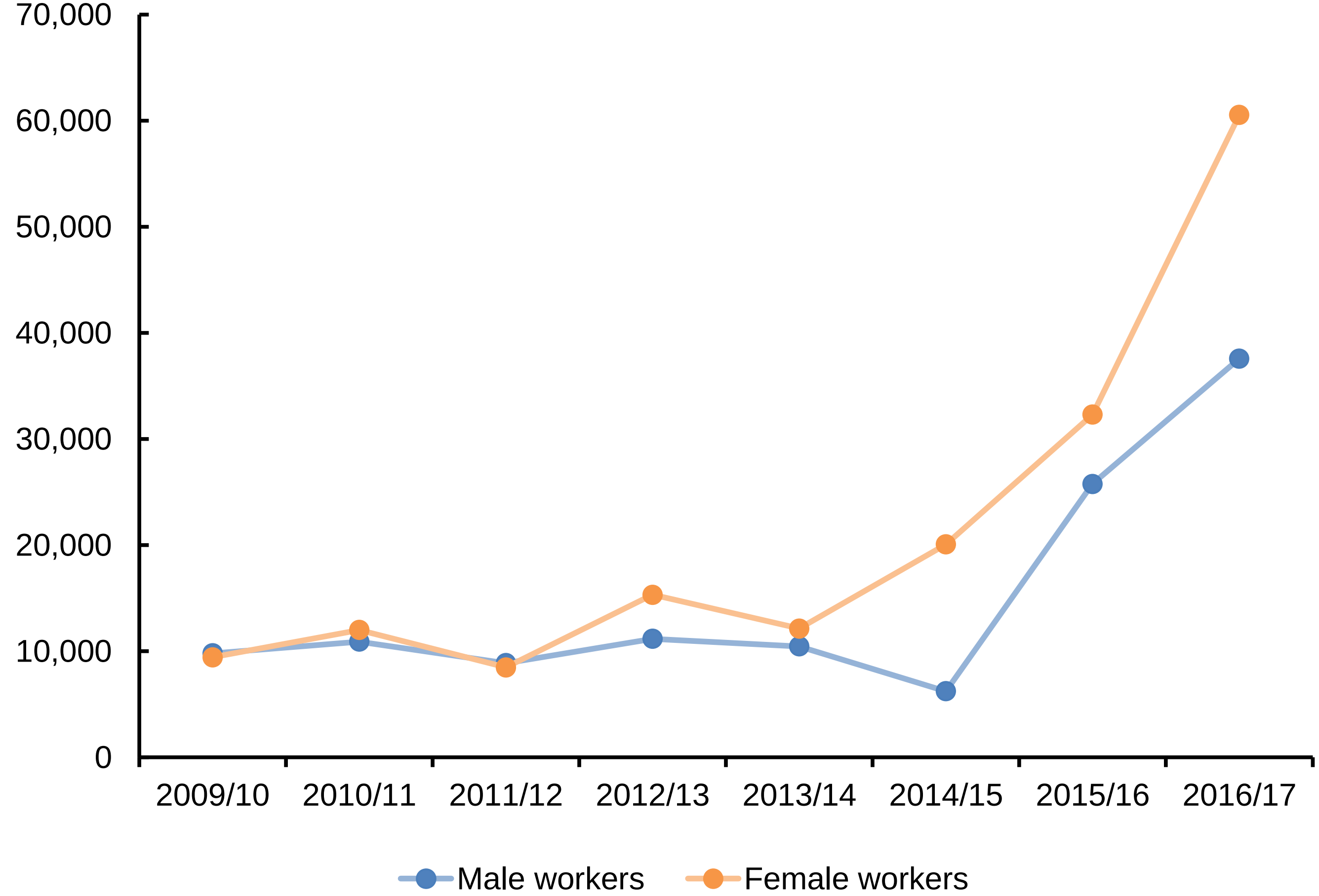


- These charts show the total arrears and the number of workers identified in cases by whether the originated from a complaint or from targeted enforcement.
- Targeted enforcement now accounts for a much larger share of arrears and workers than previously.

Source: LPC analysis using BEIS data from “National Minimum Wage: Government evidence to the LPC”
https://www.gov.uk/government/collections/national-minimum-wage#government-evidence-to-the-lpc

It is possible that HMRC's pro-active approach is compensating for some groups' inability or unwillingness to complain

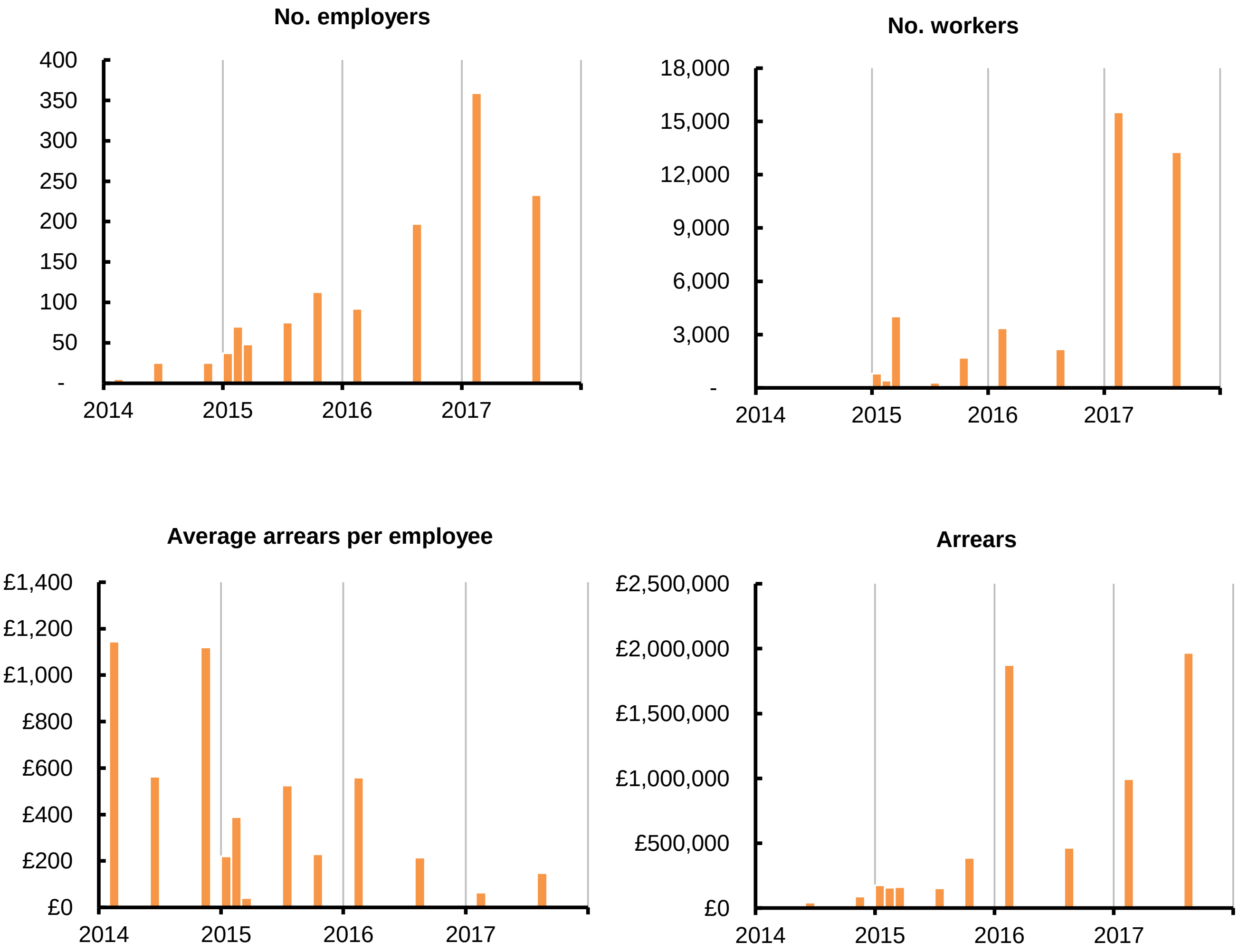
Figure 10: Gender of workers identified in HMRC enforcement cases



- This chart shows the number of workers found to be underpaid by HMRC in their investigations by gender. The chart shows that in the between 2009/10 to 2011/12 there were roughly equal numbers of male and female workers identified. But in the most recent data for 2016/17 female workers represent around two thirds of workers identified in cases by HMRC. This matches the proportion of low-paid workers we estimate to be female in Figure 3.
- This is despite the fact that female workers only make up just over half (56%) of complainants to ACAS, the official route for complaints by workers.
- This suggests that the more pro-active approach to investigations may be helping to compensate for the reluctance or inability to complain that some groups of workers may have.

Source: LPC analysis using BEIS data from "National Minimum Wage: Government evidence to the LPC"
https://www.gov.uk/government/collections/national-minimum-wage#government-evidence-to-the-lpc

Use of naming of employers found to underpay has increased, but the average arrears per worker has declined

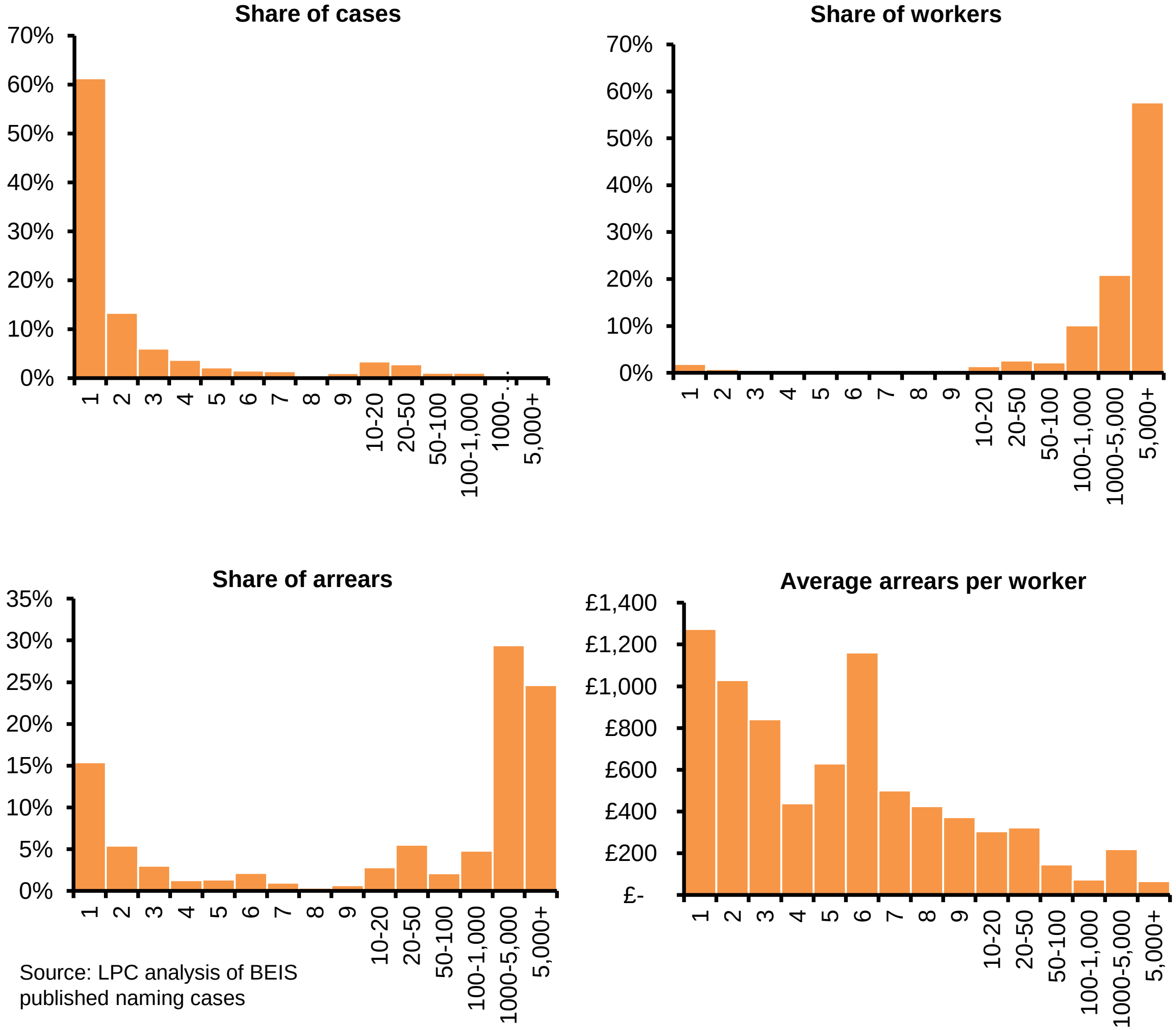


- These charts show the number of workers, employers, total arrears and arrears per head involved in each of the naming rounds carried out since 2014.
- The number of employers named has steadily increased across rounds, as has the number of workers involved with those cases.
- Average arrears per worker seem to be declining across naming rounds. This is a result of the larger cases, which tend to involve many more workers but have lower arrears per worker. The Debenhams case again exemplifies this - workers were owed just £11.48 each on average.

Source: LPC analysis of BEIS published naming cases

Cases involving 1 or 2 workers are where workers tend to lose out most financially, but larger cases may involve thousands of workers

Figure 14: Distribution of naming cases by the number of workers involved in each case



Source: LPC analysis of BEIS published naming cases

- These charts illustrate the distribution of naming cases by the number of workers involved. The top left panel shows that the vast majority of cases involve just one worker (784 out of 1,280 or 61 per cent). The top right panel shows that these single worker cases account for just 2 per cent of workers in all naming cases.

- Unsurprisingly, the cases involving more workers account for more, those involving more than 1,000 workers accounted for 79 per cent of workers involved in naming cases – just over 32,000 workers. But there are just 6 cases like these that have been named so far.

- The average arrears per head tend to decline with the size of the case (bottom right panel in Figure 14). Cases involving two or fewer workers have on average over £1,000 in arrears per worker, compared to an average that is one tenth of that amount for cases involving 100 or more workers. So even though cases with one worker account for just 2 per cent of workers identified, they account for 15 per cent of the total arrears.

- The larger cases affect many thousands of workers but it is the smaller cases, those involving just one worker, where workers seem to lose out the most financially on average.

Recommendations

- Government should fully evaluate its communications efforts and look to repeat them each year alongside the NMW (National Minimum Wage) and NLW upratings if they are shown to raise awareness and reduce underpayment. This should be combined with a broader approach aimed at raising the number of formal complaints made by workers to the ACAS helpline, which remain low relative to our estimates of the scale of underpayment. This includes better publicity around the third party complaints process, developing case studies and/or guidance based around successful complainants and publicising the improvements in the time taken to resolve a case.
- For employers we recommend improved guidance around the technical errors that other employers have made, so they can learn from each other's mistakes. But we also need action on recalcitrant employers, so efforts to both increase the number of prosecutions and publicise those that do occur would be welcome. The naming rounds, including the most recent in August of this year, have been successful in generating press attention and raising awareness. Making naming of employers a more regular and predictable occurrence may help build on this momentum and increase press anticipation of the announcement.
- Qualitative research continues to show that a small core of recalcitrant employers remain unconcerned by the consequences of their non-compliance. For example, some believe that their staff won't complain, others are unaware of the increased resources for HMRC or the increased use of naming. Action to publicise the increase in enforcement activity e.g. the number of complaints or the number of cases investigated, perhaps by sector and locality may help get the message through. Adding a simple 'tick box' declaration to payroll software whereby the employer is asked to confirm that all of their staff are paid at the correct level could also be a helpful 'nudge' to encourage compliance.
- Finally, there are a range of actions for HMRC. We recommend that HMRC establishes information systems that allow Government to learn as much as possible about the nature and extent of non-compliance from the cases it investigates. These information systems should provide enough information to monitor how well policy is responding to the challenge overall as well as on specific groups and issues. The new apprenticeship levy system, also managed by HMRC, will provide intelligence on which employers are paying the levy and, potentially, what types of apprenticeship they are studying. If this is the case it may allow HMRC to identify employers at risk of underpaying their apprentices. HMRC should use this intelligence as part of their risk based approach to proactive investigations to help tackle the high levels of non-compliance amongst apprentices. Finally, there are opportunities for HMRC to gather intelligence from other parts of Government. This includes testing processes for automatic referral from other inspection bodies and working with Jobcentre Plus' Universal Jobmatch Team to identify online job adverts that appear to be non-compliant.

For the full report visit:

www.gov.uk/government/publication/non-compliance-and-enforcement-of-the-national-minimum-wage-september-2017

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