

# Wage Reform And Tripartism: A Test Of Trust At Work

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This article looks at Singapore's history of wage reform and at the role played by the National Wages Council (NWC) to ensure industrial harmony through the implementation of flexible wages. Technical issues aside, it is evident that the success of wage reform lies in the foundation of trust between the tripartite partners in labour, management and government. Conversely, a lack of trust between any of the three partners will pose a serious threat to the building of a nimble yet stable economy in the face of globalization's ruthless hand.

## Overview of Labour Relations and Wage Policy

**G**lobally, good labour relations are never to be taken for granted. Frequent strikes in developed countries cripple economic progress, disrupt daily lives and affect the livelihood of many. Singapore's labour relations have come a long way from the high unemployment in the early 1960s; through the tight labour market and rising wages of the 1970s; riding the storms of recession in the mid 1980s and 1997 Asian crisis.

Wage policy in the early 60s was based on the bargaining strength of unions and management. There was unemployment and workers readily took to the streets to demonstrate their strength. Although the Government attracted many foreign investors to start labour-intensive industries in Singapore, it soon had to intervene in the labour market and industrial relations. For example, to minimise disputes on working conditions, the Employment Act was introduced in 1968 to spell out such conditions, and the basic rights and duties

of employers and employees.

By the 1970s, the fruits of Singapore's industrialisation programme manifested themselves in full employment and rising wages. With a tight labour market, the Government feared unbridled wage increases and disputes which could dampen investors' confidence and economic growth. The Government intervened and laid the foundation for tripartite relations among government, employers and workers, which paved the way for Singapore's subsequent industrial peace.

## History and Philosophy of the National Wages Council

**T**he NWC was set up in 1972 as a tripartite body comprising a neutral chairman, government representatives, employers and unions. The NWC was set up at the suggestion of the late Dutch economic advisor to Singapore, Dr Albert Winsemius. Its philosophy is grounded in corporatism, which is a traditional feature of the Dutch labour market.<sup>1</sup> Essentially, corporatism is a form of organization where government and organized interests (mainly trade unions, employer associations) jointly develop and implement social-economic policies. The government does not operate at a distance and organized interest does not have to lobby — it is a welcome partner in the conference room. There is tripartite consultation at all stages of legislation and policy making. This model is in contrast with that of non-corporatist countries such as the UK, which have very decentralized, firm-level bargaining and no institutionalized consultation between government and organized interest. In the UK labour relations are complicated by political interests, especially the power wielded by the unions over the British Labour Party.

<sup>1</sup> Dutch labour relations had an early tradition of consultation and bargaining at the central level, with wage cost as a key variable, and with workers and employers dealing with each other and with the government. There was also a tradition of government intervention, interwoven in a process of consultation and advice, not as bluntly imposed rulings. In the Netherlands in 1960s, corporatism was evident in an institution called the Social Economic Council, which was a public organization with an independent chairman, and equal number of representatives from union federations, employer associations and independent members, appointed by the government.

The first Singapore NWC chairman (whose tenure lasted from 1972-2001) was academic economist Prof Lim Chong Yah. The representatives were top leaders from labour, management associations, permanent secretaries of ministries and chairmen of statutory boards. The Council is essentially a negotiating body at the national level for national guidelines on wages, bonus and benefits. The government representatives played an integrative third party role given their ready access to statistical information.

Annually, the NWC reviews wage rates in relation to the economy's performance. It then recommends appropriate wage adjustments and submits them to the Government for approval, which has the power to accept, reject or modify the recommendations. Over the years the NWC's recommendations have gained credibility and authority as they have all been accepted by the government.

The key to the NWC's success is the involvement of and frank exchange between employers and unions, with the Government performing an advisory role in providing information about the economy, labour market and growth prospects. The NWC undertakes a holistic review of Singapore's economic indicators such as productivity growth, international competitiveness, unemployment, inflation and the global economy.

NWC recommendations are meant as guidelines for negotiation between employers and the unions. They have provided a bedrock for industrial peace and ensured conducive conditions for Singapore's continued growth, prosperity and employment. Two major NWC contributions are the wage restraint policy in the 1986 recession to help companies regain competitiveness and wage reform by the introduction of a flexible wage system.

## NWC Recommendations 1972-1988

### *1972-78 Moderate wage increase*

During the 1973-74 world recession, the NWC recommended moderate wage increases as Singapore's aim was to attract foreign investments. When global inflation affected Singapore, the NWC recommended high wage increase in 1974. Between 1975 and 1978, the NWC recommended moderate wage increase as there was slower growth with the economy recovering from the oil crisis.

### *1979-84 High wage increase*

The early part of this period was characterized by labour shortage and low productivity. In line with the government's push to restructure the economy through more high value-add and higher-skilled industries, the NWC pushed up wages. This would encourage more efficient use of scarce manpower through automation. In 1980 and 1981, the NWC encouraged wage increase to be based on individual performance so as to enhance labour productivity. For the rest of the period, high wage increases continued. By 1985, Singapore's labour costs were substantially higher than its competitors, with productivity growth lagging behind real earnings.

### *1985-87 Wage restraint*

By the second half of 1985, Singapore had slipped into its first post-independence recession. GDP suffered its first negative growth since 1964. Unemployment hit 6.1% and about 95,000 jobs were lost. The Government took a 15% cut in CPF rate to cut wage costs. To reinforce this counter-recessionary strategy, the NWC recommended severe wage restraint. Unions and employers accepted the call. Increase in average earnings slowed from 7.9% in 1985 to 0.8% in 1986. These cost-cutting measures in 1986/7 brought down unit labour costs in manufacturing by more than 15% and the economy recovered.

### *1988-present Qualitative wage adjustments*

The 1986 recession revealed the rigidities of the wage system and spurred the Government to rethink its competitiveness strategies, through the setting up of the Economic Committee in 1986. NWC's quantitative guidelines in the past were not suitable for such turbulent times and had in fact added wage rigidity to the system. In charting a new direction for the economy, the Government had to find measures to add flexibility into the wage system without creating instability through direct negotiation that was not anchored by NWC quantitative benchmarks. Otherwise, the industrial peace that had been built over the decades would be at stake.

## Evolution of Wage Reform

**T**he Economic Committee (EC) in 1986 had a **Sub-Committee on Manpower** that studied the rigidity in Singapore's wage system and the need for wage reform, including the need for a fine-tuning of NWC's role and responsibilities.

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The rigidities include a seniority-based system that was linked to years of service rather than the company’s profitability or individual’s contribution. Further, there was a long salary time scale with high maximum pay and fixed annual increments guaranteed to all employees. The long range within each salary band implied that at each grade, the minimum and maximum pay was quite wide apart. An employee who stays in that same grade doing the same job gets fixed annual increments until he hits the ceiling or maximum pay in his grade. Over the years, his salary would become quite high for doing that same job he did many years ago. As these increments were built into the basic wage structure, they became a financial burden for firms, especially those with many older workers. Consequently, these older workers had to be retrenched during the recession.

The EC therefore recommended the removal of wage rigidity so that wages would reflect the job worth and the employees’ productivity. It also advocated a flexible wage system’ and encouraged companies to adopt variable components such as bonuses, profit-sharing or productivity incentives.

The EC also fine-tuned the role of the NWC by recommending a move away from *quantitative* to *qualitative* guidelines after allowing a few years of adjustment for companies and unions to prepare for a flexible wage system. These will be done by sectors and allow market forces to determine the appropriate wage levels, with the actual amounts to be annually negotiated between employers and unions.

### The Flexible Wage System: Rationale and Features

A flexible and competitive wage system will benefit companies in three ways. First, it will allow companies to make fast adjustments to their cost structure during volatile business cycles and shocks. By responding more

rapidly to business conditions they will be able to remain cost-competitive. Next, they will be able to cut wages swiftly to survive tough times and reward workers in good times. These can be done by linking the company’s salaries to its profitability. Rewarding employees for their performance will also motivate staff. If designed properly, the flexible wage system (FWS) will also help to preserve jobs by helping employers to cut costs rather than to retrench workers.

Implementing a new approach to wage policy is a true test of tripartite relations in Singapore. The successful adoption of a flexible wage system in most companies requires the common understanding and acceptance of its benefits by employers and unions; high-level management buy-in and leadership by example; and overcoming implementation issues such as overhauling present HR management systems.

The tripartite Sub-Committee on Wage Reform formed in 1986 studied the implementation issues. The Sub-committee highlighted five principles to help companies reward workers fairly without affecting their cost-competitiveness:

1. Wages should reflect value of the job
2. Wage increases should lag behind productivity growth
3. Wage increases should consider the company’s profitability and individual’s performance
4. Wage increases should not always be given on a permanent basis
5. There should be stability in the worker’s income.

The features of the flexible wage system are therefore:

1. a basic wage to reflect the value of job and provide income stability.
2. an Annual Wage Supplement (AWS) of 1

month's basic wage which may be adjusted under exceptional circumstances.

3. a variable wage component based on a company's performance to be paid yearly or half-yearly. Together with the AWS, up to 20% of wages can be made variable.

Further, the FWS should give small increments to reward length of service, loyalty and experience. To better reflect job worth, the maximum and minimum ratio in a salary range should be about 1.5 times. Variable payments can be from profitability or productivity indicators or from a combination of both.

### Introducing the Flexible Wage System: 1986-2004

#### *Public Sector Wage Reform*

Before 1986, wage increases were paid directly to civil servants through their base salaries, without any consideration for variability. In 1986, a task force was appointed by then Finance Minister to consider how the public sector could adopt a FWS. The form of the new civil service flexible wage system then looked like this:

1. A basic wage
2. A monthly variable component (MVC)
3. A variable 13<sup>th</sup> month NPAA
4. A mid-year or year-end variable bonus (Annual Variable Component or AVC)

With this wage system, all adjustments to wages will first be made through the variable bonus. If a downward adjustment is warranted and exceeds the amount of the mid-year or end-year variable bonus, the monthly variable component (MVC) and/or 13<sup>th</sup> month NPAA can then be reduced. The intention was to grow the AVC to about 2 months that can be adjusted annually in line with national economic growth.

Being the largest single employer in Singapore employing about 145,000 people, the public sector's adoption of the FWS would have a large demonstration effect for private sector firms still unsure about wage reform. The Task Force's recommendations were accepted by the Government for implementation on 1 July 1988.

#### *Teething problems*

In 1993, the NWC appointed a tripartite Review Committee to study whether the objectives of the FWS had been achieved and how to

recommend refinements to the system. Some of the problems identified included the absence of a proper performance appraisal system to reward individuals; the AWS amounting to more than one month into the basic wage; difficulties in interpreting and measuring profit and productivity; capping of bonus at 2 months' wages, as well as the reluctance of employers to share information with employees and unions.

#### *Negotiations Requirements*

To implement a FWS, employers and unions need to agree on wage changes. They need to have good information on economic, labour market and wage-related indicators. They also need to measure the company's performance and to have clear links between wage and productivity. In essence, they must agree on a mutually-acceptable variable component. Union leaders therefore have to be as knowledgeable as their management counterparts, and to be aware of the factors influencing employees' productivity such as skills, technology, training needs and membership profile. To enhance information sharing, agencies such as NTUC, Singapore National Employers' Federation (SNEF), Labour Ministry and the National Productivity Board played an important role. Surveys, data and training for implementing job evaluation systems were conducted to facilitate the process.

#### *The First Test of the FWS: The Asian Financial Crisis*

The 1998 Asian Financial Crisis was a key test of the soundness of the Civil Service's Flexible Wage System. The Civil Service was able to quickly react to reduce wage cost, cutting the AVC from 2 months to 0.75 month in response to the grim economic climate. In 1999, as the reductions to annual components were not sufficient, cuts to the gross monthly salaries of the civil servants were further implemented. Public officers in the higher divisions were given wage cuts of up to 3%, with Ministers taking the lead with a 5% cut. These wage cuts were effected using the variable NPVP component, and would not have been possible without close consultation with the unions and their support. When Singapore's economy made a quick rebound in 2000, the Civil Service was able to restore the wage cut made in 1999 quickly, and to pay a 1.75-month AVC. It was a strong endorsement of the FWS.

#### *September 11, the Iraq War and SARS*

The FWS continues to be an important tool that enables the country to weather the impact of other

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storms, such as the economic uncertainties arising from the September-11 attacks, war in Iraq and SARS. It allowed the Civil Service to make rapid and timely adjustments to Civil Service pay in response to the crises. In November 2001, in response to the economic uncertainty, Ministers and senior civil servants again led by example, taking wage cuts of up to 10%. In July 2003, a further 10% wage cut was taken off the gross monthly wages of Ministers and senior civil servants. In November 2003, in view of declining private sector salaries as shown by our benchmark analysis, the Civil Service re-based the AVC rate from  $\frac{3}{4}$  month to  $\frac{1}{2}$  month. Bearing in mind a monthly salary cut would more directly affect the daily livelihood of officers, cuts were made to the AVC. As wage levels vary with the economy and labour conditions, the FWS will continue to be an important tool for us to use to respond quickly to the changing conditions.

### How Far Have We Come With Wage Restructuring?

SAARs necessitated many emergency measures to cope with the sudden plunge of businesses and job loss. Workers have understood and witnessed the real threat to their employment and some companies were forced to make wages variable. The unions, particularly the Food, Drinks and Allied Workers Union (FDAWU) supported the moves to cut costs such as compulsory no-pay-leave, shorter work weeks etc. Wage cuts were also taken by management. Due to the hotels' close cooperation with the unions, morale was kept up and trust was preserved between workers and employers. Therefore hotel workers were not retrenched and the efforts paid off when business returned and hotels could ramp up their services quickly and economically. From these experiences, hotels have seen the benefits of restructuring and are committed to implementing flexible wages.

This is however not the case across the board. While most companies recognize the advantages of a more flexible and competitive wage system, till today many companies have not taken the step because of the lack of expertise and resources.

The call for a more flexible and competitive wage system was reiterated in the reports of the **Economic Review Committee (ERC)** and **Tripartite Taskforce on Wage Restructuring** (formed in July 2003 by NWC recommendation) which submitted its report in Jan 2004. The latter was formed by government, SNEF and NTUC to push for wider implementation of wage restructuring. The Competitive Base Wage System (CBWS) model was recommended. This was essentially based on five wage principles, namely sustainable growth, competitiveness, flexibility, motivation and stability. These are similar to the principles behind the FWS with the following new principles:

- Sustainable growth: The wage structure should support business sustainability, investment, job creation and better opportunities for all.
- Motivation: Management should incentivise employees to give their best and add greater value. Management should also take the lead in wage restructuring in bad times.

There is a need to extend the efforts to more sectors of the economy as well as to small and medium-sized companies. The ERC recommended a 30% variable component (20% AVC and 10% MVC) for rank-and-file employees, 30-40% for middle management and no less than 40% for top management. The Taskforce also recommended that the AVC should reward employees for their individual performance as well as their contribution to company performance. The MVC should be linked to company performance and by virtue of it being paid out monthly, allows companies to adjust wages when faced with short-term unexpected economic shocks without having to wait until the end of the year.

The civil service has been taking the lead in wage reform, but it remains to be seen if the rest of the sectors will follow suit. Why is implementation a stumbling block for many?

### Implementation Issues

**D**uring the keynote speech at the National Tripartite Conference on Wage Restructuring on 30 Jan 2004, then DPM Lee Hsien Loong described the implementation issue as follows:

“While the arguments for wage restructuring are compelling, actually doing it is not easy. For companies it means designing workable schemes, and persuading workers of their merits in order to bring them on board. For unions it means participating in changing arrangements which workers have become used to, and taking a broader and longer term view of workers’ interest. For workers, it means accepting more variability and less certainty, in exchange for more job security and an upside when the outcome justifies that. For older workers particularly, moving away from seniority-based wages means accepting painful but necessary adjustments to improve their employment prospects.

Further, wage restructuring cannot be done by the Government alone. We cannot simply pass a law or publish a formula which applies to every company. . .

Commitment by all parties, and especially from the top, is essential.”

### Some Mindsets Must Change

**R**eform is painful. There is an inevitable conflict of interests among the various stakeholders. Good relations between workers and management and union leaders can determine the success or failure of wage restructuring efforts. Some fundamental mindsets are a hindrance.

First, one must be convinced that wage restructuring and reform are not wage cuts. Workers might not trust the company to give them an upside when times turn better, and see the designation of MVC as a cut in monthly salary. Workers must understand that companies need to make adequate profit, and that iron rice bowls are gone forever. They must also accept that it is

better to have variable wages to allow the company flexibility in tough times than to risk being retrenched. Time, dialogue, communication and information sharing are needed for workers to buy into the concept.

Second, some think the job of wage restructuring is that of the HR manager. But it is the CEO that must take the lead. It is a strategic issue of business strategy and people-management and not simply an administrative or numbers game. The employees must trust that there is a good system of Key Performance Indicators or that the appraisal system is linked to company’s performance and individual effort.

Third, timing is an issue. Some employers fear that wage restructuring will worsen the morale of a company. Others feel that while the economy is on the mend, there is no real urgency for wage reform. They would rather not have the hassle of tinkering with wages when they need to compete more aggressively for workers. Others continue to think that they can cut wages or retrench workers when the need arises hence there is no need for fundamental reform. There must also be agreement between management and unions on when MVC can be cut. Naturally unions would not want the management to dictate when an MVC cut is necessary.

Fourth, there must be willingness for the employers to share information with their workers on the company’s performance, challenges and future plans. They need to build trust and confidence with union leaders to share concerns and exchange views.

Finally, some SMEs or family-owned businesses simply do not have the expertise, resources or proper HR system to put wage restructuring in place.

### Challenges for the Future

**T**o thrust implementation forward, the Tripartite Taskforce undertook a three-pronged strategy. First, a “first wave” of successful examples of wage restructuring was created to provide “a catalyst and encourage companies to follow their footsteps. HR experts and officials from NTUC, SNEF and MOM worked closely with selected companies to kick-start the process. Second, it helped interested companies build up HR capabilities by providing training to HR consultants to build up the capacity of the HR

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industry in the medium term. Thirdly, it marketed the national wage restructuring effort through smaller platforms such as industry associations and sectoral working groups within industry so as to generate confidence and greater buy-in.

The Government, through the work of the Tripartite Taskforce, worked closely with 4 sectors (hotel, electronics, chemicals and land transport) to lead them to implement wage restructuring. The Government hopes that the rest of the companies and unions in other industries will achieve similar results. Then-DPM Lee said that he hoped by next year, over 50% of the total workforce in large companies and 40% of the total workforce in SMEs would come under some flexible wage system.

Today’s knowledge-based economy poses new challenges for wage reform. A rise in part-time and contractual work could lead to a move away from unionized labour and question the *raison d’être* of unions. In uncertain economic times influenced by the ups and downs of security and terrorist threats, it might also be harder for companies and employees to forge a common understanding of and definition of “good and bad economic times” and the need to reduce variable components to save jobs. Trust might not have time to develop a long term footing if workers are forced to move from firm to firm when jobs become more mobile. Another challenge is our ageing society which calls for equitable treatment of both young and old workers without creating disincentives for work or compromise reward for performance.

## Conclusion

**W**age restructuring is one of the key implementation challenges faced by Singapore in order to prepare for future economic challenges. The NWC remains a key

instrument for maintaining tripartite consensus and unity to serve as a foundation to build a nimble and progressive economy. Then-DPM Lee summed up the value of the NWC’s role:

“The NWC allows us to speak with one clear voice to each other, as well as to investors. This is a unique and precious advantage. Very few other countries can have the unions, employers and the Government seated harmoniously in one room discussing how to restructure wages and develop a flexible labour market.”

(Then-DPM Lee Hsien Loong’s keynote address at the National Tripartite Conference on Wage Restructuring on 30 Jan 2004)

To preserve this unique advantage, the foundation of trust cannot be shaken. Apart from unceasing government efforts, unions have a critical role to play in enabling the continuation of open and constructive dialogue between the management and workers. ■