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# 7 Business impacts

## Key points

- The cost to business, and associated implications for female employment, of direct employer financing of paid parental leave was raised as a major concern during the course of this inquiry. General government revenue funding will avoid both the (mainly transitional) costs to business from direct employer responsibility and discrimination against female employees.
- Existing entitlements to unpaid parental leave already impose compliance and other costs on business. The additional effects on business from the Commission's specific paid parental leave proposal will mainly depend on the way the proposal influences:
  - current decisions about the duration and number of parental leave absences
  - labour force participation over the longer term
  - the provision of voluntary paid parental leave arrangements.
- The Commission's proposal will impose some compliance obligations on businesses, but the impacts on individual businesses (small and large) will be modest, and will only be felt if a parental leave occurs in any given year.
- Where employers act as 'paymasters' for eligible employees with sufficient workplace tenure, advance payment of leave instalments to employers will avoid any cash flow consequences from the paymaster function. Statutory parental leave payments made via employers should not be included for determining payroll tax or workers compensation premiums.
- Continuation of superannuation entitlements during paid parental leave absences for certain eligible employees will add to business costs. While a prima facie case for employer provision of superannuation exists, the compliance burden associated with the scheme's initiation phase and current economic circumstances suggest that implementing the superannuation component should be deferred. It should be implemented following a review into the scheme three years after its inception, subject to consideration of its impacts at that time.
- A range of program design features have been incorporated to help reduce the potential uncertainty, disruption and administrative costs associated with a statutory paid parental leave scheme, especially for small firms.
- Voluntary paid parental leave schemes reflect firm-specific employment circumstances. However, a statutory leave scheme will still deliver some benefits to firms not currently offering paid leave voluntarily. But a mandatory scheme has the potential to devalue the signal that voluntary schemes send of a firm being an employer of choice. To avoid this devaluation, the Commission anticipates that many existing voluntary schemes are likely to be retained by employers.
- The scope for a statutory scheme to crowd out voluntary arrangements also depends on its relative generosity. Firms that may have considered introducing paid parental leave in the future could choose other family friendly policies as alternative employment benefits. To the extent that such substitution reflects a set of working conditions that are more highly valued by employees (perhaps due to changing societal norms), crowding out could be viewed as a positive outcome.

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## 7.1 Introduction

A poorly designed statutory paid parental leave scheme has the scope to affect business performance adversely, with potentially severe consequences for those firms operating at the margin of viability. Mitigating those potential risks is therefore an important consideration in scheme design. But implementation by the Australian Government of the Commission's proposed scheme itself is unlikely to pose major financial or other risks for the business community, primarily because the proposal does not involve a large direct financial contribution by firms (see chapter 8). That said, the extent to which paid leave affects parental choices about the duration and number of absences from work and parental engagement with the workforce more broadly would have both beneficial and detrimental implications for the business sector.

Importantly, those effects need to be viewed in the light of existing rights to unpaid parental leave and the many diverse voluntary schemes currently offered in Australian workplaces. This chapter looks at the impacts of the proposed statutory paid parental leave scheme on employers, with a particular focus on examining potential differences in outcomes across industries and between firms of different size. A summary of the specific business impacts from the Commission's proposal is provided at the end of this chapter.

## 7.2 Business costs

Employee absences impose a range of costs on firms regardless of the purpose for which the leave is taken. Those costs may include expenses incurred in hiring and training replacement staff, reduced productivity (from both the temporary and returning employee) and the costs of leave administration. The nature and magnitude of those costs will depend to some extent on the duration of leave taken, with lengthier absences (such as for long service or parental leave) generally associated with greater disruption for firms than shorter breaks.<sup>1</sup> Disruption costs may also be magnified in the case of parental leave because of the uncertainty about when (or even whether) an employee will return to work. Equally, the greater financial security that the paid parental leave scheme provides may make return dates more certain for a proportion of employees.

Business costs will also depend on firm-specific training investments, employee skill levels and the employment size of the firm. Larger firms employing less

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<sup>1</sup> Alewell and Pull (2001) note the possibility that parental leave schemes that offer employees leave of intermediate duration may involve the highest disruption costs because they render work-sharing inefficient while employing replacement staff remains impractical.

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specialised workers are likely to have greater scope to redistribute workloads to other employees and thus lower the potential cost and loss of productivity from training a temporary replacement. Smaller employers, on the other hand, are more likely to require replacement staff and this will entail a range of administrative and financial costs in addition to the direct wage burden.

The combined submission from NSW Business Chamber and Australian Business Industrial described the nature of the options open to firms and the associated costs:

When employees take parental leave, employers bear the expense of advertising and recruiting for replacement staff. Employers bear the substantial ‘on-costs’ associated with engaging new staff, including induction and training, and the inevitable period during which the new employee has reduced productivity. Then, before the employer is able to extract any significant return on investment, the employee on parental leave is due to return. Alternatively, some employer’s choose to ‘make do’ without the employee for the period of leave in which case, other employees are expected to work harder to pick up the slack and/or the employer loses some business capacity.

Small businesses and businesses in regional areas are particularly disadvantaged. In most cases they are not in the position to easily cover staff absence, particularly when skilled or professional staff are involved (sub. 134, p. 8)

And the Chamber of Commerce and Industry Western Australia (sub. 147, p. 15) estimated that the costs associated with employing a replacement employee were between 20 and 35 per cent higher than the employee being replaced.

### *Existing parental leave employment provisions already impose costs on firms*

The impact on firms of the Commission’s proposal will depend on how it affects current employee decisions about leave duration and fertility. Those effects need to be viewed in the context of existing rights to unpaid leave (which will rise from 12 to 24 months under the National Employment Standards from January 2010) and the availability of paid leave (of variable duration but typically at full pay) to more than 50 per cent of women and men in paid work. The distinction between the cost of complying with existing employment conditions and the additional costs associated with a statutory paid leave scheme was explicitly recognised in submissions by most employer groups, including that from the South Australian Wine Industry Association:

If paid parental leave is fully government funded then the direct administrative and financial impacts on employers are basically unchanged. However, indirect costs would increase with any increase in participation, i.e. more employees taking paid parental leave, as employers would be required to recruit and fill the job for a temporary period. (sub. 137, p. 4)

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Currently, rights to paid and unpaid leave and access to other forms of leave (such as annual and long service) mean the average length of maternity leave absences in Australia is around 37 weeks — considerably longer than the Commission’s proposal for 18 weeks of paid parental leave at the adult minimum wage. While this suggests *overall* duration effects might be modest (assuming voluntary schemes continue in their current form), the average figure masks considerable variability in the leave experiences of women and the industries and firms in which they are employed. As discussed in chapter 3, self-employed women and those on lower incomes typically return to work much earlier than more highly paid female employees (who are also more likely to have access to paid maternity leave).

The design of the Commission’s proposed scheme (particularly the setting of the payment rate at the adult federal minimum wage) will provide proportionately greater financial relief for women on lower incomes (especially those working part-time) and should elicit the greatest extension of leave duration from that cohort. But as mentioned earlier, disruption costs for firms from this group of employees is likely to be lower than for more highly skilled workers — at least for larger employers. Employer costs also need to be viewed in light of the relatively low risk of a paid parental leave event actually occurring for a particular firm in any given year, either currently, or under the Commission’s proposed scheme (see table 7.1 and appendix K).

However, for smaller firms with a high concentration of female employment, such as in community pharmacy, childcare services or hospitality industries, the risks will be greater (as will the associated variability and uncertainty) than the industry- and economy-wide averages shown in table 7.1. Indeed, in arguing against employer funding of paid parental leave the Pharmacy Guild of Australia observed that:

... women are over-represented both among professional pharmacy staff and pharmacy assistants. Over 85% of all persons engaged in community pharmacy are female. Between 40% to 50% of the female cohort are in the prime child bearing age range. (sub. 245, p. 4)

A range of factors determines the risk to a firm of a parental leave event occurring in any year, including the number of female employees and their age-specific fertility rates. The most common age for women to give birth is 31 years, with a fertility rate of 13 births per 100 women. As such, a small business employing five women of that specific age would face a 50 per cent probability that one or more staff members would have a child in that year. While this hypothetical example suggests *disruption* costs for certain small firms could conceivably be quite high, those risks already exist under current parental leave entitlements (paid and unpaid). The Commission’s leave proposal would only add to those disruption costs

substantively if it induced a large increase in fertility rates<sup>2</sup> — an unlikely outcome according to a recent study into Australian fertility trends:

Family policies are more powerful in providing income support, improving child and parental welfare, and serving other social goals than in affecting fertility rates. (Lattimore and Pobke 2008).

**Table 7.1 Expected number of female paid parental leave events, by industry<sup>a</sup> and firm size**  
per 100 total employees, per year

<i>Industry</i>	
Finance and insurance	2.3
Health and community services	2.3
Accommodation, cafes and restaurants	2.2
Education	2.0
Retail trade	1.9
Cultural and recreational services	1.9
Personal and other services	1.9
Government administration and defence	1.8
Property and business services	1.8
Communication services	1.3
Wholesale trade	1.1
Transport and storage	1.0
Electricity, gas and water supply	1.0
Mining	1.0
Agriculture, forestry and fishing	1.0
Manufacturing	0.8
Construction	0.5
<b>All industries</b>	<b>1.6</b>
<i>Firm Size</i>	
Less than 20 employees	1.1
20 employees or more	1.9
<b>All firms</b>	<b>1.6</b>

<sup>a</sup> Estimates derived by applying age specific fertility rates to the age and sex structure of each industry. Eligibility for paid parental leave is based on the criteria outlined in chapter 2: that is, approximately 85 per cent of all employed females are assumed to be eligible under the Commission's proposed scheme. The above estimates will exaggerate the actual incidence of the *use* of statutory paid parental leave since not all of those eligible will actually choose to take the leave.

Sources: ABS 2007 (cat. no. 3301.0); ABS 2008c (cat. no. 6105.0); ABS 2008g (cat. no. 8155.0); Productivity Commission calculations.

In addition, for the vast majority of smaller firms, the risks of disruption from parental leave would be considerably lower than those suggested by the contrived illustration shown above. By way of example, a recent press report covering the

<sup>2</sup> The extent to which labour force attachment increases will also increase the number of women potentially eligible for paid parental leave.

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introduction of paid maternity leave by a Melbourne-based recruitment firm noted that with around 60 female employees (many aged in their twenties and thirties), only about two or three of those employees were anticipated to be on maternity leave a year (Nader 2008). Citing the general manager of workplace relations policy at the Victorian Chamber of Commerce and Industry, that report also highlighted the spread of paid parental leave across firms and that such arrangements were no longer confined to larger organisations.

But participants in sectors with a high concentration of female employment argued that the Commission's estimate of the average risk facing firms across the economy significantly understated the actual risk facing their industries. Some provided anecdotal evidence of just how high the risk of a parental leave event occurring was. The Pharmacy Guild of Australia, for instance, said:

The Guild does not agree with the Productivity Commissions assumption that the chance of an employee taking parental leave is 1.1% per year as this is not accurate for the community pharmacy industry. In fact, there is currently an example of a small pharmacy in ACT with a staff count of 20 which currently has three (15%) women on un-paid maternity leave. This example shows that the 1.1% estimate may be inaccurate for our industry. (sub. DR325, p. 2)

Hair and Beauty Australia similarly commented at the draft report hearings:

In our industry it's a very, very high probability. Looking at the career of a person, they come in as an apprentice, they do their four years, they may work for a few years and then they go off and have a baby. It's inevitable probably for close to about 95 per cent of employees. So despite the fact that the commission report recognises that it's a low probability, generally in our industry it's a very, very high probability. (DR trans., p. 500)

And in a child care context, Tadpoles Early Learning Centres (sub. DR334, p. 1) pointed to just over 10 per cent of its 261 employees (around 85 per cent of whom are aged between 20 and 40 years) being pregnant during 2008.

In line with the specific examples presented by these participants, the Commission again acknowledges that individual firms will, from time to time, face greater risks than the industry-wide averages shown in table 7.1. But equally, those risks (and the associated disruption costs) already exist under existing parental leave provisions.

For small businesses generally, the Commission estimates that just four per cent of firms with less than 20 employees will experience a parental leave event in any given year.

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### *Employer provision of superannuation*

The draft report noted that the Commission's recommendation that superannuation entitlements continue during parental leave absences would add to business costs (at least until they can be passed on to employees in the form of slower wage growth). However, the magnitude of the costs is likely to be modest, even for small firms, given the design features of the broader proposal. Superannuation contributions during parental leave would relate to the employee's wage or the federal minimum wage, whichever was the *smaller* (though employers could voluntarily pay more), would only be available to a subset of current beneficiaries as they will need to meet two sets of employment eligibility criteria, and would be a tax deductible business expense (chapters 2 and 8).

The Commission estimated the *maximum* cost to an affected business in a single year of a woman taking statutory paid parental leave would be around 3 per cent of her pre-existing employee compensation (see chapter 2). The *expected* cost to businesses in any given year would be much lower than this and would depend again on the probability of a parental leave event actually occurring.

Drawing specifically on the above example (see also box 7.1):

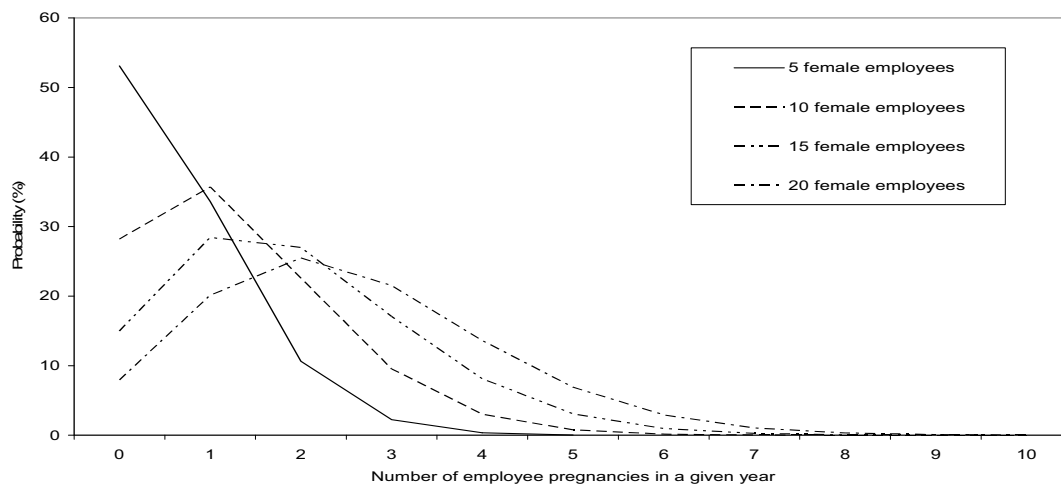
- at worst, the *expected* annual cost of superannuation contributions for a business employing just one female permanent part-time employee on the adult minimum wage would be less than half of one per cent of her annual wages (using the highest age specific fertility rate — that is,  $0.13 \times 3.1$  per cent)
- a small business employing five such women would face an *expected* annual cost of just under 2 per cent of the total wage bill ( $0.13 \times 5 \times 3.1$  per cent)
- the relevant share would be lower for women on higher wages because the maximum superannuation contribution payment would be 9 per cent of the federal minimum wage (though employers could voluntarily pay more) and also lower for female casuals, as they may not be meet the eligibility criteria proposed by the Commission .

Importantly, from a cash flow perspective smaller firms, in particular, may need to provision for the full 3 per cent of employee compensation to meet that liability when the parental leave event actually occurs.

**Box 7.1 Examples of the likelihood of employee births in small firms and the potential impact of the superannuation component of the proposed leave scheme.**

The figure below depicts the likelihood of employee births for four hypothetical small businesses. These businesses employ five, ten, fifteen and twenty women who are all between the ages of 30 and 34 years — the ages at which women are the most likely to have a child. As most small businesses would not have staff solely comprising women in these age groups, the estimated costs shown below of the superannuation component of the proposed paid parental leave scheme should be regarded as maximum potential impacts.

**Figure 1 : Likelihood of employee births by firm size — some hypothetical cases<sup>1</sup>**  
30 -34 year old females



On the basis of these likelihoods, the Commission estimates the expected cost of employer contributions to superannuation for these four hypothetical businesses would represent just 0.3 per cent of their total payroll each year (if all female employees were earning \$35 000 per year).<sup>2</sup>

A more realistic example of the actual employment and age structure of a small business might be a firm with five female and five male employees with two women aged under 25 years, two women aged between 30 and 34 years and one 45 year old woman. Using fertility rates associated with these age groups, the expected cost of employer contributions to superannuation would be even lower, at only 0.09 per cent of total payroll per year (if each employee earns \$35 000 per year).

Notes: 1) The likelihood of an employee birth in firm is estimated using age-specific birth rates for 5 year age groups. The probability of a birth occurring for a group of women in the same age group is assumed to be Poisson distributed.

2) The Commission also estimated the expected cost of superannuation contributions would be around 2.4 per cent of net profit before tax. This assumes total payroll represents 60 per cent of gross income (which is typical of service intensive industries such as child care but much higher than the figure for industries such as retail and hospitality services). Operating profit before tax assumed at 8 per cent of gross profit.

Source: Productivity Commission estimates based on ABS (2008e).

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In responding to the draft report, Catalyst Australia (a public policy network comprising unions, academics, individuals and other organisations) compared the magnitude of the financial burden on employers with the overall benefits to them from a largely taxpayer-funded scheme. It said the maximum cost to business of around three per cent:

... is very modest when balanced against the retention benefit to an employer and to the economy more generally. For this reason, we consider employers can meet the cost of paying superannuation and meeting existing [leave] accruals ... (sub. DR374, p. 3)

But many employer groups were not convinced that the costs associated with the superannuation proposal were modest and they opposed the superannuation component on those grounds. The South Australian Wine Industry Association, for example, said that even with the low risk of a parental leave event occurring, the higher cost base would result in discrimination against female employees:

Superannuation payments by employers in this instance are a direct increase to the cost of employment with no resultant productivity. While the incidence of parental leave may be low for some smaller organisations, it does not belie the fact that business costs will increase and this could act as a deterrent to employing a woman of child bearing age where that choice exists, or where 2 candidates, one male and one female, are equally considered for the vacant position. (sub. DR323, p. 2)

Others were concerned about the disproportionate impact on industries with a high concentration of female employment. In that context, Childcare Associations Australia (CAA) called for a pooled arrangement (an option not endorsed by the Commission in the draft report) to spread the cost across all firms:

CAA believes that the employer [superannuation] contributions should be a contribution from all employers and not be limited to those employers whose employees access maternity leave. Under the proposed arrangements the burden of employer contribution will be high in those industries that have a high dominance of female employees — this includes but is not limited to Early Childhood Education and Care (ECEC) service providers. It is also worth noting that many employers are subject to payroll tax and superannuation payments are included in this tax. CAA would prefer a “pooled employer” contribution as the benefits of female workforce participation are shared across the whole community — not just at the individual business level. (sub. DR407, pp. 1–2)

As touched on by CAA, some also suggested the Commission had underestimated the total costs faced by employers because the wage and/or superannuation payments made to employees during parental leave absences could be subject to (varying rates of) payroll tax and workers compensation premiums, depending on the jurisdiction and the gender of the employee. The Australian Mines and Metals Association said in that regard:

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While Victoria, New South Wales, Tasmania and South Australia’s legislation provides an exemption from payroll tax in respect to wages payable to employees on maternity or adoption leave, other jurisdictions (Northern Territory and Western Australia) do not. Moreover, the exemption provided in section 53 of the *Victorian Payroll Tax Act 2007* applies only to female employees taking maternity leave and male and female parents taking adoption leave and is limited to a maximum of four weeks pay, which would quite obviously be inconsistent with the Commission’s proposed scheme. Furthermore, Queensland’s *Pay-roll Tax Act 1971* subjects superannuation payments to payroll tax treatment, which would result in further additional costs to employers which could be avoided if the Government were to make these payments directly to all eligible employees. (sub. DR348, p. 10)

Clubs NSW referred specifically to the likely treatment of the superannuation component of the proposed scheme for payroll tax liability in New South Wales and the uncertainty surrounding whether the parental leave payment would be classified as wages:

... it would seem that employers would be liable for payroll tax under Section 17 of the *Payroll Tax Act 2007 (NSW)* (“PTA”) to pay payroll tax on superannuation contributions. However, an additional complication is the lack of clarity of whether parental leave payments are considered wages or not, especially in the case when the employer makes the payment directly. Section 10 of the PTA defines taxable wages as wages payable for services performed by the employee, thereby suggesting government funded parental leave payments may not be wages. However sections 13, 14 and 46 leave open an interpretation that government funded parental leave payments might be wages.

We note that s53 of the PTA states that 14 weeks paid parental leave is not ‘wages’ but anything beyond this amount is, and hence attracts payroll tax obligations for non-excluded employers. Accordingly, we would assume that the first 14 weeks of paid leave will be exempt from payroll tax but not the remaining 4.

Overall, it is not clear whether or not the proposed government funded paid parental leave would attract (the state based) payroll tax. If it is deemed to then we would seek this is met by the Federal Government, as the funder of the scheme, and not employers. (sub. DR328, pp. 7–8)

The NSW Business Chamber and Australian Business Industrial were also concerned more generally about whether workers’ compensation and payroll might apply to taxpayer-funded parental leave payments and the potential for increased business uncertainty:

The Draft Report has no discussion about how the system will interact with the workers’ compensation and payroll tax systems. This has the potential to increase the cost of the scheme for employers. As a further complication, the definition of ‘wages’ for the purposes of workers’ compensation and payroll tax varies across jurisdictions, although recently there has been some progress towards interstate harmonisation, particularly between New South Wales, Victoria and Tasmania. Using NSW as an example, it is clear that the interaction between these obligations and the current paid

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parental leave proposal is unclear, complicated and overly dependent on the particular circumstances of the employee. (sub. DR340, p. 11)

In response, the Commission reiterates that from an employer's perspective, an employee covered by the proposed paid parental leave scheme would not be on paid leave, but rather would be using the unpaid leave provisions of the National Employment Standards. Therefore, the Commission does not consider that parental leave payments funded by taxpayers would be treated as wages for the purposes of determining payroll tax or workers compensation premium liabilities. That said, any residual legislative uncertainty regarding the treatment of the taxpayer-funded component of the scheme should be addressed through appropriate amendments to payroll tax and workers compensation statutes in each jurisdiction before the scheme is introduced.

But as noted by the participants above, any employer-funded superannuation payments would be subject to payroll tax (for those firms not exempt on the basis of their payroll size) in some jurisdictions. Using Queensland as an example, this would increase the maximum gross cost to larger employers (those with an annual wage bill in excess of \$1 million) by around \$41 per employee on parental leave (4.75% of \$881).

Although the aggregate employer impost from the superannuation component of the scheme would still be considered modest in light of the retention benefits accruing to employers, the Commission is mindful of the business compliance burden (particularly for small firms) associated with the scheme's establishment phase and at a time of considerable economic uncertainty.

Therefore, while the Commission continues to see a prima facie case for employer funding of superannuation on statutory paid parental leave, it is proposing delayed implementation. The Commission recommends that the Australian Government should implement this component of the scheme following a review of the statutory paid parental leave scheme three years after its inception, but subject to consideration of its operation and impact at that time (recommendation 2.14 in chapter 2). That review could also canvass issues such as whether a cash 'opt-out' on this element of superannuation would be warranted to meet the immediate financial needs of lower income families in particular (see chapter 8).

#### *Compliance costs, cash flow consequences and increased uncertainty*

The Commission noted in the draft report that the operation of the proposed scheme would also impose compliance and other obligations on firms in order for:

- an employee's eligibility to be verified

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- parental leave payments to be made via the employer (see chapter 8)
  - the operation of the scheme to be monitored, reviewed and fine-tuned if necessary.

Employer obligations would include completion and lodgement of a parental leave pro forma detailing items such as employment duration and status, hours worked, expected leave start date and so on for each leave event. Self-employed parents, on the other hand, would need to complete and submit statutory declarations on their eligibility status and possibly provide supporting financial documentation (perhaps via a registered tax agent).

Dedicated record keeping requirements to enable program performance monitoring and government auditing (to minimise the risk of fraud) would also impose a burden on employers and the self-employed compared to current parental leave arrangements. In addition, payroll and leave systems (manual or automated) would be likely to require modification to facilitate the separate identification and distribution of the parental leave payment and, where relevant, to differentiate existing superannuation entitlements from the capped arrangements under the Commission's proposal (see chapter 2).

The Commission also noted that employers would face cash flow consequences from the Commission's preferred approach to payment delivery because there would be a delay between a business actually making the payment to its employees and then being reimbursed through reduced PAYG withholding remittances to the ATO. However, the Commission estimated the cash flow impact would be modest.

But small business representatives in particular (where parental leave absences are more likely to require temporary replacements) took exception to the Commission's view regarding cash flow consequences. Clubs NSW, for example, said that its:

... members' concern with this proposal is that this would create a cash-flow burden, especially on smaller clubs. Such clubs would already be paying the wages of the replacement employee, often subsuming the reduction in productivity until the employee gets up to speed, and may not have the sufficient cash-flow to also pay the employee on parental leave and wait to be reimbursed. (sub. DR328, p. 5)

Similarly, Master Grocers Australia commented that:

It has to be borne in mind that any employee on parental leave has to be replaced by another employee and the wages normally paid to the absent employee are provided to the replacement. Even if there was a short delay before the reimbursement is made by the Federal Government the process would place an administrative and financial burden on the employer. There is not only the additional "red tape" involved in making and claiming the reimbursement, but there is also the problem of cash flow for any small business. (sub. DR324, p. 4)

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The Pharmacy Guild of Australia referred to the unique circumstances of its constituency that would exacerbate the cash flow impact of the Commission's proposed paymaster function:

About 70% of an average pharmacy's revenue is derived from the dispensing of drugs listed on the Pharmaceutical Benefits Scheme (PBS). Of this, only 20% is received at the time of dispensing the drug. The remaining 80% is paid by the Federal Government. This government reimbursement component is claimed through Medicare Australia and takes between 9 and 16 days to reach the pharmacy after the date of dispensing.

This, combined with GST being paid on stock purchased but not being charged on sales, results in pharmacies being in a significantly more difficult cash flow situation than most small businesses. ...

Therefore, unlike other small businesses, pharmacies are always in a negative cash-flow situation and this in turn creates a need to lodge monthly Business Activity Statements in order to retrieve the money paid out as soon as possible. (sub. DR325, pp. 2–3)

Hair and Beauty Australia even raised the prospect that very small employers may not have a sufficient PAYG liability to offset the initial parental leave payment:

The other issue is that given they're microbusinesses often, that's with less than five employees, if you have an employee going off on [maternity leave] and you pay your PAYG on a monthly basis, it could well be that PAYG instalments of your few other staff is not sufficient to cover the wages being paid to the employee on maternity leave. The complexity, I would imagine, in trying to recoup the difference or the cash flow issues with having to wait until such time as you have amassed enough credit in your PAYG instalments is just untenable for some of these businesses. They don't work on that level of margin that they can afford to have an extra \$2000 out of their business on a monthly basis. (DR trans., p. 499)

The Commission acknowledges these concerns, particularly given that current difficulties in accessing business credit to address short-term cash flow shortages might exacerbate such risks. Furthermore, information provided by the ATO and FaHCSIA suggests that providing credits through PAYG withholding payments would be very costly to implement compared with alternative public sector delivery systems (such as those used by Centrelink) and would also not adequately manage compliance risks (see chapter 8).

Accordingly, the Commission proposes an alternative delivery mechanism through fortnightly *prepayment* to employers of statutory parental leave entitlements by Centrelink, typically commencing around the time of the birth of the child (and triggered by the same processes that lead to payments to parents of the baby bonus). The employer would then pay eligible parents as part of their normal pay cycle. While such an approach continues to involve administrative costs for government, it

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would overcome the cash flow consequences of the Commission’s draft proposal and would allow more appropriate risk management by the Australian Government.

The draft report also acknowledged that the Commission’s proposal might sometimes increase business uncertainty about whether an employee would return to work. This uncertainty would arise because sometimes an employee who otherwise would have formally resigned prior to the birth of their children would delay such notification in order to qualify for the higher parental leave payment as opposed to the baby bonus.

While the Commission recognises the additional compliance burdens and costs for business, it again notes the employers would only experience any impacts if an eligible mother were to give birth. In addition, the Commission has also proposed a range of measures to reduce the uncertainty, disruption, compliance and other costs associated with its paid leave scheme (see chapter 2). Those measures include:

- closely aligning the design of the proposed scheme with the forthcoming National Employment Standards
- advance payment of statutory parental leave instalments to employers acting as paymasters to avoid any cash flow impacts on those firms
- providing evidence-based guidance to employers on how to minimise disruption costs
- increasing the proposed notice period required under the National Employment Standards for employees extending leave beyond the originally indicated date from four to six weeks
- introducing a ‘keeping in touch’ provision similar to that in the statutory United Kingdom parental leave scheme and a range of voluntary Australian paid schemes (see, for example, BP Australia, sub. 210 and Diversity Council of Australia sub. 239).

### **7.3 Business benefits**

Many firms currently provide paid maternity leave on a voluntary basis. These firms are typically, but not exclusively, larger employers of professional and other highly skilled workers operating in primary labour markets. Key motivations for the introduction of paid leave arrangements have been to:

- provide a signal that the employer is ‘family-friendly’ and values female staff (and hence is an employer of choice)
- increase employee loyalty and promote higher retention rates (thereby avoiding re-hiring costs and fully exploiting investments in training).

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A number of submissions from employer groups pointed to these and other specific benefits from voluntary paid parental leave, including that from the Diversity Council of Australia (an employer advisory and strategy organisation), which said:

Leading employers have long recognised the benefits of paid maternity leave to productivity and business which include:

- Attracting and retaining talented employees;
- Protecting the significant investment in training and developing employees;
- Improving staff retention and reducing turnover; and
- Supporting family-friendly practices in workplaces as crucial to keeping skilled workers. (sub. 239, p. 4)

GM Holden focused on retention issues and the associated loss of firm-specific training investments as key determinants in the introduction and modification of its scheme:

... the inability to retain more than one third of these female employees [even with 6 weeks paid maternity leave] was a significant issue given the investment over time in their skill development and the loss of corporate knowledge. (sub. 222, p. 5)

Empirical evidence does indeed point to retention benefits from paid leave schemes. Studies in the United Kingdom, for example, have found maternity leave entitlements induced more women to return to their previous employer within seven months than would otherwise have been the case (see chapter 5). Interestingly, the greatest impact was for less educated lower skilled women, highlighting the importance of financial constraints for low-income families. These findings also imply that the introduction of statutory paid parental leave in Australia would disproportionately affect the labour force participation rates of women on lower incomes (see below).

Increasing recognition of retention benefits have led to a proliferation of voluntary schemes over the past five years, which has extended coverage of paid parental leave to over 50 per cent of women and men (see chapter 3). But while that trend could be expected to continue in the absence of a statutory leave scheme, it is unlikely to lead to (anywhere near) universal provision because attraction and retention are less important issues for firms that mainly employ lower skilled workers who are less costly to train and replace.

In arguing against employer funding of paid parental leave, the Australian Federation of Employers and Industries specifically cautioned against assuming the benefits from voluntary schemes were relevant to all firms:

Why hasn't paid maternity leave, or more recently parental leave, with all its purported benefits been more widely adopted? ...

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Where benefits are derived, for example, where staff retention is an issue, in attracting skilled staff, or for corporate marketing purposes, employers will offer whatever benefits they see as relevant for their circumstances and which may be sustainable. However, where there are no offsetting gains, parental leave is an additional on cost incurred as for other payments for time not at work arising from various forms of leave — annual, long service, study, public holidays, personal and carers etc. (sub. 202, p. 14)

That view regarding the differential nature of retention benefits among firms from paid parental leave, and the implications for funding a statutory scheme were shared by other employer interests including the Australian Chamber of Commerce and Industry (sub. 135), Australian Industry Group (sub. 182) and the Chamber of Commerce and Industry Western Australia (sub. 147). However, while the value of employee retention may be outweighed by the cost of paid leave for those firms that do not currently provide paid leave, a paid leave scheme would still be of some benefit to them (and that benefit should be realised under a largely taxpayer-funded scheme). The importance of retention to all firms is also likely to vary in line with the business cycle and labour market conditions, with Australia's experience of widespread labour shortages in recent years a case in point.

More broadly, there would be other benefits (beyond retention) accruing to all businesses from a statutory scheme if it were to:

- reduce wage pressures (in general and for lower skilled women in particular) as a result of increased workforce participation of women
- raise productivity as a result of improved maternal well-being and morale from more preferred work/life choices.

However, there is also a risk that a statutory scheme (regardless of how it is funded) would devalue the signal that voluntary leave arrangements send to existing and prospective workers about firms being an employer of choice. As a result, firms on the cusp of introducing their own paid leave schemes could be dissuaded from doing so. While this could affect the ability to retain and attract staff, the actual outcome would depend on how firms currently offering paid parental leave respond to the introduction of a statutory paid leave scheme.

## **7.4 Effects on existing voluntary schemes**

The impact of a statutory scheme on the behaviour of firms currently (or prospectively) offering paid parental leave will depend, in part, on the relative generosity (duration, payment level and eligibility conditions) of existing arrangements compared to the taxpayer-funded alternative (see box 7.2).

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The more generous the statutory scheme, the greater the potential that a firm will withdraw or reduce the generosity of its own arrangement. The Commission noted in the draft report that should the government introduce a statutory scheme, a firm currently (or prospectively) offering paid leave could respond in several different ways, including by:

- abandoning its scheme (or plans for one), with employees then relying solely on benefits provided by the statutory arrangement (in other words the statutory scheme crowds-out existing and future voluntary schemes)
- continuing existing parental leave benefits in parallel with statutory entitlements
- topping-up payments from the statutory scheme to full replacement wages for the duration of the statutory arrangement
- providing alternative/additional employment benefits in order to differentiate itself from other firms and signal it is an employer of choice.

Participants' views on the likely outcome were mixed. Some considered the risk of crowding-out was high. For example, the Centre for Independent Studies noted:

It must be assumed that if a taxpayer-funded scheme is introduced, some employers who currently offer paid maternity leave will stop providing it, transferring a cost that is now borne by business to the taxpayer. (sub. 89, p. 9)

The Brotherhood of St Laurence shared that view and commented on the efficiency implications:

A relatively straightforward option to administer is for the government to fund a paid parental leave scheme out of general revenue. A universal system would be expensive, however, and could lead to higher taxes which might not be politically desirable. As many employers already provide paid leave, this kind of system would crowd out this funding and thus not be a very efficient way of spending taxpayer dollars. (sub. 92, p. 3)

Others, including the ACTU (sub. DR365, p. 11), referred to a recent media report stating that six of nine firms surveyed had '... refused to commit to keeping their schemes once the Government introduced its own.' (Rehn 2008). The ACTU (and a number of other participants) then called for the application of a 'no disadvantage' test to ensure no employee was worse off as a result of the introduction of the statutory scheme (see below).

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## Box 7.2 Features of selected voluntary paid parental leave schemes

### *AMP Limited*

- full pay for the first 14 weeks of leave or half pay for the first 28 weeks
- leave can be taken as a single block or over multiple time periods
- available to male and female employees and for adoption

### *ANZ Banking Group*

- a lump sum of 12 weeks full pay at the beginning of parental leave, or full pay for the first 12 weeks of leave or half pay for the first 24 weeks of leave
- no minimum service period to qualify

### *Australian Securities Exchange*

- 6 weeks of leave at full pay with an additional week of paid leave for every year of service up to an additional 6 weeks

### *GM Holden*

- 14 weeks leave at full pay or 28 weeks half pay for employees with two years service (6 weeks full pay or 12 weeks half pay if service period greater than one year and for casuals with more than one year's service)
- can be taken as a lump sum at beginning of leave period
- available to male and female employees (as primary carers)

### *Goldman Sachs JBWere*

- 16 weeks leave at full pay with the option to take half pay for 32 weeks

### *Lend Lease*

- 14 weeks at full pay to all employees (male and female) after 12 months of service

### *McDonalds Australia Limited*

- 8 weeks leave at full pay after 12 months continuous service (or part-time equivalent), 4 weeks paid on commencement and 4 weeks on return

### *Myer*

- 6 weeks leave at full pay for permanent staff with at least 18 months service

### *National Australia Bank*

- lump sum of 12 weeks full pay at the beginning of parental leave, or normal pay for the first 12 weeks of leave, or half pay for the first 24 weeks

### *Rio Tinto*

- 12 weeks leave with 8 weeks paid at commencement (by normal pay cycle, lump sum or half pay for 4 months) and 4 weeks on return (no minimum return period)

### *Slade Group*

- \$100 per week for up to 52 weeks for female employees with at least two years service history (\$150 per week for those with at least four years service history)

### *Woolworths*

- 8 weeks at full pay with 6 weeks paid at commencement and two weeks on return, for staff employed continuously for two years on full or permanent part-time basis

Sources: Gough 2008, Nader 2008, sub. 222, sub. 239, sub. 251.

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But employer groups took a different position. Commerce Queensland, for example, highlighted the importance of being an employer of choice as a key reason why firms would maintain existing arrangements:

HREOC believes that it would be unlikely that employers who currently provide paid parental leave would seek to remove this entitlement if the Government introduced a national paid parental leave scheme that provided a minimum entitlement for women in paid work. Commerce Queensland shares this opinion. Those employers that currently provide paid parental leave do so on the basis of the business case in their workplace and in order to be an employer of choice. Providing a payment above the government minimum entitlement will continue to benefit these businesses. (sub. 172, p. 15)

The Catholic Commission for Employment Relations added that employer of choice motivations were an accepted theme in human resource literature.

Attraction, recruitment and retention are crucial issues facing Australian employers. Becoming and remaining an ‘employer of choice’ is a constant theme in human resource management literature. Retaining existing private paid parental leave schemes is one mechanism to distinguish one employer from another. (sub, DR337, p. 8)

The Chamber of Commerce and Industry (CCI) Western Australia went further in pointing to the statutory obstacles that would prevent crowding-out:

CCI submits that an employer already offering a voluntary scheme would not be able to either abandon, continue in “parallel” or “top-up” an existing scheme in response to the introduction of a statutory scheme without altering the contract of employment (any such alteration requiring agreement with both parties). If an employer has provided for paid parental leave in their employment contract, they will be required to continue with this payment to all existing eligible staff, who would receive their employer entitlements on top of their statutory entitlements. (sub. DR316, p. 5)

The Commission acknowledges the protections provided to existing employment conditions by industrial relations legislation<sup>3</sup> including through a ‘no disadvantage’ test applied to collective agreements and designated awards by the federal Workplace Authority.<sup>4</sup> But it also notes the information provided in the submission by the Finance Sector Union (sub. DR306, pp. 17–21), which highlights the divergence between parental leave benefits contained in some industrial agreements (the basis of the employment contract) and the more generous benefits actually provided by employers (at least in the finance sector). In that context, some employers could reduce the duration of their voluntary schemes without being in breach of the employment contract.

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<sup>3</sup> Under the Workplace Relations Amendment (Transition to Forward with Fairness) Act 2008.

<sup>4</sup> The no disadvantage test to be introduced on 1 July 2009 under the Fair Work Bill 2008 will only apply to the minimum employment conditions contained in the NES.

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Other employers put on record their intention to maintain their existing schemes or introduce hybrid arrangements. For example, the Tasmanian Government said it:

... expects to continue the existing parental leave benefits for State Service employees in conjunction with the proposed new statutory entitlements, but notes the Productivity Commission's findings that full replacement wages during the additional proposed 18 weeks statutory leave for highly paid women would be very costly and, given the already high level of attachment to the workforce, would have few incremental labour supply benefits. (sub. DR411, p. 8)

And GM Holden reported that its employees would be no worse off following the introduction of a statutory scheme:

Although only at the exploratory stage, GM Holden would be interested in combining any new statutory arrangements with those we have already in place for our employees.

GM Holden would therefore want to have the ability to combine the two schemes into a hybrid arrangement as long as our employees would not be disadvantaged. For example, in relation to the leave for the mother or primary carer, GM Holden would be interested in re-organising the funding provided by the statutory 18 weeks paid leave at minimum wages and combining it with our current provisions to form some kind of hybrid arrangement. (sub. DR388, p. 6)

Finally, the Business Council of Australia (which represents Australia's top 100 companies) stated that the introduction of a statutory scheme:

... will allow investments to be made by them in some other supports that facilitate the work/family operation. Access to reasonably priced and quality child care, flexible working arrangements and breast feeding facilities are three of those most highly valued. (sub. DR288, pp. 1–2)

On balance, the Commission continues to consider that, given the specific proposed design of the scheme, it is unlikely that there would be a wholesale withdrawal of existing paid parental leave schemes. This is because of the higher (full-wage) payment rate under voluntary schemes for most employees (see below), the negative signal regarding the firm being an employer of choice that outright withdrawal would send to a firm's workforce and, to a lesser extent, the industrial relations attention that such a response would inevitably invite.

Even were crowding out to occur sometimes, there are potentially considerable difficulties in applying a no-disadvantage test. These include that:

- a proper test would need to take account of the fact that employers can re-configure the package of benefits. A test would then need to consider how all elements of the package of employee benefits might have changed after the introduction of a statutory scheme. In practice that would often be difficult and time-consuming

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- any response by an employer might take some time, and it would be hard to determine the appropriate counterfactual against which to measure disadvantage. For example, say that one month after the government introduced a statutory scheme, the employer reduced their leave provisions, but paid a wage increase of two per cent. It could be that the two per cent represents reconfiguration of the package of benefits or it could be an increase that was going to happen anyway.
  - sometimes particular employees might be disadvantaged, even if many employees were advantaged by a change in a private scheme. For instance, suppose an employer initially offers 8 weeks of full replacement paid parental leave. After introduction of a statutory scheme, it then offers to substitute its existing scheme with one that top ups the statutory scheme to full replacement wages for the full 18 weeks. So an employee getting \$1200 a week for 8 weeks would now get a total of \$21 600 instead of \$9600, with the employer contribution rising by \$2212. However, an employee getting \$700 week would have a reduced net employer contribution of \$2800. This raises the question of whether a no disadvantage test would need to apply at the individual or enterprise level, with the former more difficult than the latter.

Nonetheless, the Commission cannot say with certainty how businesses generally will respond to the introduction of its proposed scheme. Anecdotal evidence from the operation of the taxpayer-funded leave scheme in New Zealand indeed suggests that firms continued to offer their voluntary arrangements (in addition to the statutory provisions) after the statutory scheme was introduced. Against that background, the Commission would expect that many Australian businesses would restructure their existing leave schemes to top-up government funded leave to full replacement wages and then use the balance (if any) to extend the period of leave at full pay.

However, the Commission also presented examples in the draft report of firm-specific employment circumstances that may be affected by its proposal. For instance, a minimum wage payment could be considerably more generous for part-time employees than the parental leave benefits currently offered by their employers (especially if voluntary payments are taken at half pay). On that basis, firms with a high concentration of part-time staff may be influenced, other things being equal, to withdraw a voluntary scheme (or restrict eligibility to full-time staff alone).<sup>5</sup> Conversely, if voluntarily provided benefits are comparatively low, the provision of an additional statutory payment may increase retention levels for these firms.

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<sup>5</sup> Equally, the eligibility conditions in the Commission's proposal are much broader than some voluntary schemes in that they do not exclude casuals or non-permanent part-time employees and require only 10 of the previous 13 months in continuous employment (rather than 18 month or 2 year eligibility periods with the same employer for some schemes). Those features may also influence decisions on the nature of existing voluntary arrangements.

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Overall, it would be prudent to, at the very least, monitor the reaction of firms that presently offer voluntary paid leave schemes. Should a pattern of behaviour emerge indicating that firms were systematically abandoning voluntary schemes, some form of policy response may be appropriate. Given that large scale withdrawal would undermine the objective of increasing the time parents can spend with their newborn children, re-consideration of who finances the statutory scheme (either in whole or part) would be one policy option worth investigating. An assessment of the statutory scheme's impact on voluntary arrangements and the most appropriate response should be an element of the review of the scheme to be undertaken three years after its introduction (chapter 2).

Finally, the use of voluntary paid parental leave schemes as signals that firms are employers of choice means the availability of a statutory scheme may (depending on the relative generosity) serve to lessen the strength of that signalling. This may motivate firms that may have considered a voluntary scheme in the future to offer an alternative benefit to specific employees they wish to attract or retain (such as other family friendly policies like in-house childcare facilities). To the extent that such substitution reflects a set of working conditions that are more highly valued by employees (including because of changing societal norms), crowding out could be viewed as a positive outcome.

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### Box 7.3 Summary of business impacts

The impacts on business from the Commission's paid parental leave proposal would be constrained by:

- government initially funding all of the scheme's cost, with the possible future implementation of superannuation contributions by business
- deferring the implementation of the superannuation component until completion of a review of the scheme three years after its inception, and subject to consideration of its legal and other administration issues for government, and its effects on the viability and compliance costs of the business sector at that time
- limiting the *mandated* super contribution rate to the statutory rate (currently 9 per cent), even if the business usually paid more than this (but with scope for parties to privately negotiate higher amounts)
- restricting these contributions to employees who
  - passed the eligibility requirements for statutory paid parental leave (in particular, the 330 hour, continuous employment test) and
  - received super entitlements before going on paid parental leave and
  - were eligible for unpaid parental leave under the National Employment Standards (NES)

The maximum financial cost (including superannuation) in respect of any employee would be 3.1 per cent of usual annual salary cost (reducing for those on higher incomes). A significant number of small businesses would not face any costs from parental leave in any given year.

The employer would act as the paymaster for government. Using their usual pay cycle, they would pay an employee on paid parental leave the federal minimum wage, but only where the employee was entitled to unpaid parental leave under the NES.

Where an employee worked with multiple employers, the employer allocated the tax free-threshold for PAYG withholding purposes would act as paymaster.

The government would fully reimburse the employer in advance for any paid parental leave payments to be made to eligible employees.

The business would only face additional compliance costs when an employee was on paid parental leave — with no change otherwise.

Compliance costs would be minimised by using existing administrative systems, advance payment of statutory parental leave instalments and better leave notice arrangements than under the current NES.

Business would benefit from a scheme through higher employee retention rates.