



TRANSCRIPT OF PROCEEDINGS
Fair Work Act 2009
TRANSCRIPT IN CONFIDENCE

1052533

**JUSTICE ROSS, PRESIDENT
VICE PRESIDENT CATANZARITI
DEPUTY PRESIDENT ASBURY
COMMISSIONER HAMPTON
COMMISSIONER LEE**

AM2014/305

s.156 - 4 yearly review of modern awards

**Four yearly review of modern awards
(AM2014/305)**

Melbourne

9.04 AM, THURSDAY, 1 OCTOBER 2015

PN10431

JUSTICE ROSS: Any change to the appearances in Melbourne or Sydney? No? I gather there's an issue, Mr Dowling, that means you're not quite ready to deal with Professor Lewis, is that right?

PN10432

MR DOWLING: Yes. My apologies, your Honour. Some documents are on their way.

PN10433

JUSTICE ROSS: No, that's all right. We might deal with the objections to the Quiggin evidence which we were going to deal with at the outset in any event, because it seems to us if we uphold some of those objections then we have to remove part of Professor Lewis' material as well. Now Ai Group has made a submission. They've indicated that they're content for us to determine the matters on the papers subject to affording you a right to respond to their written submission. Can I ask the representatives of Ai Group whether there's anything you wish to add to your written submission?

PN10434

MR GOTTING: At this stage, your Honour, no. At this stage we haven't seen any material from United Voice, whether by way of submission or letter or any form of correspondence. So our only concern would be to ensure that we would have an opportunity to see anything that they put on and respond to it.

PN10435

JUSTICE ROSS: They'll be putting on what they say now and you can respond to that, so. We can't deal with it on the papers. We can't give them an opportunity to file something and then you to reply because Professor Quiggin is on today.

PN10436

MR GOTTING: I wasn't seeking to suggest otherwise, your Honour.

PN10437

JUSTICE ROSS: Okay.

PN10438

MR GOTTING: I just understood that the process was that each party was to file some documents in advance of today, and as far as I am aware we have not received anything from United Voice.

PN10439

JUSTICE ROSS: I can't recall what the process was. Were directions issued or any agreement between you?

PN10440

MR DOWLING: Not to our understanding, your Honour, no.

PN10441

JUSTICE ROSS: All right.

PN10442

Mr Gotting what are you referring to then?

PN10443

MR GOTTING: On Friday there was a discussion at the mention at about midday that there would be an exchange of submissions between us. The timetabling was to be agreed between the parties. We filed a document on 28 September and I think it was uploaded on 29 September and we expected that there would be a response from United Voice in accordance with the indication that was given at the mention.

PN10444

JUSTICE ROSS: The indication would have been in the course of any discussions between yourselves and United Voice because I don't think I dealt with any timeframe for filing material. I was going to leave that to the parties. Are you content for us to hear from United Voice now?

PN10445

MR GOTTING: Yes.

PN10446

JUSTICE ROSS: And for you to say whatever you want to say in response?

PN10447

MR GOTTING: Yes.

PN10448

JUSTICE ROSS: All right.

PN10449

MR DOWLING: Thank you, your Honour. Your Honour, the document provided by those acting for the Australian Industry Group has an attachment at the very last page which you will see sets out a table that includes each of the seven objections.

PN10450

JUSTICE ROSS: Yes.

PN10451

MR DOWLING: It includes the response made by United Voice in the last of the columns.

PN10452

JUSTICE ROSS: Yes.

PN10453

MR DOWLING: That's a convenient reference point, your Honour. Can I firstly say in terms of a more general response before I come to the specific ones, your Honour will see that each of the objections is made on the same basis both in relation to there being no basis for the opinion and all in relation to the opinion not being based on expertise. Can we say as a global response firstly that there doesn't appear to be any dispute more broadly that Professor Quiggin is properly

qualified as an expert economist. No objection is taken to his evidence otherwise, in that respect at least.

PN10454

He is as a result of that, we say, properly qualified to give his opinion about established economic concepts, and some of the objections I will come to deal with those, and we say also that in respect of each of the disputed parts his opinion is clear. Lastly, by way of general response it is said by us that much of the objections - and I'll deal with them more particularly, but much of the objections are either responding to something that Professor Lewis has said or Professor Lewis himself then responds to the objections.

PN10455

Now the submission made by AiG is that that doesn't make something that might be inadmissible admissible and we accept that submission. But we say this, it does at least do two things. It does at least confirm that the subject matter, at least in the view of both experts, is within their relevant expertise and it does highlight that in respect of the responding expert there is no complaint made about a lack of or a shortcoming in reasoning.

PN10456

In the case of Professor Lewis where he responds to Professor Quiggin there's no complaint made by him that there's a difficulty in understanding the reasoning, or that the reasoning is not somehow clear. That we say is indicative of it being within the field of expertise and it properly being able to be understood in its proper context. Can we then go to the particular objections. The Bench will see that the first of them appears at page 7 and within paragraph 20. That paragraph has four subparagraphs and the objections are within the last two of those subparagraphs. Can I say this about paragraph 20 in respect of both of these objections; the Bench will see that the commencing words to paragraph 20 set out the opinion held by Professor Quiggin:

PN10457

The effects of penalty rates on aggregate employment in the hospitality industry are limited and outweighed by other factors affecting employment such as the general state of the economy. My reasons for this are -

PN10458

And he then sets out four reasons. Now it's important contextually, we say, the opinion is set out in the first paragraph and the reasons thereafter follow.

PN10459

JUSTICE ROSS: Yes, but the reasons also express opinions.

PN10460

MR DOWLING: Yes. But all we're saying, your Honour, is that what is expressed to follow is within the context of the broader opinion and are an explanation for that broader opinion. The first of those - - -

PN10461

JUSTICE ROSS: But that doesn't mean that opinions expressed in support of the broader opinion - if Ai Group's submission is accepted, in those opinions there should be the expression of a basis upon which they're made.

PN10462

MR DOWLING: That's right, your Honour. We don't say that automatically makes them admissible and therefore it's okay, but we do say there's a proper context.

PN10463

JUSTICE ROSS: Okay.

PN10464

MR DOWLING: The first of those is the last sentence of subparagraph (3) and it's the words beginning "It is therefore likely that". Now we say two things in response to that. Firstly what is clear from that is Professor Quiggin is stating that:

PN10465

Absent regulated penalty rates, equal bargaining would produce higher wages on weekends and public holidays.

PN10466

And that opinion is clearly expressed in support of the previous sentence. But can we say this additionally. The concept that workers will value weekend and public holidays or weekend and public holiday labour at higher rates than weekday labour is expressed by Professor Lewis himself. You will see that in the third a paragraph of page 39 of Professor Lewis' report. It's a concept that's dealt with by both of them. If the Bench is at page 39 - - -

PN10467

JUSTICE ROSS: And Professor Lewis doesn't provide the basis for his opinion either.

PN10468

MR DOWLING: No. No, but they both - - -

PN10469

JUSTICE ROSS: Express a similar sentiment.

PN10470

MR DOWLING: Yes. Now in respect of the next objection, that is subparagraph (4)(iv). There are two objections in this paragraph. The first is to the second sentence in that paragraph commencing:

PN10471

However any increase in consumer expenditure on such days would be likely to come at the expense of expenditure at other times.

PN10472

This we say is an application of the principle of demand shifting to make the simple point that consumer demand is finite and it is likely that consumers who

dine out on a Sunday, for example, will consequently not dine out on a Tuesday. Now we don't understand that to be a contentious proposition. There's some dispute between the experts as to the extent of that shifting, in our submission, but it is as we described earlier a broadly accepted application of an economic principle and comes within Professor Quiggin's expertise. The third sentence, we accept that the first half of the first sentence, that commencing:

PN10473

Moreover the fact that many establishments close on Mondays when there are no penalty rates suggest that pay rates are not a primary determinant of opening hours.

PN10474

Now the first part of that "The fact that many establishment close on Mondays" we accept Professor Quiggin hasn't set out his basis for saying that. In our submission perhaps the simplest way of dealing with that is for Professor Quiggin to be asked by those cross-examining him, "What is the basis for that statement?" He has either got a proper basis or he hasn't.

PN10475

JUSTICE ROSS: Either that or - and depending on what we do with the objections - we can hear from each of you about this - but either it can be dealt with in cross-examination or you can ask the question with leave in chief.

PN10476

MR DOWLING: Yes.

PN10477

JUSTICE ROSS: And then it can be the subject of cross-examination.

PN10478

MR DOWLING: Yes. That leads to objection - - -

PN10479

JUSTICE ROSS: That might be the fairer course for the cross-examiner, that's all.

PN10480

MR DOWLING: Yes. I understand, your Honour. I accept that. That leads to objection number 4 which appears at paragraph 24. I think it might be convenient if we deal with both objection 4 and 6 together because they deal with a relatively similar subject matter. Objection 4 appears at the last sentence of paragraph 24 and reads:

PN10481

This change will be offset by an increase in the employment of operator family labour on days other than Sundays and a reduction in the employment of hired labour on those days.

PN10482

Skipping over objection 5 which I'll return to, objection 6 then appears at the end of paragraph 27:

PN10483

If the operator and family members work more hours on Sunday as a result of penalty rates they will in all probability work less hours at other times, requiring the employment of more hired labour at those times.

PN10484

Again this is a basic economic concept or principle we say, the substitution of labour. That's something that's clearly within Professor Quiggin's expertise. The notion of the substitution of owner operator labour with hired labour is a significant part of Professor Lewis' report and report in reply, and this in large part if not completely is the criticism in response by Professor Quiggin. He makes clear from the paragraphs in between the two I've described the offsetting effects for the context of that substitution of labour, and the offsetting effect that he's describing, the increase in family labour on weekends to offset the predicted decrease of family labour on weekends, is all properly within the rubric of this discussion about the substitution of labour and properly within his expertise we say. Can I then go backwards in the document to objection 5 which appears at the top of page 9. That is the paragraph commencing:

PN10485

Similarly to the extent the reduction in penalty rates lead to the removal or production of Sunday surcharges -

PN10486

et cetera. Again this we say is a discussion about demand shifting and his conclusion:

PN10487

There is little reason to suppose that total expenditure on café and restaurant services would increase substantially as a result of the shift of demand towards Sundays.

PN10488

It is in some respects the inverse of what's discussed by Professor Lewis at page 28 of his report commencing at the bottom of 27 where he says:

PN10489

For instance firms may redirect production to those periods when overtime or penalty rates are not paid, in order to reduce labour costs. That's the same concept being discussed and no basis set out for that assertion. But in our submission it's properly within the area of expertise of both of them and something they can properly opine about. That leaves the last of the objections which is objection 7, which is in appendix A, and the objection commences on page 12, at the very bottom of page 12, and there Professor Quiggin commences:

PN10490

Since part-time employees are particularly likely to receive penalty rates, the expansion in employment for this group suggests that any adverse effects of penalty rates are less significant than they were in the past.

PN10491

Dealing with the sentence backwards, the expansion in employment for this group is dealt with in the previous paragraph and that's his change in the part-time workers from 1.63 per cent of employed persons in 1984 to 3.74 per cent of employed persons in February 2015. So he has dealt with, in our submission, and set out his basis for the assertion that there has been an expansion in the group. What he hasn't done, we accept, is to say why it is in the first part of that sentence he says:

PN10492

Since part-time employees are particularly likely to receive penalty rates...

PN10493

He doesn't explain why that is so. Again the most practical course, in our submission, is that he can either be asked in chief the basis for that part of the sentence and then it can be dealt with in cross-examination, or alternatively he can be asked in cross-examination. Unless there are any questions they are the submissions of United Voice in response to those objections.

PN10494

JUSTICE ROSS: Thanks Mr Dowling.

PN10495

Mr Gotting, anything in response?

PN10496

MR GOTTING: There are a couple of matters, your Honour.

PN10497

JUSTICE ROSS: Yes.

PN10498

MR GOTTING: The first is there's no dispute that Professor Quiggin is an expert economist. The nature of the objection though is that some of the opinions that he expresses in the report in the paragraphs and sentences we have identified are not based on his expertise and in our submission they are more akin to a personal view rather than based upon that expertise, and that is the foundation for the objections that we have made. The second matter that I wanted to indicate was that the fact that Professor Lewis has not made complaint about responding to some of the issues that Professor Quiggin has raised does not render those opinions of Professor Quiggin admissible.

PN10499

It's obvious that Professor Lewis is not a lawyer and nor is he an advocate and he is not in a position to deal, with respect, on the issue of whether some of the opinions that are set out in the Quiggin report are or contain a basis of opinion, as is required or as is good practice by reference to the principles that have been set

out in Dasreef. The third thing that I wanted to raise was to endorse something that fell from your Honour the President concerning the lack of a division between broad opinions and particular opinions, and the absence of such a division having any relevance to the question of admissibility.

PN10500

In terms of the objection to paragraph 20(3) nothing that my learned friend said really identified a basis for the opinion that parties would be bargaining on equal terms, and therefore we maintain an objection to that sentence in paragraph 20(3). In terms of paragraph 20(4) there was an attempt by my learned friend to justify that paragraph or that sentence by reference to demand shifting but, with respect, there is no basis for that opinion and no connection between the opinion that's there set out and the principle of demand shifting in that sentence, and therefore I maintain the objection. I accept though that one basis upon which the issue could be resolved would be strike out that sentence from paragraph 20(4) and allow United Voice, with leave, to address that question in chief.

PN10501

JUSTICE ROSS: If we come to it, Mr Gotting, if we come to that issue that we don't uphold the objection, what is your preference? That United Voice ask the questions in chief as to the basis of the various opinions to which you have voiced the objection, or would the matter simply be left to be dealt with in cross-examination or by questions from the Bench?

PN10502

MR GOTTING: My submission is that it would be appropriate for the Commission to grant leave to United Voice to deal with the matter in chief.

PN10503

JUSTICE ROSS: And if we were to reject the objections that would appear to be the fairest course, because then you can consider the answers given and whether you want to explore it further in cross-examination. All right. Thank you, I'm sorry - - -

PN10504

MR GOTTING: So can I just clarify that when your Honour indicated rejecting the objection, I assume you meant rejecting the material based upon the objection?

PN10505

JUSTICE ROSS: No, I wasn't intending to be quite that precise. Yes, either we - - -

PN10506

MR GOTTING: Or, I'm sorry, the basis of - - -

PN10507

JUSTICE ROSS: Either we dismiss the objection to those aspects of Professor Quiggin's evidence or we could uphold the objection and then the matter can be explored. I don't quite see why we would do that. If we remove it - if we uphold the objection, we uphold the objection and that part of his evidence would be

removed. I'm talking about rather the circumstance where we do not uphold the objection and the material remains.

PN10508

MR GOTTING: I'm sorry, I misunderstood the basis of the question. Can I just clarify the position. If the objection was rejected then the relevant sentences in the report would be admitted into evidence, and in that circumstance it would be a matter for Ai Group to decide whether it wanted to explore those sentences in cross-examination.

PN10509

JUSTICE ROSS: Well, it would also be a matter - - -

PN10510

MR GOTTING: And in those circumstances it would not be necessary for United Voice to address it in chief, and in those circumstances my submission is that it would be inappropriate for the Commission to grant United Voice leave to deal with the matter further in chief.

PN10511

JUSTICE ROSS: We might be asking the question as well, whether they deal with it in chief or not.

PN10512

MR GOTTING: I obviously cannot curtail in advance any questioning by the Bench. If that issue is explored by the Bench we would - - -

PN10513

JUSTICE ROSS: Well, I can put you on notice I'm intending to explore it with Professor Lewis as well where I'm not clear as to what the basis of it is. I'll ask the question, because Professor Lewis' report suffers from the same vice that you say Professor Quiggin's report suffers from. Professor Lewis also expresses opinions for which the factual basis is not clear.

PN10514

MR GOTTING: I obviously will not seek to argue in advance that the Commission is precluded from raising those issues or for that matter any issue that it wishes to raise with Professors Quiggin and Lewis.

PN10515

JUSTICE ROSS: Particularly as this is not an inter-parties matter, it's a review. So the witnesses - - -

PN10516

MR GOTTING: I'm not seeking to argue against - - -

PN10517

JUSTICE ROSS: Yes.

PN10518

MR GOTTING: I'm sorry.

PN10519

JUSTICE ROSS: I'm just putting - look, the issue is this, Mr Gotting. Given that I've advised you that if we don't uphold your objection then it's likely we will ask questions as to the basis of the various opinions to which you have voiced objection, in those circumstances do you think the better course is that United Voice explore those matters with the witness in examination-in-chief?

PN10520

MR GOTTING: In my submission if the objection is rejected the appropriate course is for the Commission if it wishes to explore the issue with Professors Quiggin and Lewis, and then to afford each of the parties an opportunity to cross-examine or further explore by examination-in-chief any issues that arise out of the questions that flow from the Bench and the answers given to those questions.

PN10521

JUSTICE ROSS: Yes, I don't think we'd be doing that. We wouldn't be allowing United Voice to further explore in examination-in-chief the matters we've raised. If we have any questions we would put them at the end of cross-examination. We would grant the cross-examiner leave to ask any questions that arise from our questions and then the examiner-in-chief - - -

PN10522

MR GOTTING: That protects - - -

PN10523

JUSTICE ROSS: - - - would put their re-examination.

PN10524

MR GOTTING: Your Honour, the course that you have just outlined is acceptable to the Ai Group.

PN10525

JUSTICE ROSS: All right. I'm sorry, Mr Gotting, I interrupted you as you were going through the points that Mr Dowling had raised.

PN10526

MR GOTTING: No, I was happy to deal with the question. I think I was dealing with paragraph 20(4) and the submission that I wanted to make was that there was no connection between the concept of demand shifting, which is the apparent basis of the opinion, and the text that appears in paragraph 20(4). The next issue that I wanted to raise in response was the matters that have been raised by Mr Dowling concerning paragraphs 24 and 27. I maintain the objection based on the absence of a basis for the opinion, notwithstanding the submissions that Mr Dowling put.

PN10527

The submissions that I made concerning paragraph 20(4) and in particular those relating to demand shifting would equally apply to the objection to paragraph 25 and may I just additionally highlight that paragraph 25 deals with the issue of a reduction in Sunday surcharges, and it's not clear that that topic is within the

expertise of Professor Quiggin, and additionally there seems to be no basis for that opinion in any event. Those are the matters that we wished to raise in response to Mr Dowling.

PN10528

JUSTICE ROSS: All right, thanks Mr Gotting.

PN10529

Is there anything further on this issue by any party?

PN10530

MR IZZO: Your Honour, just one comment. I note that depending on how the objections fall you stated that there might be an impact on the Lewis report.

PN10531

JUSTICE ROSS: I think there will be. Yes, not might be.

PN10532

MR IZZO: We'd just seek to be heard on that.

PN10533

JUSTICE ROSS: Of course you would be.

PN10534

MR IZZO: That's all.

PN10535

JUSTICE ROSS: And I was just pointing out that it seems not only there are some passages to which Mr Dowling took us to, but there are other passages where the same argument might be put. So I think it would require some examination of Professor Lewis' report and we wouldn't do that without hearing from each of you. All right?

PN10536

MR DOWLING: Sorry, your Honour, I should for completeness just say the approach that your Honour described involving the Commission or Bench asking questions of both witnesses and then if anything arises for the cross-examiner, that's acceptable to us.

PN10537

JUSTICE ROSS: All right. Thanks Mr Dowling. Look, we'll adjourn for 10 minutes just to consider what has been put and we'll come back with our ruling. Thank you.

SHORT ADJOURNMENT

[9.34 AM]

RESUMED

[9.46 AM]

PN10538

JUSTICE ROSS: United Voice have filed a report by Professor John Quiggin, the Quiggin report. On 15 September Ai Group filed an objection to parts of the Quiggin report. The objection relates to particular sentences in paragraphs 20(iii)

and (iv), paragraph 24 and 27 and paragraph 9 of appendix A. In addition the whole of paragraph 25 is objected to. In each instance the objection is substantially the same, namely that there is no basis for the opinion expressed and that the expressed opinion is not based on the witness' expertise. As to the second proposition, Professor Quiggin's specialised knowledge within the meaning of section 79 of the Evidence Act is in the area of economics.

PN10539

It is common ground that Professor Quiggin is an expert economist. Having regard to Professor Quiggin's qualifications and experience, including the extent and scope of his published work, we are satisfied that he has the requisite specialised knowledge to express the opinions which are the subject of the objections. The second objection to the evidence is that no basis for the opinion is expressed. The argument put is that what has been called the basis rule operates to exclude the evidence which is the subject of the objection.

PN10540

The so-called basis rule is said to be a rule of evidence by which opinion evidence is to be excluded unless the factual basis upon which the opinion is based is established by other evidence. In support of the existence of such a rule, Ai Group rely on the judgment of his Honour Heydon J in *Dasreef*. It seems to us that the objection put really goes to the weight to be attached to the evidence rather than its admissibility. We have decided to dismiss the objection. We make three points in this regard.

PN10541

1. We are not persuaded that the basis rule form part of the common law of evidence. In this regard we note that the evidence of his Honour Heydon J in *Dasreef* are obiter and were not adopted by the plurality in that case. In this regard we refer to the reference to the case [2011] 243 CLR 588 at paragraph 41 of the plurality.

PN10542

2. Even if the basis rule was part of the common law it has been displaced by the relevant provisions of the Evidence Act. In support of that proposition we rely on *McNeill v The Queen* [2008] FCAFC 80.

PN10543

3 Our third point is that if we are wrong about the operation of the so-called basis rule we would nevertheless admit the evidence. Section 591 of the Fair Work Act provides that the Commission is not bound by the rules of evidence and pursuant to section 590 the Commission may inform itself in relation to any matter before it as it considers appropriate.

PN10544

Given the nature of these proceedings we consider that it is appropriate to admit the evidence. Further, we are not persuaded that any unfairness arises from the admission of the evidence having regard to the manner in which we propose to deal with the evidence. We acknowledge that the witness does not appear to have stated the factual basis for the opinions expressed which are the subject of the objection. In this regard we reject United Voice's submission to the extent it goes

this far, that the sentences in question are merely the reasons for the opinion expressed by Professor Quiggin at paragraph 20 of his report.

PN10545

Even if that were so, the basis of the reasons has not been disclosed. We propose to ask the witness questions regarding the basis of the opinions expressed which are the subject of the objections. The witness can then be cross-examined and re-examined as to these issues as the parties see fit. In the absence of a satisfactory basis for the expressed opinions it is likely that we would give little weight to this aspect of Professor Quiggin's evidence. We would make the same observation more generally in respect of the other expert witnesses.

PN10546

That concludes how we - or the objections to Professor Quiggin's evidence.

PN10547

JUSTICE ROSS: Are we ready to proceed with Professor Lewis?

PN10548

MR GOTTING: If the Commission pleases.

PN10549

JUSTICE ROSS: Thank you Mr Gotting.

PN10550

MR IZZO: We just call Professor Lewis.

PN10551

THE ASSOCIATE: Please hold the Bible in your right hand and state your full name and address for the Commission.

PN10552

PROFESSOR LEWIS: Professor Phillip Edwin Thomas Lewis (address supplied).

<PHILLIP EDWIN THOMAS LEWIS, SWORN [9.52 AM]

EXAMINATION-IN-CHIEF BY MR IZZO [9.52 AM]

PN10553

MR IZZO: Your Honour, before I proceed to examine Professor Lewis, we noted recently that the reply evidence that Professor Lewis prepared to Professor Borland's expert evidence has the same page number appearing on virtually every page. After about page 3 every page number says page 26. What we have done is we have prepared some varied versions for the Court which merely change the page numbers. They've been handed to the union parties. I don't think there's any objection. I have five copies here, three for the members here and two for those absent.

*** PHILLIP EDWIN THOMAS LEWIS

XN MR IZZO

PN10554

JUSTICE ROSS: All right. Thank you.

PN10555

MR IZZO: Professor can I ask you, you should have four documents in front of you I hope?---Yes.

PN10556

Thank you. Good. The first document is a report that you've prepared for "Penalty rates in the retail, café, restaurant and hairdressing and beauty industries" and it runs for 47 pages?---That's correct, yes.

PN10557

So that's the first report. The second report is a report that's titled, "A reply to the report. Effects of penalty rates in the restaurant sector by Professor John Quiggin, University of Queensland" and that runs for 15 pages?---Yes, that's correct.

PN10558

The third report is a report "Penalty rates in the retail, café, restaurant and hairdressing and beauty industries. A reply to a report by Professor Jeff Borland" and that report dated 3 September runs for 39 pages and you should have some - the page numbers have been amended to ensure they're sequential?---Yes, that's correct.

PN10559

And the fourth document you should have with you is a one page document which starts:

PN10560

On the 17th of September 2015 I was asked the following question by Australian Business Lawyers and Advisers.

PN10561

You set out the question and your response. That one page document is dated 20 September 2015. Do you have that document with you?---I have, yes, thank you.

PN10562

You have. In respect of all of those four documents first of all can I ask you a series of questions. The first is did you prepare all four of those reports?---I did, yes.

PN10563

Do they contain opinions you genuinely hold?---They do.

PN10564

And are those opinions based wholly or substantially on your knowledge, experience or expertise?---Yes.

PN10565

I'd seek to tender all four documents, your Honour.

*** PHILLIP EDWIN THOMAS LEWIS

XN MR IZZO

PN10566

JUSTICE ROSS: All right. I think we're up to ABI3. We'll mark the four reports in order, ABI3, ABI4, ABI5 and the last one, the one page report that has been referred to, dated 20 September, ABI6.

EXHIBIT #ABI3 REPORT TITLED "PENALTY RATES IN THE RETAIL, CAFE, RESTAURANT AND HAIRDRESSING AND BEAUTY INDUSTRIES"

EXHIBIT #ABI4 REPORT TITLED "A REPLY TO THE REPORT. EFFECTS OF PENALTY RATES IN THE RESTAURANT SECTOR BY PROFESSOR JOHN QUIGGIN, UNIVERSITY OF QUEENSLAND"

EXHIBIT #ABI5 REPORT TITLED "PENALTY RATES IN THE RETAIL, CAFE, RESTAURANT AND HAIRDRESSING AND BEAUTY INDUSTRIES. A REPLY TO A REPORT BY PROFESSOR JEFF BORLAND" DATED 3 SEPTEMBER

EXHIBIT #ABI6 REPORT COMPRISING ONE PAGE AND DATED 20/09/2015

PN10567

MR IZZO: No further questions, your Honour.

PN10568

JUSTICE ROSS: Thank you Mr Izzo.

PN10569

Cross-examination?

CROSS-EXAMINATION BY MR DOWLING

[9.56 AM]

PN10570

MR DOWLING: Yes, your Honour.

PN10571

Good morning Professor Lewis?---Morning.

PN10572

Now it is correct that you have given evidence in this Commission before?---It is, yes.

PN10573

And particularly in relation to the question of penalty rates within modern awards?---Yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10574

And is it correct that in 2012 you were asked to prepare for Australian Business Lawyers and Advisers in respect of applications made by their clients to amend the Restaurant Industry Award?---That's correct, yes.

PN10575

Right, and that report that you prepared was relied upon by Australian Business Lawyers and their clients in seeking that review or variation of that award, the 2010 Restaurant Industry Award?---I'm not sure to what extent they relied on it.

PN10576

Perhaps I might provide a copy to you. You've got a document there headed "Restaurant Industry Award 2010. A report for Australian Business Lawyers and Advisers". Is that the report you prepared in or about 2012 for Australian Business Lawyers?---I think so, yes. It looks as though it's the report, yes.

PN10577

All right, can I ask you to turn to paragraph 12 of that report - sorry, my apologies. If you turn over the first page you'll see an introduction and at the bottom of page 2 you'll see a paragraph numbered 12. Do you have that?---Yes, that's right. Yes.

PN10578

And that starts:

PN10579

In the event that the Restaurant Modern Award was amended to -

PN10580

?---Yes.

PN10581

And it says:

PN10582

Exclude penalty rates for work on Saturdays and Sundays for full-time and part-time employees. Limit the obligation of loading, 25 per cent for casual employees working Monday to Sunday -

PN10583

et cetera:

PN10584

Eliminate penalty rates for work between 10 pm and 7 am for employees. Restrict -

PN10585

Over the page:

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10586

- payments for permanent full-time employees and part-time employees to 25 per cent loading for work on the sixth consecutive day and 50 per cent loading for work on the seventh consecutive day.

PN10587

And the last subparagraph:

PN10588

Casuals to a 50 per cent loading for work on the sixth consecutive day.

PN10589

Paragraph E deals with junior rates and paragraph 5 deals with small business employer provisions. If each of those things, you were asked:

PN10590

What impact would this have on the profitability of establishments and employment in the restaurant and catering industry and the efficient and productive performance of work in the restaurant and catering industry and on business, including productivity, employment costs, regulatory burdens in the restaurant and catering industry?

PN10591

Do you see all of that?---Yes.

PN10592

Does that accurately record the variations that were sought on which you were giving advice about the impact, in the second part of this paragraph?---This was - my report answered this question, I'm not quite sure to what extent. In later hearings, et cetera, these were actually sought or actually accepted.

PN10593

I might put the question in a different way. The basis of your opinion that you set out here is in the event of the variations that are identified in the first part of paragraph 12. Is that fair?---I'll just look at my answer to that question.

PN10594

Certainly?---Yes, there do seem to be just over two pages answering that point.

PN10595

So the answer you are giving in respect of the effect that's described in the second half of this paragraph 12 is the effect as a result of the variation sought in the first half of paragraph 12?---That's correct, yes.

PN10596

Is it also fair - excuse me for attempting to paraphrase such a large report, but is it also fair to say that your opinion as part of this report was that penalty rates had their origins in a labour market that was quite different to the modern Australian labour market?---That's correct, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10597

Is it also fair to say that your opinion was that Sunday penalty rates have not really been assessed in the light of contemporary circumstances, they are a bit of a relic?---I don't know if I would use the word "relic" but - - -

PN10598

A product of the past, they hadn't been properly assessed in terms of contemporary society?---It is a paraphrasing. I think I would say that their origins were very much in a different type of economy to the one we had and it was time to reassess some of those principles.

PN10599

Is it correct and fair to say that you have replicated significant portions of your 2012 report into the report you have provided as part of this proceeding?---That's correct, yes.

PN10600

Perhaps to assist you, because I want to ask you some questions about that, can I give you another version of your report provided in this proceeding, and what we have done in this report is highlight those parts that are replicated from your report from 2012. I might work from the back if that's okay. If I ask you turn to page 39 of the version of the report that I have just provided to you you'll see that part deals with who would benefit from removing penalty rates. Do you see that?---Yes.

PN10601

Save one sentence, that is a complete replication of that part that you provided in 2012?---That's correct, it's the same argument.

PN10602

Of course, in 2012 you were largely dealing with the removal of penalty rates, weren't you, as identified by Question 12 that I took you to a moment ago?---That's correct, yes.

PN10603

You're not dealing with the removal of penalty rates in this proceeding are you?---I was asked the - my report specifies - I simply was asked questions by Australian Business lawyers and advisers and wrote my report in answer to those questions.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10604

Did you know when you wrote the answers to your questions whether you were dealing with the removal of penalty rates in the same way that they are described in Question 12 in 2012, or did you think you were dealing with some other type of variation?---I simply pointed out the effect of removal of penalty rates. In fact I think in the modern - in the more recent one, there are something like 11 possible changes that are proposed and, therefore, to deal with each one of those in turn would be rather onerous, and the basic point is you make the principle, that removal of penalty rates will actually have these effects, and if you simply modify

those changes then what you'll get is essentially the same substantial result but with a lesser degree.

PN10605

My question was a little different. My question was when you prepared the report in 2012, and I'm talking about the whole report, I'm not limiting it to this part, did you understand that you were dealing with the removal of penalty rates in the same way they were sought to be removed in 2012, or did you understand when you prepared your report - - -

PN10606

JUSTICE ROSS: No, no you need to rephrase your question. You started by referring to the 2012 report. I assume you're referring to his most recent report.

PN10607

MR DOWLING: I am, my apologies. When you prepared this report filed in this proceeding in 2015 did you understand that what you were being asked to comment on related to an application to remove penalty rates in the same way they were being sought to be removed in 2012?---I was aware that the actual proposal was not to remove them altogether but my brief from the Australian Business lawyers was that that was the question that I was to address.

PN10608

I suggest to you also that you were, in terms of the brief you were provided, you were not at any stage asked to answer the question who would benefit from removing penalty rates. Are you able to say whether that's correct or not correct?---I'm not actually sure without looking.

PN10609

You will see on page 2, to assist you, you say, "My report addresses the following questions," and none of those asked you to address the part commencing on page 39. Is that an accurate statement?---There are several of these questions which refer to what is the importance - sorry - what is the impact to the relevant industries of employment, et cetera. What impact do labour costs have on the profitability of the relevant industries, and to what extent do the penalty rate provisions affect employment in the relevant industries.

PN10610

Then what other supply and demand factors are important. I think it's important because you can't understand the effect on employment without looking at the whole economy effects. For instance, employment will rise largely because there'll be greater demand for the product and, therefore, to simply address employment in isolation from what the effects of the whole economy will be, and who will benefit from that, seems inappropriate.

PN10611

You accept you weren't asked the question who will benefit from removing penalty rates but you say, do you, that you thought it was a necessary ancillary part, did you?---That's correct.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10612

If you turn next to page 32, and that is the part commencing, "Are penalty rates relevant to the modern Australian economy?" Do you see that?---M'mm.

PN10613

Again, if you look at the following pages through to - all the way through to page 39, you will see, and I take it you accept, that that is a replication of what you provided in 2012?---That's correct, yes.

PN10614

If you next turn to page 21, and that deals with the employment effects, starting at the bottom of the page, again, I want you to cross-reference this, if you feel you need to, but again you accept that that is significantly a replication of what you produced in 2012?---That's correct.

PN10615

That leads to page 29, which is your Table 4A. Do you have Table 4A on page 29?---I do, yes.

PN10616

That sets out the estimated employment effects of penalty rates for Sundays and public holidays for permanent employees. It's correct that this sets out those estimated employment effects based on the complete removal of penalty rates, doesn't it?---That's correct, yes.

PN10617

I take it you are aware that the report you provided in 2012 was the subject of some comment by the Deputy President that heard the restaurants' review in 2012, and then later the Full Bench. They considered your evidence and they passed comment on it, didn't they?---I'm not aware of the comments.

PN10618

Perhaps to be fair, if I can provide you firstly with a copy of a decision of the Full Bench in the restaurants' review of 2012. I apologise, this is a little awkward, but if you could have your primary report in front of, that is the one marked ADI3, it's your long report of 47 pages. If you turn to page 32 of that report that's the part dealing with are penalty rates relevant to the modern Australian economy. Do you have that?---Sorry, which document am I looking at now?

PN10619

You are now looking at - I want you to have to one side for a moment the document you were just handed, which the decision of the Full Bench but, at the same time, if you can open your long report filed in this proceeding to page 32, sorry, to page 34, my apologies. If I can ask you to open the Full Bench decision at page 54 and you will there see a comment - you will there see a heading part-way down the page "Sunday Work Contemporary Australian Society and the Restaurant Industry Workforce." Do you see that?---Yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10620

They are there dealing with some evidence that you gave. You see there, before the dot points, it says, "Professor Lewis gave evidence to the following effect"?---Yes.

PN10621

I just want to confirm with you that the evidence you gave in 2012 is in the same form as the evidence you're giving in this proceeding. The first dot point is the change from 96 per cent to about 60 per cent. You will see that at the top of your page 34 in this present report?---Yes.

PN10622

Then the next dot point deals with the drop from 44 per cent to 17 per cent. You will see that in the paragraph at the bottom of page 34?---That's correct, yes.

PN10623

Then the third dot point is the 17 minutes. You will see that at the bottom of page 37 of your present report. I think you're referring to men there, for men, the amount of time spent on sport and outdoor activities increases by only 17 minutes per day?---M'mm.

PN10624

Then the last dot point, which is dealt with over the page by the Full Bench, the contemporary workforce being characterised by weekend as well as weekday work part-time, casual work, et cetera. You will see in the middle of page 39 where you say, "The Australian economy is dominated by the service sector in which part-time work, casual work, working men, flexibility are the norm," et cetera. So should we understand from that exercise that the evidence you gave and that was referred to in paragraph 123 in 2012 is the same as the evidence you give in this proceeding?---That's correct.

PN10625

I want to ask you some questions about that but while you've got page 55 open of the Full Bench decision you will see there at paragraph 125 the Full Bench says:

PN10626

It is necessary to note at the outset that much of the RCAV's case about the disability associated with Sunday work appeared to suggest that penalty rates have not been assessed in the light of contemporary circumstances and were a relic of a stage in the development of Australian society which existed in the mid-twentieth century but was long past.

PN10627

I put to you a little while ago that - I don't think you liked the word "relic" but you generally accepted that these penalty rates were something of the past, and I put to you that it was part of your evidence that they hadn't been assessed, hadn't been recently assessed. The Full Bench said:

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10628

This is not so. As recently as 2003 the issue of the disability associated with Sunday work and the proper penalty rate to be applied to such work was considered by a Full Bench in the context of their Victorian retail industry.

PN10629

Do you see that?---Yes.

PN10630

If you can skip ahead to paragraph 128:

PN10631

We do not consider that there has, since 2003, been any real change in the Australian society in the workforce such as to render the Full Bench decision in the SDA v \$2 and Under anything other than a contemporary general assessment.

PN10632

The view you held in 2012 that there hadn't been a contemporary assessment, I'm suggesting to you, was quite directly criticised by the Full Bench in 2012.

PN10633

MR IZZO: Can I object, your Honour. My recollection - there's two issues here, I think. If we go to paragraph 125 of the Full Bench's decision - - -

PN10634

JUSTICE ROSS: Do you want to deal with the objection in the absence of the witness?

PN10635

MR DOWLING: I don't know what the objection is.

PN10636

JUSTICE ROSS: No, neither do I. Perhaps if you can put it, discuss it, and we'll see.

PN10637

MR IZZO: My understanding is they would like Professor Lewis to leave the room.

PN10638

JUSTICE ROSS: Professor Lewis, can we ask you to just wait outside for a moment while we deal with this?

<THE WITNESS WITHDREW

[10.18 AM]

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10639

MR IZZO: Your Honour, I understand that the two propositions that are being put to Professor Lewis, the first, is that he has given an opinion that penalty rates haven't been assessed for some time. The second is that in 2012 he held a view that penalty rates have not been assessed for some time. That is not the evidence

he's given today. When he was firstly cross-examined on this issue he said, no, that's not the case. He said their origins are from historical - - -

PN10640

JUSTICE ROSS: This was about the relic point?

PN10641

MR IZZO: Sorry.

PN10642

JUSTICE ROSS: Was that in response to the relic proposition?

PN10643

MR IZZO: Yes, that's right. Then, secondly, if we go to paragraph 125 - - -

PN10644

JUSTICE ROSS: Just in relation to that point, can't that be dealt with by Mr Dowling simply asking the question about what his view is? What his view was then? We can crystallise how he puts that. But I mean wouldn't you characterise his evidence in these proceedings as being that penalty rates don't suit contemporary circumstances?

PN10645

MR IZZO: That may well be his evidence but it's not that they haven't been recently assessed by the Commission. I think they're two different concepts. What is being put to him is that they have been recently assessed.

PN10646

Professor Lewis is not a lawyer, he's not dealing with whether they've been assessed recently or not. He is dealing with whether they're relevant to today's society, not about what the Commission has done. That feeds into the second element of the objection, your Honour, because at paragraph 125 - - -

PN10647

JUSTICE ROSS: Just bear with me for a moment, Mr Izzo. Yes?

PN10648

MR IZZO: At paragraph 125 what the Full Bench says is that it's RCAV's case that the penalty rates haven't been assessed. That was the case of the party bringing the application, not that that was Professor Lewis's view. The question that has just been put to him is that he has held a view - he held a view in 2012 that they hadn't been assessed contemporaneously - sorry let me rephrase that.

PN10649

The question that was put to him is that he held a view in 2012 that penalty rates hadn't recently been assessed and he holds that view now that they haven't recently been assessed. I don't think he's ever given that evidence, so I am saying the basis upon which the question has been put is not correct.

PN10650

DEPUTY PRESIDENT ASBURY: But really, Mr Izzo, wasn't Professor Lewis's response to that question not so much the penalty rates themselves, but he was

talking about the principles upon which they're based? I thought that's what he was referring to when he said it's time to reassess some of the principles. That's what he actually said in my recollection. I don't know he's even talking about the level of the penalty rates, I think he's talking about the principles upon which they're based.

PN10651

MR IZZO: Your Honour, my understanding of that type of comment is that he is saying that, yes, the rationale behind penalty rates which has its origin historically is not appropriate for today's society. I think he is making that point. But the point he is not making is that the Commission hasn't recently looked at this or hasn't recently considered this, and that is what is being put to him by the United Voice.

PN10652

JUSTICE ROSS: At paragraph 25 even that proposition as a submission is inferred by the Full Bench rather than - they don't seem to be saying that they put that. I mean not having gone through the transcript of it. They may have, but they say - the Full Bench says in the second sentence:

PN10653

It is necessary to be noted at the outset that much of the RACV's case was about the disabilities associated with Sunday work.

PN10654

So the proposition is that much of the RACV's case about the disabilities associated with Sunday work appeared to suggest that Sunday penalty rates have not been. So, I'm not sure that even the RACV was putting that penalty rates had not been assessed in the light of contemporary circumstances.

PN10655

Your proposition is the Professor Lewis didn't put that and it was the RACV's case. I'm not even sure on the basis of that paragraph if it was - - -

PN10656

MR IZZO: Your Honour, as someone who was involved in that case, I think the \$2 case was referred to in submissions. But I think that's somewhat - I think that just reinforces the view that regardless of what the RACV position was certainly it's not a position that Professor Lewis has expressed.

PN10657

JUSTICE ROSS: So the essence of your objection is that the question is unfair because the basis is incorrect, he hasn't given evidence of that character.

PN10658

MR IZZO: That's right, your Honour.

PN10659

JUSTICE ROSS: What do you say about that, Mr Dowling?

PN10660

MR DOWLING: I have understood his evidence in the same way that Deputy President Asbury had understood it, and that is that he was effectively saying the principles needed to be reassessed. That includes the reasoning behind it, the justification for it. He is saying that needs to be reassessed. Now, it's at odds, we say, with the Full Bench, saying we have.

PN10661

JUSTICE ROSS: That's a different proposition to say that, that the principles need to be reassessed, you then - isn't there a leap in logic to suggest that, well, he is saying that they haven't been assessed in the light of contemporary circumstances by us. Well, he hasn't made any submission about what we're doing.

PN10662

MR DOWLING: I can ask him that.

PN10663

JUSTICE ROSS: Perhaps if just the basis is dealt with first, and then the question, that would resolve the objection as well.

<PHILLIP EDWIN THOMAS LEWIS, RECALLED ON FORMER OATH [10.25 AM]

CROSS-EXAMINATION BY MR DOWLING, CONTINUING [10.25 AM]

PN10664

MR DOWLING: Thank you, Professor Lewis. Could I ask you to turn to - I want you to keep with you there the decision of the Full Bench that we've already looked at, and perhaps if you can go to page 32 of your report, which I think you have got open. On that page you should see the heading, a third of the way down, "Are Penalty Rates Relevant to the Modern Australian Economy." Do you see that?---Yes.

PN10665

The second sentence reads:

PN10666

However, penalty rates have their origins in a labour market quite different to that of much of the Australian labour market today.

PN10667

The last sentence of that paragraph:

PN10668

The Australian economy has undergone significant structural change over the past decades as discussed earlier.

PN10669

Jumping a paragraph:

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10670

Penalty rates have their origins in the old economy.

PN10671

Should we understand from that evidence, firstly, that it's your view that penalty rates and their origins need to be reassessed in the light of the modern Australian economy?---They need to be - sorry - my view is that the need to be reassessed in the light of the fact we have a modern service-based economy.

PN10672

Secondly, is it your view that this Commission has not properly reassessed those penalty rates and their origins?---It may have properly assessed in terms of their own view. My view is that another assessment would come to a different conclusion.

PN10673

Another assessment since the one they refer to in 2012?---Yes.

PN10674

You don't say there's been any marked change since 2012 of course?---I don't think there's been a change but I think - I personally would disagree with their assessment of 2012.

PN10675

I think I took you to paragraph 125 and then I took you to paragraph 128. Can I ask you to go back to paragraph 128 and particularly to the last sentence of that paragraph? You see there it says:

PN10676

Indeed we consider that Professor Lewis's evidence to some extent missed the point. He described Sundays in terms of various types of activity, when it is the lack of activity on Sundays which provides space for leisurely interaction with family and friends.

PN10677

Do you see that?---I do, yes.

PN10678

Have you seen that criticism before?---I have seen it before, I can't quite recall where.

PN10679

It's been drawn to your attention at some stage has it?---No, I think I actually saw it as one of the either (indistinct) comments, I'm not sure. And I've also - it rings a bell but I couldn't actually pinpoint exactly where I've read it.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10680

Is it something that you took into account at all in the preparation - we know this part? They are referring to, as I understand it, at least significantly, the evidence you set out at paragraph 123, the effects in terms of religious observance and time

spent on weekends, and they are saying that, in some respects, misses the point. Was that something that was brought to your attention before you filed the report in this proceeding in 2015?---It hasn't been drawn to my attention by anybody in particular.

PN10681

But is it something you were aware of before you prepared your report in this proceeding in 2015?---It's a difficult one because the lack of activity works both ways, doesn't it? I mean - - -

PN10682

I'm not asking you to answer the question at the moment, for the moment I'm just asking you whether this is something you were aware of when you prepared your report in 2015?---I am aware that, yes, for a lot of people, the lack of activity on Sunday is quite important.

PN10683

But you chose not to address this very criticism in your report in 2015, did you?---But the – my argument was essentially the crucial one was that addressing, again, comments that I quoted in my original report on page 17, that in fact even in as far as 2005 MPs who were in Parliament were saying various things about the importance – the very importance and sport and religious activity and I was addressing those two particular questions.

PN10684

Yes. That's at page 33 where you encapsulate a speech from the New South Wales Parliament?---That's correct.

PN10685

I'm not asking you about that. I'm asking you whether, if you're aware of the criticism that you've missed the point and what you should have been looking at, whether you agree with it or not, was the lack of activity of Sundays is something you chose not to address in this report in 2015; is that right?---I chose – no I didn't address it, no.

PN10686

And can you explain why you didn't address it?---I didn't think it particularly important to the main argument.

PN10687

All right. Now, can I then ask you, whilst you've still got the Full Bench decision in front of you, can I ask you to turn to paragraph 99? You'll see there this addresses the report that was filed, and the paragraph begins:

PN10688

Similarly the report commissioned to be prepared by Professor Lewis concerning the effect of penalty rates required him to assess -

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10689

et cetera. The next sentence begins:

PN10690

Professor Lewis stated a conclusion based upon the application of a mathematical formula to calculate the elasticity of demand for labour using 'reasonable assumptions' about the elasticity of substitution of labour and the elasticity of demand for output that the penalty rate and the restaurant award at 50 per cent on Sundays has reduced demand for labour on Sundays by 50 per cent as a lower estimate to 100 per cent as an upper estimate. He then used those figures to conclude that the reduction of Sunday penalty rates for casuals in accordance with the primary application would increase the demand for casual labour on Sundays between 29 and 87 per cent.

PN10691

Now, the next sentence reads:

PN10692

The alternative application was not actually modelled by Professor Lewis.

PN10693

Can I just clarify where they refer to the – if you can answer this. You may not be able to. There was an alternative application put in that case to vary penalty rates that are sought, so there was the application that I took you to in terms of question 12 and those removals, and then there was an application to vary which was an alternative application. Now, the Full Bench here say you did not model the alternative application. I just want to confirm from you that that's correct?---No, I didn't. I don't think so, no.

PN10694

All right. Can you turn ahead to paragraph 103. And the second sentence of 103 reads:

PN10695

Professor Lewis' report suggested that almost any regulatory intervention in that market produces inferior outcomes and proceeded on the basis that a largely unfettered labour market should be left to determine what, if any, extra payments should be made to employees who work on weekends.

PN10696

Stopping there, is that an accurate description of what your report suggests?

PN10697

JUSTICE ROSS: His report in these proceedings or?

PN10698

MR DOWLING: Sorry. Thank you, your Honour. I'm talking about your report in 2012?---Sorry. Right.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10699

That's what they are making comment on?---I don't think I say there's been no regulation I just – I think that essentially the markets do perform fairly well and that in fact probably a market rate would be better to determine the actual rates for

Sunday and public holiday and in this case it was because it was Saturday work. Clearly but I do believe there has to be a minimum wage of some description which has to be determined by society.

PN10700

So in terms of this regulation point is it a fair encapsulation of the evidence you've just described that, in terms of the penalty rate issue, that is not something that you think should be regulated. There might need to be other regulations in terms of the labour market, but in terms of the penalty rate issue that's not something that should be regulated?---Yes, that's probably a fair description of my opinion. Yes.

PN10701

Now, you'll see there, the Full Bench goes on:

PN10702

However the FW Act –

PN10703

that's the Fair Work Act –

PN10704

required intervention in the labour market by way of the making of awards by the Commission that achieved the modern awards objectives in section 134 and further requires the Commission in making awards to take into account the need to provide additional remuneration to employees working unsocial hours or working on weekends.

PN10705

And they there refer to a section of the Act. Now, what they're saying is it's not quite as simple, Professor Lewis, as saying we can't regulate anything to do with unsocial hours. We're forced to look at it by operation of this section of the Act. Again, is this something that your attention was directed towards this criticism that your attention was directed towards or that you're aware of when you prepared the report in this proceeding?---I am aware of that. It's just I realise the dilemma the Commission has because of the wording of the Fair Work Act.

PN10706

Is there a reason you didn't address this issue identified by this criticism of this paragraph?---What I was asked to do I – well, I was asked to report on what would be the impact for removing penalty rates on employment. Okay. What regulators choose to do after, okay, does not affect my decision nor my analysis that reductions in penalty rates and removal of penalty rates would actually have significant employment effects, and I wasn't asked whether this was legally possible, but I presume, particularly in the current political climate it's a very valid issue to be discussing.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10707

But you appreciate, of course, you're here to assist the Commission and the Commission is saying, as I para-phrase it in paragraph 103, it's not as simple,

Professor Lewis as saying we can have a completely unregulated penalty rate system. We have to look at it. Now, I'm suggesting to you, as a responsible expert, coming along here, giving advice to this Commission about a completely unregulated penalty rate system you should have had regard to the criticism that's made in paragraph 103?---But I did in my comments, for instance, on Professor Rose, point out that in the market system the rates would not actually fall to the non-penalty rate. They would actually fall, but there would still be a significant premium for working Saturdays and Sundays, and therefore I suppose in retrospect my view should have been more that if the Fair Work Commission needs to set a penalty rate it should set one much nearer to the market rate than the current one.

PN10708

But that's not what you were saying there. You were simply saying if it's left to the market the rate for Saturday and Sunday would be higher than the Monday to Friday because people wouldn't work for the Monday to Friday rate. You're not suggesting that that reply was answering the criticism that's addressed in paragraph 103, are you?---What I'm saying is this is the impact that penalty rates are likely to have had on employment. Okay. If you remove them all together there would be significant employment effects. I don't expect these to be totally removed but I would expect that, on the basis of that evidence, there would be sufficient reductions, and that the reductions would be more in line with what market rates have been identified by Professor Rose.

PN10709

All right. Can you go to the next paragraph, please. You'll see there it starts:

PN10710

The Commission and its predecessors have consistently rejected the proposition that labour market modelling of the type engaged in by Professor Lewis in his report based upon specific elasticities for the demand for labour are capable of providing a reliable guide as to the way in which changes to minimum wages and conditions actually affect employment levels, in particular industries or the economy generally.

PN10711

Had you read that criticism?---I haven't actually read this criticism, no.

PN10712

You hadn't read it?---No.

PN10713

I guess that would explain why you didn't address it?---I beg your pardon?

PN10714

That explains why you haven't addressed it. You've not seen it before?---I'm not sure – I'll read it and I'll tell you whether I've addressed it or not.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10715

My question to you, so that you're clear, is whether you were aware particularly of what is said in paragraph 104, and you made an effort to respond particularly to the comments in page 104 in your report in 2015?---I was aware that there was criticism that the modelling is not, by some parties, is not a very good kind. I disagree with that.

PN10716

Not some parties, the Commission we're talking about?---Okay. Yes.

PN10717

You're aware of it?---I'm aware of it, but the point is that if you haven't got a model to suggest what the minimum should be, what changes should be made, everything else is going to be an arbitrary decision.

PN10718

All right. Well, I'll come back to that. But while I've got you in the decision I want you to jump ahead to paragraph 111. Sorry, to be fair, I need to take you back to 109. And you'll see in 109 there's a reference to the annual wage review decision and there summation of the varying studies of elasticity of demand for labour in Australia with numbers ranging from minus .15 to minus .1. You see that paragraph at 109?---Yes. Yes.

PN10719

And then you - - -

PN10720

MR IZZO: Your Honour, in fairness, I think he should probably – if we can identify it's the annual wage review, the witness should be informed which year it was in. And to assist my friend I think that's identified in paragraph 108.

PN10721

JUSTICE ROSS: It's the 2005 review.

PN10722

MR DOWLING: Did you understand - - -?---Sorry?

PN10723

It's being suggested that the 108:

PN10724

Reliability of modelling of the effects of wage adjustments based on estimates as to the elasticity of demand for labour was extensively discussed by the Full Bench in the safety net review wages 2005.

PN10725

Do you see that? And then there's an extract at the top of the next page and then the extract in paragraph 109 dealing with the elasticities in the range of minus .15 to minus .8?---Yes, I can see that. Yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10726

All right. Now, if you then go to paragraph 111, it there address is your report, and it says:

PN10727

It may be observed from the decision from which we have quoted above that the various Full Benches were dealing with contentions concerning negative elasticities in relation to minimum wage increases. Professor Lewis, in his report, was of course contending for positive elasticities in relation to wage reduction noting that that distinction at the range of 1 to 3 as the figures calculated represent labour demand elasticity by Professor Lewis in order to model the effects of penalty rates do not appear to bear any relationship in terms of quantum to the numbers advanced in the debate referred to above.

PN10728

Again, is that a criticism that you were aware of when you prepared your report in this proceeding?---I wasn't aware of this criticism, no.

PN10729

And is it fair to say that you have maintained the same level in terms of the range of 1 to 3 in your report filed in this proceeding?---Which elasticity are you talking about, sorry?

PN10730

If you go to page 28 of your report, half-way down the page you say:

PN10731

On the basis of the above studies we can reasonably assume that the elasticity of substitution for hired labour is between 1 and 3.

PN10732

?---That's correct. Yes. However, for completeness, okay, other elasticities are included.

PN10733

All right?---Point 5, a mid-range of those estimates you have in the Commission's document.

PN10734

Yes. It's not included in that paragraph but you're referring to the table that appears over the page. Page - - -?---No, it's got:

PN10735

However, for completeness elasticity of minus 0.5 is included in the analysis.

PN10736

Yes, sorry, and where you say "included" you're referring to it being included in the table that follows over the page?---That's right.

PN10737

All right.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10738

JUSTICE ROSS: Mr Dowling, the Full Bench decisions to which you've been taking the witness to are dealing with the elasticity of demand for labour.

PN10739

MR DOWLING: Yes.

PN10740

JUSTICE ROSS: Not the substitution elasticity.

PN10741

MR DOWLING: For higher – I appreciate that. Thank you.

PN10742

JUSTICE ROSS: All right.

PN10743

MR DOWLING: And in the last sentence of the same paragraph you say you've included the point 5:

PN10744

Including the analysis to account for the possibility that there is a lesser degree of substitution than suggested by the above studies and the price elasticity of demand for the relevant industries is between minus .1 and minus .3

PN10745

?---No, it's between minus 0.1 and minus.3.

PN10746

Sorry. Yes, minus 0.1. You maintain those elasticities?---They're in the table, yes.

PN10747

Yes. Now, I want to ask you one other thing about this proceeding in 2012 and it requires me to show you also what it was that the Deputy President had to say. Can I hand to you a copy of her decision. Do you have that? Do you have a document headed Decision and it has a date, 10 October of 2013 on it?---Yes, I have.

PN10748

All right. Can I ask you to turn to page 39?---Page 39?

PN10749

Of that document.

PN10750

JUSTICE ROSS: Paragraph 39 or?

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10751

MR DOWLING: Page 39, your Honour?---I haven't got – no page numbers.

PN10752

JUSTICE ROSS: I haven't got the page numbers.

PN10753

MR DOWLING: Sorry. Mine has page numbers. It appears other people's doesn't. If you can turn then to paragraph 235. Do you have a paragraph commencing:

PN10754

It is surprising given that.

PN10755

?---Yes. Yes.

PN10756

You're smiling. Have you seen this paragraph before?---No.

PN10757

You haven't. All right?---It's funny how confusing it is.

PN10758

Let me read it to you:

PN10759

It is surprising given that there have been times in Australia when penalty rates were not mandatory that no empirical evidence was able to be called to support the theory put forward by Professor Lewis that if wages costs are reduced employment would increase. In the period March 2006 until 1 January 2010 the new constitutional corporations there were no penalties payable as these businesses were only required to comply with the Australian Fair Pay and Conditions Standards, and since 1 January 2010 they have been transitioning from 0 per cent penalty rates to the full penalty regime in the award.

PN10760

Now, is it your evidence that that paragraph was never brought to your attention?---Yes.

PN10761

Well, perhaps, if you wait there for one moment. Sorry, to be fair, I need to take you on a little bit. Paragraph 236:

PN10762

Further in Victoria State Common Rule Awards were abolished in 1993 and were not re-established until 1 January 2005. Employees who were employed by the same employer when the Common Rule Award was abolished had their conditions rolled over but new employees were only entitled to the minimum terms and conditions set out in schedule 1A.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10763

And, again, the Deputy President there she says:

PN10764

No empirical evidence was called that showed that during this time Victoria had created additional jobs in the restaurant industry and other industries or contributed to greater economic activity or increased Victoria's GDP. Despite these periods of deregulation no empirical evidence was provided which supports Professor Lewis' proposition that reduced labour costs led to an increase in employment.

PN10765

Should we take it that you haven't seen any of those paragraphs?---That's correct.

PN10766

I need to take you back to the Full Bench decision. I'm sorry you've got so many documents there in front of you, Professor Lewis. Can you go back to the Full Bench decision to paragraph 118. There's a paragraph there that says:

PN10767

There are clear examples in the history -

PN10768

Do you have that paragraph?---Yes.

PN10769

of industrial regulation of the restaurant industry in which weekend penalty rates have been abolished or reduced but no evidence was forthcoming to demonstrate that this had discernably positive effects in terms of turnover and employment.

PN10770

Do you see that?---Yes.

PN10771

And then the Deputy President was correct, referring to 2006, 2010. Jumping to the next sentence:

PN10772

However no evidence was called –

PN10773

And I want to draw your attention particularly to the next sentence. The one beginning:

PN10774

There was another historical opportunity which we can identify. Prior to the work choices period commencing in 2006 restaurants in New South Wales were largely regulated by an award of the Industrial Relations Commission –

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10775

Reference decision of Justice Marks –

PN10776

In 1996 the New Wales Commission heard and determined various applications including an application from Restaurant Catering Association of New South Wales and other employers in respect of that award. The employer's application sought, amongst other things, a reduction in weekly penalty rates.

PN10777

I'm suggesting to you that that presents another, what might be described as, a period for a natural experiment was – have you seen that paragraph before?---No, I haven't.

PN10778

All right. As part of your report in this proceeding were you asked to look at periods where there had been a change in penalty rates or some other change in the wage rate that might provide a natural experiment for you to set out some empirical basis for your simulation exercise? Is that something you were asked to do in this proceeding?---I do believe, if my memory serves me correctly, I did get an email asking were there any periods of when – along the lines you've described.

PN10779

To assist your memory?---Thank you.

PN10780

You'll see this is an email from Mr Izzo to you dated 4 June. And can I take you to the second paragraph which reads:

PN10781

It might be of help if we could also look at employment consequences that have taken place in those periods where labour costs have not increased in the past, i.e., during the accord or perhaps during the one year in 2008/2009 when there was no minimum wage increase. The reason we raise this is that the Fair Work Commission's judgment on penalty rates two years ago was critical that we had not provided evidence of circumstances where flat wage periods have had positive impacts on employment, et cetera.

PN10782

Do you recall receiving that email?---Yes. I do now, yes. Yes.

PN10783

And when you read that the Fair Work Commission had been critical in the judgment two years ago, did that prompt you to go back and read how it was they had been critical for not providing that type of evidence?---I think I concentrated more on the accord period rather than one year in 2008/2009 which I regarded as hardly likely to share much evidence.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10784

That's not the question, Professor Lewis?---I know, but I'm saying – let me finish. The – in order to undertake an exercise like the one you're describing would actually entail quite a detailed research project requiring - - -

PN10785

That's not my question either, Professor Lewis?--- - - -considerable funding and therefore I didn't undertake it.

PN10786

That's not my question either?---No.

PN10787

Did you - - -?---So I can - - -

PN10788

- - -when you received an email saying that the Fair Work Commission had been critical, in Mr Izzo's words, did that prompt you to go and have a look at the Commission judgments that I've just taken you to to see how it was they were critical about a failure to provide this type of empirical evidence. Did you do that?---No, I did not.

PN10789

And is there a reason you didn't do that?---I didn't think it was relevant given that I thought it would be a very difficult research exercise to carry out.

PN10790

You didn't think it would be relevant to conduct some empirical evidence based on a natural experiment period. You didn't think that would be relevant?---I think it may have been relevant. Right. But, given the time available, and this is dated June, and I believe the report was in – my final report had to be done within – I can't remember, July, I think. I didn't think there was enough time for us to carry out the detailed experiment that would bring about that information.

PN10791

Did you think it might be prudent, given you're here to assist the Commission that you would at least look at their criticisms and explain why it is you hadn't addressed their criticism?---I think it might be in retrospect, yes.

PN10792

But you chose not to look?---I used - - -

PN10793

MR IZZO: I think he's answered that question anyway, your Honour.

PN10794

MR DOWLING: I'll withdraw that, your Honour. It might be a convenient time. Can I please, your Honour, tender, working backwards, the email that I've just shown Professor Lewis.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10795

JUSTICE ROSS: I think the next exhibit is United Voice 21. I'll mark that exhibit UV21.

**EXHIBIT #UV21 EMAIL FROM MR IZZO TO PROFESSOR LEWIS
DATED 04/06/2015**

PN10796

MR DOWLING: Can I separately tender that version of professor Lewis' report filed in this proceeding that marks up those parts that are replicated from 2012.

PN10797

MR IZZO: Your Honour, can I just make one comment in respect of that?

PN10798

JUSTICE ROSS: Sure.

PN10799

MR IZZO: I know that my friend has asked Professor Lewis about whether certain sections replicate what occurred in 2012. I don't think he took him to all of the sections. Could we just reserve a right to perhaps – and I'm sure this can be dealt with, if there is any issue between the parties, but if - - -

PN10800

JUSTICE ROSS: Yes. It's really just a comparison of the two documents, isn't it?

PN10801

MR IZZO: It's just a comparison of two documents. If we identify any issue in that, then we reserve our position on the tendering, but I imagine it shouldn't cause any huge issue.

PN10802

JUSTICE ROSS: All right. I'll mark that exhibit UV22.

**EXHIBIT #UV22 PROFESSOR LEWIS' REPORT REPLICATING
2012 REPORT**

PN10803

MR DOWLING: I should, for completeness, put in evidence also the 2012 report.

PN10804

JUSTICE ROSS: Exhibit UV23.

EXHIBIT #UV23 PROFESSOR LEWIS' 2012 REPORT

PN10805

MR DOWLING: And I don't know whether your Honour is minded to mark as exhibits - - -

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10806

JUSTICE ROSS: No, I don't think we need to.

PN10807

MR DOWLING: Thank you, your Honour.

PN10808

JUSTICE ROSS: The two decisions you mean?

PN10809

MR DOWLING: Yes. Now, can I ask you next – I'm sorry with all of the documents. I might – I can tidy them up for you. The two decisions: the decision of the Full Bench and the decision of Deputy President Gooley you can put those to one side?---Yes, excellent.

PN10810

Now, what I would like to have before you now is the report you prepared that is the reply to Professor Borland. I think you were - - -

PN10811

JUSTICE ROSS: ABI5.

PN10812

MR DOWLING: ABI5. That's right, your Honour. I think you have a copy which is different to mine, Professor Lewis, marked with page numbers handwritten at the bottom, but that won't cause a problem for us. Now, can I ask you to turn to page – sorry, that part of that report where you are responding to paragraph 8 of Professor Borland, which is at page 4. Now, you're aware, of course, having read what Professor Borland has to say, that he is critical of you for your use of the minimum wage literature. You understand that as a general criticism of course?---Yes.

PN10813

It was a general criticism, of course. Now, what you say in response to that is included under paragraph 8 in the bold, red type. In the last sentence you say there: "The evidence on minimum wage effects is not directly relevant. Rather it is the estimates of elasticities from minimum wage studies which are relevant." You see that?---Yes.

PN10814

Should we understand from that that your elasticities are derived from those minimum wage studies?---No, they're not.

PN10815

All right?---Partly, sorry; one or two of them fall within that range. Most of them are from other studies but some of the - it does rely, use evidence from minimum wage studies.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10816

I'm confused because as I understood it from that sentence, you say, "It is the estimates of elasticities from minimum wage studies which are relevant"?---Because this relates to the minimum wage.

PN10817

So at least some of your elasticities are taken from those minimum wage studies?---That's correct, yes.

PN10818

Now, I simply want to suggest to you that there is a difference with the elasticities coming from minimum wage studies that makes them not reliable for penalty rates purposes and that is because the elasticities coming from the minimum wage studies will apply relevantly to all relevant employees, whereas the penalty rates will apply only to some employees with respect to some hours they work in some industries. Is that a fair criticism of a contrast between or one reason to be cautious in using elasticities from minimum wage studies?---Could I explain? There are two elasticities: one is the elasticity of employment with respect to the minimum wage, which is generally regarded to be low. Clearly, that is not relevant to this penalty rate case. I rely on the elasticities of substitution, some of which are a byproduct of the minimum wage studies. In fact, high elasticities of substitution imply minimum wages have little effect. So one would expect high elasticity substitution, which is my argument for penalty rates having employment effects, you actually get relatively low minimum wage effects.

PN10819

Well, to be fair to you I need to put to you squarely Professor Borland's criticism and his criticism firstly is when you are deriving your elasticities from the minimum wage studies, they are not reliable to use for an examination of penalty rates because they apply to all employees. Penalty rates only apply to some employees.

PN10820

MR IZZO: Objection, your Honour. I actually think that's not a summary of Professor Borland's position at all. I actually think - and I'm happy to do this in the absence of the witness - but I think that's quite a misstatement of Professor Borland's position.

PN10821

JUSTICE ROSS: Well, even if it's not put by Professor Borland, why can't he put the question?

PN10822

MR IZZO: He can put it but he's said that it's Professor Borland's view and I'm saying it's not.

PN10823

JUSTICE ROSS: Right. You can take us to the part of Professor Borland's report or just ask the witness what's the criticism?

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10824

MR DOWLING: Can I take you to paragraph 9 of Professor Borland's report? There he says: "In my opinion the evidence cited by Professor Lewis is of little relevance to the question of how a change in penalty rates would affect employment. The empirical studies cited examine types of wages changes that are very different to changes in penalty rates and examine effects on populations of workers who are different to the workers who are affected by penalty rates." You understand that criticism?---With respect, I think - as I say in my comment below - Professor Borland has missed the point. I agree, okay, that the minimum wages elasticities are of little relevance to the penalty rate case. However, the substitution - elasticity substitution - which nearly every study on minimum wage finds there is a high elasticity of substitution, okay - is relevant to the penalty rate case.

PN10825

I think what Professor Borland is saying, amongst other things, is that in using even in respect of the substitution these minimum wage studies, are you are allowing them to define your parameters and they are used - the elasticities, including the substitution elasticity - is used in a very different context, which makes what you say unreliable?---No, it's not - that's not true. In fact, if you actually look at my report I only quote two minimum wage studies in the analysis anyway. The rest are actually - most of the analyses are actually from proper studies of elasticity substitution. In the vast literature on minimum wages, as I say, the way - elasticity of the minimum wage is relatively small because the effect on total employment is relatively small but the effect on particular groups of workers is high, okay? So you rightly point out that applying minimum wage to all workers is completely different to applying a wage - an increasing wage to a particular group of workers.

PN10826

You understand that Professor Borland adopts a different approach and that he says if we can't use it we shouldn't use any of the minimum wage literature as our parameters and as our framework. Perhaps the better thing to do is to go back to first principles, which Professor Borland tries to do, and ultimately concludes that the upper estimates - upper estimates of elasticities provided by you are - I think it's fair to say - implausible. You understand that's the approach that he's adopted?---With respect, the - those large elasticities are substitution labour studies. They're actually found from a study done by the bureau of labour market research on youth unemployment. They're also studied by Daly for the Productivity Commission; highly recommended study; also a wealth of studies summarising (indistinct) 1995 book and in the new Malcolm Washer book, two thousand and - I forget. There's an article in - they have got an NBR version of it in 2006. That is not the point. If there is substitution minimum wages have little effect on total employment because certain workers lose their jobs because they're not employed at the new minimum wage but other workers are employed because they're now better value for money compared to those previous minimum wage workers. So the effect on total employment is small so you must have a low elasticity of the minimum wage if there is high substitution.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10827

Perhaps I need to put the question differently?---So the point is - I mean, low minimum wage elasticity implies labour is highly substituted.

PN10828

Perhaps I need to put the question a bit more broadly to fully encompass Professor Borland's criticism. He says this simulation exercise - the derivation from these elasticities from whatever source that you have used - are not reliable and that the proper way to do it and the only sensible way to do it outside of the simulation exercise is to go back to first principles and when he does that his conclusion is your results are implausible?---Sorry, could you point out where he uses first principles?

PN10829

I don't think you have all of Professor Borland's report there. You have those parts that you've responded to. So for completeness I need to give you a copy. Perhaps as a way to short-circuit this, if you go ahead - I think the relevant part is at paragraph 29 of - which you'll find - sorry, I'll just confirm the handwritten page number for paragraph 29, page 17. Could I ask you to read paragraph 29? It's at the bottom of that paragraph that I want to direct your attention: "This assumption is not appropriate for the case of penalty rates. The main conclusion that follows is that penalty rates increase the relative cost of labour to capital much less than assumed by Professor Lewis and much less than in the empirical studies of elasticities of substitution that he describes, since all of those studies are about wage changes that apply to every day that firms operate, hence the estimated change in employment due to substitution of capital for labour, will be much less than assumed by Professor Lewis." Have you read that?---I have.

PN10830

I'm putting to you that is a correct analysis?---It's incorrect in the sense that it confuses two issues: one is the decision of the firm of the optimum capital stock, which of course will be determined largely by the cost of labour and the cost of capital on a normal day and a normal business and on capacity constraints, okay? So the size of the building, the tables, chairs, crockery, et cetera, will be determined, okay? Once they are determined they become a fixed cost.

PN10831

Yes?---The only decision a firm has to make from there is how much to vary the variable cost, which is essentially labour, and that will be determined by the cost of labour at any particular time. You can't share the labour cost out and say, "This is the average cost of labour."

PN10832

I think you agree then that those fixed costs, all of those fixed costs you describe there, they are assessed across the seven days?---Yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10833

Right. Can I take you back to - I just want to deal with two last things in relation to elasticities. Can I take you back to where you respond to Professor Borland's paragraph 11? I think he's critical of the range It's at page 6 and he - at the

conclusion of that sentence or that paragraph says: "That is the estimated elasticity cited by Professor Lewis is at the upper end of available estimates." You say, "Yes, the range of estimates of elasticity of average demand for labour is -0.3 to -0.8, slightly higher for hours with most of the range 0.6 to -0.8 and our estimates are within this range." As I understand the literature there is only one study at -0.8, which is yours, is that right?---I think so, yes; I'm not exactly sure whether that goes back over the old literature.

PN10834

When you say you're within the range you at the very upper end of the range?---The top end of the range, yes, yes.

PN10835

All right. Now, I think if I can take you to the response to paragraph 13, again so it's clear that this is put to you, which is page 7 in your document, and there is a criticism by Professor Borland about the industries that you've identified and what his criticism, do you understand, is that you've excluded other groups from the minimum wages? Sorry, let me rephrase that - I'll withdraw that: you've excluded other minimum wages groups; you've just concentrated on the minimum wages groups of the industries that you've identified?---In this article 10 years ago, what I sought to do was take a representative industry which had mainly award workers and the rest of the economy and I chose the industry on the basis it's the one that had been chosen by the ACTU to make a point at their case in 2004. So I thought it would be, given it had been used to show one view of the effect of awards and minimum wages, it would be only fair to use the same industry in my analysis.

PN10836

You understand Professor Borland's criticism? If you're looking at this minimum wage group and you're assessing it, amongst other things, against the economy as a whole, the proper thing to do would be to try and include all of the minimum wage industries and assess that against the economy as a whole, rather than just pick these industries?---Not necessarily; what you really want is industry where you have a large proportion of minimum wage workers or award workers and this particular industry I think was chosen by the ACTU because it was the largest industry containing these workers.

PN10837

Of course it was chosen in a different context. It wasn't chosen in this case. There was nothing stopping you in this case adding the other minimum wage groups?---With respect, this is a 2005 study which I'm quoting here, not the study done for this report.

PN10838

I think the other criticism that Professor Borland makes here is that it is possible, he says, that employment outcomes in the minimum wage sector and economy-wide in between '94 and 2004 may have been affected differently by other influences, such as relative growth in output and you say, well, it's not possible to control for all variables?---That's correct, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10839

It's fair to say that some variables are more easy to control for than others?---Possibly.

PN10840

And that growth in output is one of those variables you could easily have controlled for as part of this exercise?---I'm not sure it would have made that much sense but as I say, it was 10 years ago; more, of course, when I actually did the study and at the time I just wanted some quick way of looking at what had happened to minimum wage industries or award industries compared with those that had had enterprise bargaining.

PN10841

All right. When you say, "a quick way," was it - - -?---Well, it's not bad. What do you say, "Here's the changes in wages and here's the changes in employment." You notice in those industries that were basically award industries employment went up less than in the rest of the economy.

PN10842

You didn't think it was important at that time or necessary at that time to control for growth in output, for example? You could have done it but you didn't think it was necessary at that time, is that right?---I suppose what I was thinking at the time was that essentially I thought it was reasonable to control but in fact if the economy grows at X per cent it's fairly common that most of the industries are going to grow at more or less the same percent.

PN10843

I see. But it's not something that you've revisited?---No, I haven't revisited it, no.

PN10844

Can I lastly - at this point you referred amongst the studies that you identified a moment ago to the Daly et al study?---That's correct, yes.

PN10845

Excuse me one moment, Professor Lewis; I'm sorry. Sorry, I need to jump ahead a little bit to take you to this point so if I can ask you to jump ahead to page 11 and you are there responding to Professor Borland's criticism of the Daly et al study at paragraph 15 on the preceding page?---Yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10846

You see that? You say it's puzzling that he'd find fault with it. Is it fair to say you - he identifies the shortcomings of it in paragraph 15. You don't address those shortcomings. Is that fair of what it is you do in the paragraph that follows? You don't deal with them. Is that correct?---I suppose the reason is I've actually seen these arguments before and this as I say - as in most academic articles there is also fierce debate about the methodology and - et cetera. This particular article has gone through very, very rigorous peer review over the years and has been published by the Productivity Commission. I just don't think it is reasonable,

given that weight of opinion, that Professor Borland's comments would have much weight.

PN10847

Can I read to you - and you refer to it being referred to in the Productivity Commission - I'm sorry because of the size of the Productivity Commission report and other matters I can't hand this to you but I will read to you verbatim where this study is referred to by the Productivity Commission?---Excuse me, sorry; which report is this?

PN10848

The Daly et al?---So which report are you reading from?

PN10849

The draft Productivity Commission report?---This is the latest one?

PN10850

Yes, yes?---This is not the productivity report I'm referring to.

PN10851

It's not the Productivity Commission report?---The Productivity Commission produced the Daly report in 1998, okay?

PN10852

Have you seen any recent comment on - have you read the recent draft Productivity Commission report?---I've read it but not in great detail, because it's quite weighty. So - but I've read it through but I would hardly say I've absorbed it entirely.

PN10853

Do you recall any reference in it to this study we are now talking about; the Daly et al study?---No, I don't.

PN10854

Well, out of fairness I need to read to you part of it. It appears at page 876 for the Commission's reference and for the reference of the parties: "In a published research paper, Daly et al 1998, estimated the impact on youth employment of a change in average earning of youth relative to adults." There is a reference to a table C15. "They used cross-sectional data from the Australian workplace industrial relations survey from the year 1995, which they call AWIRS '95. The AWIRS '95 data did not include any data on capital and the authors therefore assumed weak separate ability in the cost function. Given this they estimated the share of youth hours of employment and total hours of employment as a function of youth average weekly earnings relative to adult average weekly earnings and output (proxy by total hours worked in a workplace) and an education index." Does that accord with your understanding so far?

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10855

MR IZZO: Your Honour, if Professor Lewis is going to be asked to respond to this, I think there is a large volume of material that is being put to him and I think

we all know the productivity report is extraordinarily lengthy. I know this is only being read from one particular section but I think in fairness to the witness it's not going to be possible for him to properly answer a question if a large part like this is read out to him and then he's asked whether he agrees or disagrees with it. Now
- - -

PN10856

JUSTICE ROSS: I suppose we'll know when we hear the question.

PN10857

MR IZZO: - - when we hear the question, yes, yes; I think that's right, your Honour.

PN10858

MR DOWLING: I just want to make sure that there's a Productivity Commission so far at least a summary of the study. Does that accord with your understanding, what I've read so far?---It sounds right.

PN10859

Okay. I just want you to tell me whether this accords with your understanding: the authors identified - and talking about the authors, Daly et al, themselves - the authors identified a number of possible shortcomings in their methodology. They reported evidence that the weak separability assumption may not hold and as a result the omission of capital from the equations may have biased the own-wage and cross-wage elasticity estimates. Is that consistent with your understanding of the author's identification of shortcomings?

PN10860

MR IZZO: I object. He's now being asked about the shortcomings that the authors of the Daly report identified in their report. He hasn't even put the document. I don't think that's fair to the witness. He should be shown the document if - - -

PN10861

JUSTICE ROSS: Which document?

PN10862

MR IZZO: I think it's the Daly report, because that's what he's being asked about.

PN10863

JUSTICE ROSS: He's cited the Daly report. Look, I think if he can't deal with it he'll say he can't deal with it. But if you're going to go through pages of the Productivity Commission report we'd be better off having an adjournment, photocopy it, give it to the witness and then take the witness through it.

PN10864

MR DOWLING: There is four sentences, your Honour.

PN10865

JUSTICE ROSS: All right.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10866

MR DOWLING: Does that description of the authors' identified shortcomings accord with your recollection?---It seems vaguely familiar but I wouldn't like to put my reputation on the line and say it's exactly what it says.

PN10867

The next sentence I will take you to, the authors also reported that the magnitude of the elasticity estimates for some equations was unreliable because of the small share of youth in the relevant data sample. Are you able to say whether that's accurate, to your recollection?---I think it is, yes.

PN10868

The next sentence that I want to - they also reported that there may be aggregation bias in the full sample and group estimates because the production structure may vary between industries?---That's correct.

PN10869

They then say, "A number of additional issues have been raised concerning the results of Daly et al by Janankar, Wait and Belchamber in 2000." Are you familiar with the Janankar, Wait and Belchamber study in 2000 raised issues concerning the Daly et al study?---I'm not too familiar. I know the debate at the time was fiercely lead by Grant Belchamber, who of course worked for the ACTU and Raja Janankar - sorry, I'm deviating a bit but it's important. We did have a very large conference held in Melbourne by the Productivity Commission to review this very article and we had eminent professors from the United States as well as the authors of the report and I remember Janankar and Belchamber were the fiercest critics of it. My recollection of that seminar was that their views were rejected.

PN10870

You accept that there's been criticism of it then, do you?---There's obviously criticism. Every academic article has criticism and qualifications.

PN10871

You accept - I'm putting to you that the Productivity Commission of this year reported those criticisms by Janankar, Wait and Belchamber in 2000?---Fair enough, yes.

PN10872

You, when you say there's been no criticism that you've seen, you just hadn't seen what's in the Productivity Commission report of this year setting out - - -?---The Productivity Commission report wasn't out when I wrote this report.

PN10873

It was of course out when you wrote your reply report in response to Professor Borland though, wasn't it?---Yes.

PN10874

Where you refer to the treatment of this study?---Yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10875

Where you refer to the treatment of this study, had you not seen its treatment in the productivity report - - -?---I hadn't seen it in this productivity - because I think from my memory I wrote this rejoinder in about four days and I wasn't expecting to have to read the whole of the Productivity Commission report in order to write the rejoinder.

PN10876

All right. I'm not asking whether you - putting to you whether you were asked to do that or not. I'm just asking you whether when you wrote this reply to Professor Borland you had not seen the criticism set out by the Productivity Commission report about Daly et al by Janankar, Wait and Belchamber?---To be fair, the Productivity Commission report did not criticise Daly. It simply reported that Janankar et al had critically - - -

PN10877

Had you seen it or not, Professor Lewis, when you wrote - - -

PN10878

MR IZZO: Your Honour, I think we've got a - - -

PN10879

MR DOWLING: No - - -

PN10880

JUSTICE ROSS: He can ask questions about when did he see the Productivity Commission report.

PN10881

MR IZZO: That's not the nature of my objection, your Honour.

PN10882

JUSTICE ROSS: All right. Could the witness be taken outside for a moment?

<THE WITNESS WITHDREW

[11.29 AM]

PN10883

MR IZZO: The nature of my objection is that I think that we may be conflating two issues: one is whether the Productivity Commission report has reported certain criticisms that have been made previously. The other is whether the Productivity Commission report itself criticises - - -

PN10884

JUSTICE ROSS: The witness has just given evidence and made exactly the same point.

PN10885

MR IZZO: But my concern is the witness doesn't even have the Productivity Commission report in his hands and he's trying to answer questions about this.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10886

JUSTICE ROSS: Well, he's answered the question in exactly the way you've put it. He's answered it and said the Productivity Commission did not criticise the report of Daly, that they reported the criticism by others.

PN10887

MR IZZO: But he's answering that based on his best recollection. In fairness to the witness, if he had the document in front of him he'd be in a better position to answer those questions, your Honour.

PN10888

JUSTICE ROSS: Can't the witness say that? I mean, he can indicate if he doesn't recall or if he wants the document. Have you got the Productivity Commission report there?

PN10889

MR IZZO: I've got the first volume but I think you said page 800, didn't you? I've got – my first finding goes to page 500 and I believe - - -

PN10890

JUSTICE ROSS: But the questions that the witness is being asked is what did he know when really. Did he read the Productivity Commission, was he aware of what it said at the time he wrote the rejoinder. What's wrong with that?

PN10891

MR IZZO: I have no objection to that. What I - - -

PN10892

JUSTICE ROSS: I thought that was the question.

PN10893

UNIDENTIFIED SPEAKER: That was the question, your Honour.

PN10894

MR IZZO: If that's the question, I don't have an objection. My concern is if the question being put is that the Productivity Commission has criticised that particular day report.

PN10895

JUSTICE ROSS: Let's just step back in this a moment. The witness has dealt with that question but, frankly, who cares what the witness says about whether the Productivity – how it's characterised? Isn't it clear on the Productivity Commission report? Whether they've criticised or they haven't, you can make submissions about that.

PN10896

MR IZZO: Certainly.

PN10897

JUSTICE ROSS: Otherwise it's just an opinion about what the Productivity Commission – how you characterise, you know, so I'm not sure how that's going

to assist us from any witness really. So, you're line of questions is about who knew what when type of - - -?

PN10898

MR IZZO: Yes, that's all.

PN10899

JUSTICE ROSS: Okay. Look, I think we'll take a 10-minute break now but can I just get an estimate as to how much longer you're likely to be, Mr Dowling?

PN10900

MR DOWLING: I think perhaps half an hour to 45 minutes.

PN10901

JUSTICE ROSS: Okay, are you batting up there, Mr Moore?

PN10902

MR MOORE: Yes, I am, your Honour.

PN10903

JUSTICE ROSS: And how long do you think you'll be at the crease?

PN10904

MR MOORE: Twenty minutes or so.

PN10905

JUSTICE ROSS: All right, well, we'll take 10 minutes now.

SHORT ADJOURNMENT [11.31 AM]

RESUMED [11.48 AM]

<PHILLIP EDWIN THOMAS LEWIS, RECALLED ON FORMER OATH [11.48 AM]

CROSS-EXAMINATION BY MR DOWLING, CONTINUING [11.49 AM]

PN10906

MR DOWLING: Professor Lewis, I was asking you some questions about what is said in the Productivity Commission draft report of August of this year about the Daly et al study. Can you just clarify for me when you wrote your reply to Prof Borland, were you aware of the comments made or the statements written in the Productivity Commission draft report about Daly et al?---No, I wasn't.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10907

Can I ask you to turn ahead, please, in your – I'm still in the document that is your response or your reply to Prof Borland – to page 12, and you'll see there – sorry, perhaps if you could turn back one page to page 11 – this is all under Prof Borland's heading Simulation Modelling of the Employment Effects of Penalty

Rates – and he sets out how he understands the equations, and then he says there are two main assumptions, and he sets out – (1):

PN10908

It is assumed that any change in penalty rates will translate dollar for dollar into a reduction in the wage rate paid to workers.

PN10909

(2):

PN10910

The calculation of the elasticities of employment assume that the organisation hiring workers is a profit-maximising firm operating for a single time period in an environment with perfectly competitive product and labour markets.

PN10911

And then he deals with the first assumption at paragraph 21 and 22 – I just want to be clear that you understand the comment made by Prof Borland and we understand your response to it. In your paragraph that appears below paragraph 22, the red bold, the third sentence commences:

PN10912

To the extent that the actual market rates of pay is determined by supply and demand for work on Sundays and public holidays might be somewhat greater than the market rate for work in non-penalty time then the estimates are biased upwards.

PN10913

And secondly, you rely on Rose – you understand Borland has criticised elsewhere, and you conclude in this part by saying:

PN10914

The high degree of unemployment among the unskilled and youth in Australia suggests many would be willing to work for non-penalty rates and the employment estimates in table 4(a) are appropriate.

PN10915

Should we understand from that that you are saying, because of – and the last sentence I'm referring to particularly – because of the high degree of unemployment among the unskilled and youth in Australia, if penalty rates were removed we would expect to see the same employment levels because these people would be willing to work for non-penalty rates, so we would see the same labour force, is that what you're getting at by that last sentence?---There would be more people employed.

PN10916

We'd have at least the same labour force because these people, the unskilled and youth, would still be willing to work for non-penalty rates, is that right?---There would be more employment, yes, because these people currently can't get a job.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10917

Are you able to tell the Commission what evidence you have for that assertion in the last sentence, that the high degree of unemployment among the unskilled and youth in Australia suggests many would be willing to work for non-penalty rates? What evidence do you present of that?---Well presuming people who are unemployed want to work, and I assume that they can't get a job at the current rates of pay, then if the rates of pay were to fall there would be more jobs available and there would be people who wouldn't stay at the jobs.

PN10918

But you're just assuming that they want work, they'll work for a non-penalty rate wage?---Well they may.

PN10919

They may?---Well we know they want to work because they tell us they want to work, otherwise they wouldn't be unemployed.

PN10920

Yes, but that doesn't tell you the wage at which they're willing to work though, does it?---No, but if the wage were to fall and they weren't willing to work that way they would no longer be unemployed. Because being unemployed, you had to be willing and able to start work.

PN10921

Perhaps I'll ask my question again. I understand the assumptions you've made in that process but is there any evidence that you point to that that is the case, that those unskilled and youth in Australia would be willing to work for non-penalty rates?---No.

PN10922

Are there any studies you point to to support that proposition?---I think it's fairly obvious.

PN10923

Can I next deal with your response to Prof Borland's paragraph 26, which deals with the second of the assumptions, so it's assumption 2 starts on page 15 – he's addressing assumption 2 – starts on page 15 and goes over to page 16, and it's there you address: affirms decision of how many hours to operate, whether to open at all or how many workers to employ et cetera on a Sunday or public holiday, independent of what has already occurred during the rest of the week. Again, I want to understand your evidence and I want you to understand the criticism that's made of it. I think a moment ago we were talking about fixed costs versus variable costs, and I think as I understand your evidence those fixed costs that we were talking about which might include the menu, the tables, the chairs, the kitchen, all of those sorts of things, they are fixed costs, and they are assessed over 7 days of the week?---They're just a fixed cost. No matter how many days you're open or closed, that's the cost, that's why they're fixed.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10924

Can I deal with your response there, at the top of page 16, in the context of the notion of the substitution of labour for capital, and to give you an example: if a business wants a new machine of some kind, the consequences of it might be – sorry, they want a new machine and the purchase of that machine might result in the reduction of a number of employees – say, for example, a special oven that might take away a particular employee's tasks. Is it right that that decision about the purchase of that capital that will affect the number of employees will be made after an assessment of the profit across all 7 days?---It remains an assessment of what the savings in labour costs will be over the whole week, yes.

PN10925

And in making that assessment, if you are making an assessment of the savings in labour from a reduction in penalty rates, you have to assess that reduction in penalty rates in that exercise across the entire week?---In that case, yes, you would expect that as the penalty rates were to fall then the firms would delay their purchases of new capital which replace labour and therefore create more jobs, yes.

PN10926

That's not my question.---It's the answer.

PN10927

It's not an answer to my question. If there's a reduction in penalty rates and you are making an assessment in terms of the purchase of this new machine, you will look at how that reduction in penalty rates affects the profit across all 7 days?---You're confusing two issues here, the profits and the decision to invest, the decision to invest to be taken by the relative price, capital relevant to labour, okay? Having established the capital stock is a fixed input, the decision is then how to allocate labour over the week to maximise profits in any particular period.

PN10928

And that assessment at least, we're agreed that assessment will be done over the 7 days?---No. If you've opened on Monday to Friday, that won't affect your decision on whether to open on a Saturday. The capital is fixed. The capital is fixed no matter what day of the week it is, so the only decision is how much labour you're going to employ for the business to operate Monday to Friday – that's gone, but now I'm going to decide whether to open on a Saturday or a Sunday or a public holiday. I make a decision on how much labour to employ depending on the cost.

PN10929

Perhaps I need to be clear. That's not what I was getting at. We're still talking about the purchase of this new oven.---Yes.

PN10930

And we're looking at the purchase of this new oven and we're assessing the profits, and the profits also as they're affected by wages and any change in them. That assessment will be made across the entire 7 days?---That's correct.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10931

Can I nextly deal with Prof Borland's report that you respond to which appears under the heading Imposing or Removing Penalty Rates. That one, I think is page 26 on my copy and on everyone else's copy. That is the real page 26. You will see there there's a heading on the bottom of the page Imposing or Removing Penalty Rates?---Yes.

PN10932

And you will see there, paragraph 38, Prof Borland says:

PN10933

The formula for predicting changes in employment when a change in wages occurs are intended to be applied for relatively small changes in wage rates.

PN10934

I will return to that. And this is - sorry, when I complete it - this is because:

PN10935

Once large changes in wages are considered, exactly the same absolute changes in wages will convert into very different percentages changes in wages, depending on whether an increase or decrease in wages is assumed.

PN10936

Now, he has two criticisms that he makes here: one is the way you do the calculation, but one is the use of the formula in this circumstance. And you understand his criticism that the formula are more appropriately used for applying in respect of relatively small changes in wage rates. Do you accept that criticism?---Sometimes yes, sometimes no; depends on the nature of the demand.

PN10937

He has a second criticism, and that is the way in which you have calculated the change in wages. To go back a moment to the process you've done here, you calculate the change in wage figure, you multiply that by your elasticity, and you come up with the employment effect?---That's correct, yes.

PN10938

So we're now only talking about the first figure, which is the change in wages figure. Prof Borland says you have to be careful about how you calculate your changes in wages figure, whether you are looking at imposing the penalty rate, and the percentage that creates; or whether you're looking at taking away the penalty rate, and what that creates. You understand the criticism?---Yes.

PN10939

So if you are increasing the penalty by 50 units, for example: the base wage is 100 in my example; you're increasing the penalty rate by 50, for example, so 50 is our numerator at the top of a fraction in this example; and the question is what denominator you have used. If you're looking at taking away the penalty rate, you have the denominator of 150; you will have 50 divided by 150; and if you're looking at adding the penalty rate you will have 50 over 100. Have I got that right so far?---That's correct, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10940

And, of course, you get very different figures. That example, 50 over 100 versus 50 over 150 produces a very different figure as to whether you're looking at imposing or whether you're looking at taking it away. Prof Borland says you've looked at imposing it; you've looked at the 50 over 150, and the consequence of that is you will get greater effects on employment at the end of your exercise. Correct?---It will be greater one way rather than the other, yes.

PN10941

Yes. And he says, "Let's look at doing it the other way and see what sums we get," and he sets out the examples in doing it the other way, 50 over 100 as opposed to 50 over 150. Your response to that, as I understand it, is to say, "Well, this problem is usually addressed by using the mid-point formula"?---That's correct.

PN10942

And in my example of 50 over 100 versus 50 over 150, using the mid-point formula we would have 50 over 125. Is that right?---That's correct, yes.

PN10943

So is it your evidence that that is the better way to do it, to do the mid-point?---It's a moot point because in calculating the elasticity you usually use the mid-point rule. The problem with the mid-point rule, it's very hard for people to understand, so what you get if you actually get a percentage change from one mid-point to another mid-point, neither of which, of course, is the actual penalty rate or the original wage. So typically we just use the one when we're going up and the other one going down. I know it's confusing.

PN10944

No, I'm not confused?---Aren't you?

PN10945

You say this is usually addressed by using the so-called mid-point formula. Do you now want to withdraw that evidence; or do you say this problem that Prof Borland - it is still right to respond to it by saying is usually addressed by using the so-called mid-point formula?---Yes, but as I'm saying, his estimates are unduly biased downwards, and mine are probably unduly biased upwards. The actual real - if there is such a thing as the real number - is somewhere in between, because as I say, it's using the mid-point rule, which I just used some examples in the blue text here, you actually get a number which is somewhere between the two.

PN10946

All right?---So I take the point that it is confusing.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10947

I don't think anyone is saying it's confusing other than you. Where do we end on all of that? Do you say, then, that the proper place - the more accurate calculation

in terms of the wage changed here would be to use the mid-point formula?---Probably, yes.

PN10948

You accept, of course, that you haven't?---I haven't, no.

PN10949

And you accept, of course, that you never have previously?---All I'm saying is if you use the mid-point you actually get the same - you get the same result of a percentage increase as you do a percentage decrease, but they're not the actual percentage increase and decrease. In your example you had a 50 per cent decrease compared to the 100 per cent increase, or whatever. Okay?

PN10950

Yes?---Okay. So you can't say that one is a much lower percentage change than the other, because it's the mid-point is the percentage change.

PN10951

Yes?---So using either method, you're going to get a different result. I'm saying it's quite common just use one or the other, as long as you make explicit what you're talking about.

PN10952

All right. Okay. You accept you haven't used the mid-point - didn't use the mid-point in 2012?---No.

PN10953

That's an answer, you say; you could use the mid-point. You've used, in your calculation, the imposition. Of course, we're not talking about the imposition of a penalty rate here, are we; we're talking about taking away. So in those circumstances if you're not going to use the mid-point, is it fair to say that it would be more appropriate to use the lower band? To use, in my example, 50 over 150, because the very exercise that the Commission is doing is to take away the penalty rate, rather than to impose it?---I think the main point of my illustration is - because I use a whole set of different assumptions. No matter what assumptions you use, effect on employment is large. I don't think anybody really knows for certain how much the employment effect will be, but it is unambiguously negative. The effect on penalty rates is unambiguously to reduce employment; and therefore reducing penalty rates will increase employment, whether you use the Borland method, my method, or the mid-point method.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10954

I'm just suggesting to you - I haven't got to the results yet, I'm just suggesting to you that when you're working out this change in wage figure, when you know the exercise for which you are doing it is a reduction in penalty rates, that the appropriate way is to do the lower band, the Borland approach, and to say: what the figure we should look at is the figure that's derived from a reduction in the penalty rate in these circumstances. Do you accept that that's right?---With

respect, I mean, the point - I was simply addressing the question that I was asked to address, which was: what impact have penalty rates had on employment?

PN10955

But you derived the process by which you came to the simulation exercise by which you chose how to calculate your change in wage figure. Mr Izzo didn't tell you how to do that, I assume?---No.

PN10956

So that's your figure. You chose that you would do the change in wage figure based on the imposition of a penalty rate. Is that right?---That's correct, yes.

PN10957

And I'm suggesting to you it would be more appropriate in the circumstances to do it based on the reduction in the penalty rate. Do you agree with that?---In retrospect, I think it probably would have been, yes. But whatever the value, the effect is very high - is negative.

PN10958

Thank you. Can I then jump ahead to Prof Borland's paragraph 52, which appears on page 34. And you've read this, obviously, and you understand the debate that Prof Borland is having with both you and, in effect, Prof Rose, is that in terms of the labour supply, that is appropriately determined by the marginal wage and not the average wage. You understand what Prof Borland is saying?---Yes, I do.

PN10959

And when he is assessing what it is that Rose has done, he says, "Well, it's not appropriate to look at the average wage when we're looking at the question of labour supply, it's appropriate to look at the marginal wage, and Rose doesn't tell me that," is what Prof Borland says?---In fact, I think you will find that the wage that Rose reports is actually the margin; it's the average of the margins. So they are exact - they are - they can be interpreted as the wage people are willing to accept.

PN10960

What you can't see - unless you engineer some figures that he has included - you can't see the full distribution which would allow you to see what the - on that full distribution - what the actual marginal rate is. You can't see it?---But the observed ones - it's an experimental design where people are asked what shifts and how many hours they would be willing to work at these rates; therefore that is their marginal rate. So Rose's estimates are averages of the marginal rates for these individuals; they're not the average rates.

PN10961

Do you know that from reading the Rose report, or do you know that from speaking to Prof Rose?---Reading the Rose Report.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10962

Do we take it from the discussion we're having that you accept that Prof Rose is right - sorry - that Prof Borland is right, that in fact the marginal figure is correct,

it's the appropriate one to look at; but you say you can work out the marginal at least from Prof Rose. Is that - - - ?---It is the marginal. Each person has a marginal rate, and what Prof Rose has done is said, "Here's the average distribution of what those marginal rates are.

PN10963

Okay?---Some people have a lower marginal rate, some people have a higher marginal rate.

PN10964

All right?---And there's an average somewhere between the two.

PN10965

I'm suggesting to you, as I think Prof Borland is, that what you still need to see properly to determine labour supply is the margin of the margin, not the - the actual marginal rate, not just the average of the marginal rate?---Sorry, what would be the margin of the margin?

PN10966

Sorry. You need to see the full distribution and work out where that marginal rate is at either end, rather than just be given the average of the marginals?---Well, it's a distribution, and you can see the distributions if you look at Prof Rose's report. Okay. And the point is - - -

PN10967

Can I just stop you there for a moment. I just want to clarify this point before we skip over it. What I'm suggesting to you is those figures do not appear in Prof Rose's report. You might be able to calculate it from - - - ?---Yes, you can. Yes. Sorry.

PN10968

- - - from his standard deviations - - - ?---Yes, that's right. Yes.

PN10969

- - - but they do not appear in the report. Are we agreed on that at least?---That's right. I don't think so. I think you're correct.

PN10970

Can I now ask you to turn to the report you prepared in response to Prof Quiggin. We've had some of this debate before, so I'm sorry to ask you to revisit it, but if you could turn to paragraph 15 on page 7 of that report, and that's where Prof Quiggin is dealing with the range of elasticities. Do you see that? And he says:

PN10971

The summary of the Australian literature is similarly selective.

PN10972

?---I'm terribly sorry, I don't think I'm - - -

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10973

Sorry. Take your time?---I haven't actually got the Quiggin reports. I've got my reply to Quiggin.

PN10974

Yes. Sorry, that's the document I'm asking you to look at?---All right. Sorry. Which paragraph?

PN10975

At page 7 of that report you will see there Prof Quiggin refers to, in the commencement of that paragraph:

PN10976

The summary of the Australian literature is similarly selective.

PN10977

?---Okay, yes.

PN10978

You say there has been no bias in the selection. I just want to make clear that you have - sorry, I think perhaps what I need to do is give you the complete Quiggin Report. If I can hand you a copy of that. I have taken you to his paragraph 15, which now, in the document that I've given you, appears on page 6. Do you have the paragraph?---Which paragraph did you say?

PN10979

Paragraph 15 on page 6?---Yes.

PN10980

Same as the one we were looking at, but we're now looking at it in Prof Borland's [sic] report?---All right. Okay.

PN10981

Got it?---Yes.

PN10982

He's critical because he says the literature review is selective. And he then refers at paragraph 16 to appendix B, which he says:

PN10983

Provides a more extensive, though not exhaustive, survey of the international of Australian literature on minimum wages.

PN10984

Can you go, then, to that. You will need to go to appendix B, which is on page 14. And you will need to jump ahead to page - so that's where the appendix starts. And then on page 19 the Australian studies commence; and then there is some cross-country comparisons starting at page 21. I want to take you to paragraph 26 on page 20 to make sure that you've seen this and you're addressing it in your response. He there says:

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10985

Dixon, Freebairn and Lim, who focused on the effect of changes in standard hours of work estimated what they described as a lower elasticity of minus 0.112 for the period 1969 to 2004. Dixon Freebairn and Lim conclude -

PN10986

then going over the page, 27 -

PN10987

most recent studies have found either negligible effects (Jenenca et al 2000, Ploughman 2007, Lee and Swardy 2011, Olson 2011) or elasticities below minus 0.3 (Mangen and Johnston, Lee, Harding and Harding, Karanasou, Salla). This pattern is broadly consistent with recent international estimates.

PN10988

Had you read all of that when you responded to Prof Quiggin under paragraph 15 in your response?---I'm aware of most of the studies.

PN10989

Do you - I suggest to you that his conclusions about those studies are correct. Do you agree?---I disagree.

PN10990

All right. You still say it's proper to put it in the minus 0.3 to minus 0.8, of which you accepted earlier you are the minus 0.8?---Yes.

PN10991

Because he says, of course, in paragraph 28 that:

PN10992

In sharp contrast to the emerging international consensus, the series of paper by Lewis and various co-authors have maintained the view that elasticity of labour demand is even higher than that commonly found by the studies from the 1980s and earlier.

PN10993

He's putting to you that it's in sharp contrast with the emerging international consensus. Do you not agree to that?---The Lewis and MacDonald study actually reports a lot of the studies that are actually in here, so that's why we've come to the conclusion that we're broadly in agreement with some of those estimates.

PN10994

He is saying that your estimates now are in sharp contrast to the emerging international consensus. Do you agree with that, or disagree?---I disagree with that.

PN10995

Can I take you next, please, to paragraph 20 of Prof Quiggin. Again, I want to make sure that we understand your response. It's there that Prof Quiggin says in his opinion:

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN10996

The effects on penalty rates at aggregate employment in the hospitality industry are limited ... outweighed by other factors.

PN10997

And at subparagraph 1:

PN10998

In general, as shown in appendix A, the effect on employment of legislated or arbitrated minimum wages and conditions is small.

PN10999

I think - is it right to say - you say, if you go down eight lines in your response:

PN11000

The net effect on total employment - the difference between the respective rises and falls in demand for the two groups of workers - may be difficult to detect.

PN11001

So that much - you're agreed to a point. Is that right?---Yes.

PN11002

But your issue is there might be effect on groups?---That's correct.

PN11003

You say there might be a fall in one group but a rise in the other, with a very small net effect on employment?---That's correct.

PN11004

Is that as we should understand things?---Yes.

PN11005

All right. Thank you. 20, subparagraph (2), Prof Borland criticises what it is you say about the decisions made over a week. We've dealt with that in respect of - by our discussions we've had about Prof Borland's comments. I want to ask you about part of your response - sorry. I want to take you to 20, subparagraph (3). Sorry, we have already dealt with this in the context of what we've said about Prof Borland. Your last sentence:

PN11006

However, the high degree of unemployment among the unskilled suggest many would be willing to work for lower rates of pay.

PN11007

That's the same sentence that you accept - - - ?---Yes, that's right.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN11008

- - - the same sentence in your response to Prof Borland, which we've dealt with. I don't need to take you there again. Can I then just deal with 20, subparagraph (4). There's a dispute between you, as I understand it, as to the effect of - if

people don't eat out on Sundays or vice versa, the effect that they might eat out on other days - the effect that other days might act as a substitute. Is that the dispute between you?---I don't think there is a dispute. I think he's backing up my argument.

PN11009

All right. So you're both agreed that if you don't eat out on one particular day, another day may act as a substitute, and you may eat out on the other day?---No.

PN11010

That's what I'm putting to you?---My point is that Sundays and public holidays are very important days for people to eat out, and they don't choose another day if they can't make it on those particular days.

PN11011

I'm suggesting - - - ?---The day of the week is important.

PN11012

I'm suggesting - - - ?---And that's what Prof Quiggin says here.

PN11013

I'm suggesting to you that the position of Prof Quiggin is that the other days will act as substitutes, but they will not be perfect substitutes. Do you agree with that?---They would be pretty poor substitutes if they're closed on Monday.

PN11014

That might mean - all that might mean is that Monday might not be the substitute. But what I'm suggesting to you is that the other days may act as substitutes, but they may not be perfect substitutes. Is that a proposition you agree with, or you - - - ?---It may be, yes.

PN11015

All right. Thank you. Can I then just deal with your response to paragraph 24 and 25. Below paragraph 24 you say:

PN11016

There is little reason to think, with reduced penalty rates, that because family labour is reduced on Sundays and public holidays, that families will increase work during the week. It is more likely the owner and operators will maintain a pattern of work which maintains their business, family wealth, consumption of goods, service, and leisure.

PN11017

I just want to understand this properly. You say if they don't work on Sundays, you don't think there's any reason to think that they will work on another day?---That's right.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN11018

You do say, though, that they will want to maintain their pattern of work which maintains their business, and their family wealth, and their consumption of goods, and their service and leisure?---Yes.

PN11019

Is it fair to say that if the reduction in - if any savings they make from a reduction in penalty rates does not properly compensate them for the loss as a result of them not working, then they won't be able to maintain their level of wealth, as you describe, and that they will then have to work some other days to maintain that wealth level at the pre-existing level?---But the family gets their wealth from the profits of the business, so the profits of the business go up, their wealth will go up. When people become more wealthy they tend to take more leisure.

PN11020

They get their profit from working in the business as well?---I know.

PN11021

And I think your evidence is that they might be the most hard-working because they're entrepreneurs, as you describe it?---That's right.

PN11022

So let's assume that they are the most hard-working of those working in the business. Then what you do by taking them out of Sunday is you take out the most hard-working, and possibly the most efficient member of the operation. Now, in exchange for that you get a saving in penalty rates?---That's right.

PN11023

But what I'm suggesting to you is the loss caused by taking out the most hard-working member of the business will not be offset by the saving you get from the reduction in penalty rate. And I'm suggesting to you if I'm right about that, the over-operator will have to work some of the hours to keep that level of profit up?---It would be very strange business if you were to reduce the costs of inputs, that they would have to start working harder.

PN11024

But you're forgetting in that equation, aren't you, Prof Lewis, that you're not just reducing the labour cost, you're taking out the most hard-working member of the business. You're taking out the owner-operator on Sunday, who you describe - - - ?---The owner-operator and its family, yes.

PN11025

He or she is the one you describe as likely to be the most hard-working; the one with the biggest profit motive and the one with the biggest work ethic. That's the one you're taking out the business. That's going to cause, I'm putting to you, a loss to be made in the business. Let's leave penalty rates to one side, we take that person out for one day, the business will lose, as a result of that person going out and someone else going in their place. Do you agree with that?---It's not an all or nothing decision, for a start - - -

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN11026

I'm not suggesting it is?--- - - they're either going to work or not. Okay. The question is: will they employ more people on a Sunday - all right - or less? And they will make decisions on what level of output maximises their profit. Okay. There's no reason whatsoever why you would think that the family asserts that 50 hours a week is the profit-maximising number of hours and therefore if you reduce the hours on Sunday you're going to have to work more during the week to make up your 50 hours. That isn't a very logical model.

PN11027

But your own evidence is that these owner-operators will maintain a pattern of work and maintain the family wealth. I'm suggesting to you if they want to maintain that family wealth and the business suffers as a result of them not working the Sunday, it is less profitable because they are not working and a casual worker is working in their place?---But I - my point is if they are successful business people, why would they deliberately carry out actions that make the business suffer?

PN11028

Well, I'm not suggesting to you they would?---You did. You said, "The business will suffer, so they will have to work extra hours during the week."

PN11029

That assumption is based on your model that with a reduction of penalty rates the owner-operator will no longer work on the Sunday?---I did not say that at all. There will be less family and owner-operated labour and more hired labour. The fact that - I did not at this stage say the owner will just let the business run itself on a Sunday.

PN11030

But they will work less hours?---They will work less hours.

PN11031

Doesn't the proposition hold equally true?---No.

PN11032

Instead of working eight hours, this most efficient worker is now going to work four; and in their place will be a casual with not the same level of efficiency and/or work ethic?---But they will make decisions on the basis of the cost of hiring a casual; the reduced productivity compared to themselves; and they will make decisions at the margin about how much input they have to put in and how much they want from hired labour.

PN11033

I see. So if - - ?---It's not a matter of, "I work less on a Sunday, therefore I'm now going to work extra hard during the week." There's no logic behind that at all.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR DOWLING

PN11034

I see. So if, in performing that assessment, they say, "Well, although I'm going to make a saving in reduced penalty rates on a Sunday, but if I put a casual in, they

won't be as efficient as me, so the business won't make more money. As a profit-maximising decision I'm going to stay there and work on Sunday." That's open on your scenario?---But it's not a matter of, "I work or I don't work." The point is the owner-operator and their families will do tasks they don't normally do because labour is so expensive.

PN11035

Of course, what I'm getting at, of course, is your proposition that they are the hardest working of the labour?---Yes.

PN11036

So is it fair to say that in making this decision as to whether they will work or not work, that is properly something that they would factor into the equation?---They will decide on the Sunday how much labour they have to put in and how much they have to hire in.

PN11037

And it won't necessarily - depending on how hard they think they work and how hard they think a replacement casual might work - that decision won't necessarily result in them deciding not to work?---But they make that decision every day of the week. They make a decision of: How many hours am I going to put into the business? How many hours are going to hire other people to do jobs in the business?

PN11038

All right. Thank you. Just excuse me one moment. There's nothing further, your Honour. Thank you. Thank you, Prof Lewis.

CROSS-EXAMINATION BY MR MOORE

[12.34 PM]

PN11039

MR MOORE: Prof Lewis, are you aware that between 2010 and 2014, that Sunday penalty rates prescribed by the retail award in New South Wales were increased from time and a half to double time?---No, I'm not familiar with all the history of penalty rates, but I am familiar with that one.

PN11040

So you are aware of that fact, or not aware?---Yes. Yes, I am aware.

PN11041

Was that something you were aware of before you produced your principal report for use in this proceeding?---Yes.

PN11042

Are you aware - and if you're not, I will inform you of this - that in New South Wales over those five years the increase from time and a half to double time was phased in at 10 percentage points a year?---No, I'm not familiar with that.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11043

You weren't familiar with that level of detail. All right. Considering that situation in New South Wales in the retail industry between 2010 and 2014, holding other economic factors constant, caeteris paribus, your analysis and evidence in this proceeding would predict that those increases in penalty rates would result in reduced employment or hours of work for New South Wales retail workers. That's so?---Everything else being held equal, yes.

PN11044

I'm sorry?---Everything else being held equal, yes.

PN11045

So your answer is, "Yes, everything else held equal"?---Yes.

PN11046

Prior to filing your reply statement in this proceeding were you shown a report also filed in this proceeding which was authored by a Ms Serena Yu entitled Evaluating the Impact of Sunday Penalty Rates in the New South Wales Retail Industry?---No, I'm not aware of that.

PN11047

You're not aware of that report?---No.

PN11048

All right. Let me tell you some things about it. Ms Yu evaluates the existence or otherwise of any employment effects in the New South Wales retail industry between 2010 and 2014 during which the Sunday penalty rates were increased in the manner in which I've just described. And she does this by examining - by making comparisons between the New South Wales retail industry and the Victorian retail industry over the same period. And during that period the Victorian - the conditions applicable in the Victorian retail industry remained unchanged at double time. Do you follow? Do you follow so far?---Yes.

PN11049

So we have a - from what I've told you, that sounds as if it is a natural experiment which presents itself as to the impacts, if any, on employment of an increase in penalty rates. One could, in principle, look at comparing the outcomes between New South Wales and Victoria?---You could in principle, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11050

Ms Yu concluded - and her evidence to this Commission will be - that there was no systematic evidence of an (indistinct) following the transitional increases in the Sunday penalty rates between 2010 and 2014, over which time the rate went up from time and a half to double time. That's her conclusion. To tell you a bit more about that before I ask you a question, I will tell you two other things that she concluded in particular. She concluded that taking into account state-specific economic conditions, including total and youth employment conditions and industry demand, the cumulative effect of the five phased increases in New South Wales on both the number of employees in the New South Wales retail industry and on aggregate hours worked in that industry, as measured by ABS data, was

not statistically different from zero. That was one of the conclusions she reached. Do you understand that?---Mm'hm.

PN11051

She also concluded that using HILDA data - you know what HILDA data is, obviously?---Yes.

PN11052

Using HILDA data, which revealed whether persons in the retail industry worked on Sundays - using that data she concluded that the cumulative effect of the increases in Sunday penalty rates on the probability of New South Wales retail workers working on Sundays also was not statistically different from zero. Do you understand that?---Yes.

PN11053

I just want to ask you this question: if you assume that the analysis conducted by Ms Yu is sound; and if you assume that she undertook a relevant and appropriate measure of the employment effects of the increases in penalty rates in New South Wales between 2010 and 2014; do you agree that the conclusion she reached that there was no systematic evidence of an adverse employment effect following those increases; do you agree that that suggests that the relationship between penalty rates and employment is not as you contend for in your evidence to this Commission?---The first question was - I will have to assume her methodology was correct.

PN11054

Yes?---And then if - okay. And secondly it's quite possible that you would detect no effect, because there are such a multitude of factors going on, it's very hard to detect. So I'm saying one of the difficulties with these studies is there are a multitude of things going on at the same time.

PN11055

But if adequate provision is made for the holding of constant of those other effects, do you agree that the conclusion she reached would suggest that the relationship between penalty rates and employment is not as you contend for in your evidence to this Commission?---If it were true that the factors had been taken care of and held constant, which I doubt.

PN11056

So is your answer yes - - -?---If - - -

PN11057

- - - on the assumptions of identified?---If she had, in fact, taken account of all the control variables, then on the basis that evidence - again, assuming the methodology was correct, I would have to agree. I'm saying: however, not knowing the study and not knowing how she controlled a few of the variables, I can't say that she is correct.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11058

So on the assumptions that I've identified, you accept - and I understand that you question those assumptions - but on the assumption is that what she has done is analytically sound, and that the measures she has used are appropriate measures of employment effects of penalty rates - or changes in penalty rates; and assuming that she has adequately held constant other potential effects; you accept, on those conditions, that the results of her analysis would be contrary to your analysis of the employment effects of penalty rates?---On the basis of a huge number of assumptions, and if they were correct, yes.

PN11059

Okay. Thank you. You said at the outset that you were aware of this increase in penalty rates in New South Wales between 2010 and 2014?---I wasn't exactly sure of the exact dates, and I think there are several differences in different states when things did occur - quite a lot of things.

PN11060

But you're aware that penalty rates for Sundays - - -?---Yes.

PN11061

- - -went up in New South Wales for retail workers - - -?---Yes

PN11062

- - - between around 2010 and through to 2014?---Yes.

PN11063

Have you been aware of that for some time?---Yes, a fair amount, yes.

PN11064

And you're aware that that was not the case in all states?---I know that - as I said, I think the amount - the variations in penalty rates over time have been quite different between states.

PN11065

You're aware generally that the making of modern awards meant that in some states Sunday penalty rates went up and they were phased in; and in other states they stayed the same?---Yes.

PN11066

You would agree with me that in principle that circumstance offered up a natural experiment which could, in principle, be investigated or interrogated for the purposes of testing the theories around whether or not penalty rates affect employment?---I think it would make a very interesting experiment.

PN11067

Yes. And it would be a very interesting experiment because it would cast empirical light on this debate around the effects on employment of penalty rates?---I think you would, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11068

And is there any reason why you did not undertake, yourself, to investigate that empirical circumstance - that natural experiment, as I put it?---I have got quite a lengthy research program underway. That would be a potential project, which of course would have to be funded by somebody.

PN11069

All right. Can I just deal with a couple of matters in your report. A very specific matter. If you could go to page 19 of your report, ABI3. Have you got that there?---Sorry, which one am I looking at now?

PN11070

It's your principal report?---Page?

PN11071

19?---Okay.

PN11072

The bottom paragraph should commence:

PN11073

The relevant industries are an important source of employment for students.

PN11074

Do you see that?---Yes.

PN11075

Do you see in the two sentences thereafter you say:

PN11076

Students made up over 45 per cent of those employed retailing.

PN11077

And as I understand it, looking over the page, you've drawn that conclusion from ABS 2011 Census data. Is that right? Am I right in that understanding?---Yes, 2011 Census, yes.

PN11078

My question is this: you don't say, do you, that all of those students - I withdraw that. You don't say that that is a reference to just full-time students, that's anyone who called themselves a student?---Yes, that's right.

PN11079

If you just go to your reply report to Prof Borland. I want to ask you some questions about the substitution effect, which was touched on by Mr Dowling with you. And you - just bear with me - you deal with this at paragraph 28 onwards, which is, of course, Prof Borland's discussion of the substitution effect, and your comments follow thereafter. Now, going back a step, one of the - this is right, isn't it, Prof Lewis - that one of the factors you identify as determining the elasticity of demand for hired labour is the elasticity of substitution between labour and other inputs?---That's correct, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11080

And your simulation in your report posits a high degree of substitution?---I give a whole range of estimates, which include a high one but my personal opinion, based on Australian studies, is that elasticity is high.

PN11081

Yes. I think you say, looking at your reply, just above paragraph 32 of Prof Borland:

PN11082

In my opinion the proposition of a high degree of substitution in the modelling exercise is valid.

PN11083

?---Yes. Yes, that's right.

PN11084

That's your view?---Yes.

PN11085

And the basis for your view that there is a high degree of substitution is based upon the research dealing with changes in junior and youth wages. That's so?---That's one of them, yes.

PN11086

I'm sorry?---Most of the Australian evidence is in terms of junior wages, yes.

PN11087

All of the Australian evidence to which you refer and rely upon in identifying the elasticity for substitution relates to junior and youth wages?---Yes, that's correct.

PN11088

Thank you?---No, it's not - genuine youth - excuse me, youth and adult wages.

PN11089

Yes. Between youth and adult wages and junior wages and adult wages?---That's right.

PN11090

Do you accept that the economic context of the comparison between junior wages and adult wages - or youth wages and adult wages - that the comparison that's there undertaken is quite different from the comparison between penalty rates and ordinary rates of pay?---Substitution is not between - substitution is between hard labour and family and owner-operator labour and capital.

PN11091

I suppose what I'm coming to is this: junior rates are rates which apply to the person of the requisite age at all times at which they work. That's right?---Mm'hm.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11092

And penalty rates, by definition, apply to all employees, but only at particular times. That's right?---That's right.

PN11093

So I would suggest to you that it would be unsound to assume that the elasticities of substitution in relation to comparisons between junior workers and adult workers are applicable in determining the elasticities of substitution in relation to penalty rates?---The point is the elasticity of substitution is basically dependent on - as the name implies - how easy it is to substitute one group of workers for another. And there are - - -

PN11094

Are we talking - I'm sorry?---And there are numerous American studies in particular, but lots of them throughout the world, which show that for the lower the skill of the labourer, the more substitutable they are for other - with other inputs. And I would say that most people would be talking about - in the penalty rates cases here - are going to be relatively low skilled workers.

PN11095

What we're talking about being substituted, though, in the case of junior labour as compared to adult labour, is very different in the case of penalty rates, is it not?---Not really, because the reason why you have substitution of juniors and adults is because juniors are relatively low skilled, and therefore they have to be paid a very low wage, or otherwise they would be substituted for by more highly skilled adult workers. Here obviously we're not talking about juniors and adults, we're talking about hard labour and owner-operator labour.

PN11096

And the substitution with capital as well?---And the substitution with capital, yes.

PN11097

Your model that you simulate in your report doesn't allow for the substitution effect to which Prof Borland refers and which you address. It doesn't allow for the substitution effect to be considered over more than one day. The paradigm is a single day. That's right?---Yes.

PN11098

So by definition, then, within the rubric of your model, the possibility of firms assessing the relative cost of capital and labour and labour and unpaid labour over a week, or a period greater than a day, that's alien to your model?---Alien is a strange word to use, but - - -

PN11099

Well, it's not a - I will use a different word, if you like: that is, that sort of assessment over a week is an assessment that your model is unable to contemplate?---It's not relevant in my opinion.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11100

No. It doesn't fit within your model?---No.

PN11101

Can I suggest to you that while your model might be one which - I withdraw that. Can I suggest to you that that model that you've referred to does not then properly account for how firms might act in the real world as profit maximisers?---No, it describes it perfectly.

PN11102

I'm sorry?---The whole point about the model is - the economic model, which - you may disagree with economics altogether, but in the economic model firm's decisions are made at the margin. As we say, what has gone before has gone before, let bygones be bygones. The only decision you have to make now is on a Saturday morning, are you going to open or not? On Sunday are you going to open? How many people are you going to employ on that day?

PN11103

Can I put this example to you: that in the face of penalty rates on a certain day, when the firm considers the extent of substitution between, let's say, paid and unpaid labour on that day, it would be rational and logical, would it not, for the proprietors to make such decisions in the context of the broader time frame - that is, let us say, over a week?---No.

PN11104

Your model has no scope and does not contemplate that firms might rationally shift their allocation of paid and unpaid labour over the course of the week. That's the case?---No, they won't do that, no.

PN11105

With capital - that is, the rate of - the elasticity of substitution between capital and labour - I think you make your point - the point in your report - your reply report - that capital is fixed in the short term?---That's correct.

PN11106

That's right. And in the long run it's variable?---Yes.

PN11107

But capital is capable, is it not, of being adjusted; that is, the utilisation or the acquiring of capital is something which a firm is capable of adjusting in the medium term, as it were, between the day and the long run?---The definition of the long run is when all the capital is - capital can be varied.

PN11108

I see. A firm might decide on the basis - well, a café or restaurant might decide on the basis of what has occurred in the preceding months, to acquire a new pizza oven?---That's correct, yes.

PN11109

So in your model does that then equate - that month - that scenario I just gave you - is that then equivalent to the long term?---Yes. But - - -

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11110

I see?---Okay, so they acquire the new pizza oven. They still have to decide how many people they're going to employ on a Saturday, Sunday and a public holiday.

PN11111

Yes, I understand that?---Which is the short-run decision. Having acquired the capital, then you have to make the decision about labour to hire.

PN11112

My suggestion to you, though, is that the binary divide between the day and the long run is somewhat misleading in the sense that the long run might in fact be a period of weeks or a month in terms of the actual real life experience of a business?---Of course, it all depends - the difference between the long run and the short run depends on the technology of the firm.

PN11113

Yes?---Okay. If you're a stallholder selling tea on the side of the road, the short run is very short.

PN11114

I see?---Okay. If you've got a very capital-intensive business, like a mine, then it takes a very long time to adjust, so the short run is very long.

PN11115

I see. So insofar as a business is able to adjust its capital allocations within a period of weeks, that would then become the long run?---That's right.

PN11116

I see. So in real terms that means that capital can, in fact, in the context of a business which is able to adjust the balance between labour and capital in a matter of weeks, it could adjust substitute between labour and capital over that period of time?---Possibly.

PN11117

All right. I want to ask you some questions about the scale effect which is dealt with at paragraph 32 of Prof Borland's statement; and in the reply you make some comments about this. The scale effect, just to begin with some basics, is one of the employment effects that can occur due to a change in the wage. That's right?---Sorry?

PN11118

The scale effect is one of the employment effects - - - ?---Yes.

PN11119

- - - that can occur as a result of the change in wage?---Yes.

PN11120

If I can simplify it this way, what it is is the change in the use of labour caused by a change in the use of paid labour - let me put that again. I was trying to simplify it, but let me have a better go at that. It is the change in the use of paid labour which results from a change in output following a wage change?---Yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11121

Thank you. So in the case of a decrease in wage rates, the effect on labour use will be higher, the greater the extent to which the wage cut is passed through as a reduction in costs?---That's correct, yes.

PN11122

And the extent to which the wage cut is passed through to a reduction in costs depends on the competitive structure of the market in question?---That's correct, yes.

PN11123

And your modelling assumes that the markets in question - that is restaurants, cafes, retailing, hair and beauty - are perfectly competitive?---Some of the - well, most - I would suggest that café, restaurants, hairdressing, beauty are competitive; retail is a mixture of highly competitive small firms and oligopolies, large firms like Woolworths and Wesfarmers, things like that, who don't - - -

PN11124

I understand. You refer to that in your reply, but I'm just asking you about your modelling?---Yes.

PN11125

Your simulation assumes a perfectly competitive market structure?---That's right.

PN11126

And under those conditions all of the reduction in wages is passed on as a reduction in the price of the output?---That's right.

PN11127

And in any market structure outside of perfect competition, not all of the cost reduction in the form of a cut in wages will be passed on?---No. There's also monopolistic competition to be passed on.

PN11128

Just to clarify your answer, are you agreeing with me that in any other market structure other than perfect competition, not all of the cost reduction in the form of a cut in wages will be passed on?---No, that's not true.

PN11129

You disagree with that?---All you need is a high degree of competition, not perfectly competitive.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11130

I see. So you say that if the extent of competition may not exactly emulate the conditions for perfect competition; if it's a reasonably close approximate for that, you would see a full pass-through of costs?---There is a form of market structure called monopolistic competition whereby firms are highly competitive, but there's something which distinguishes them from one another; so a cafe, like, for instance, might fall into this. There is something that makes you go to that cafe even though it charges a higher price and somebody else.

PN11131

You don't suggest, though, that in monopolistic competition, as you've described it in your reply, that in that market structure all of the reduction in wages is passed through?---In monopolistic competition price is equal to average cost, and therefore if the average cost. 10 per cent, therefore the price will.

PN11132

My question was different to what you answered. You're not suggesting that in monopolistic competition, as you've referred to in your reply, that all of the reduction in wages, that that cost reduction feeds through - all of that feeds through into a reduction in price?---Yes.

PN11133

You accept, do you, that none of the cafe and restaurant industries, the hair and beauty industry, or the retail industry are perfectly competitive market structures?---As I say, they're probably more easily described as monopolistically competitive.

PN11134

JUSTICE ROSS: Are you likely to be much longer, Mr Moore?

PN11135

MR MOORE: I'm sorry. I just see the time, your Honour. No, about five minutes, I think.

PN11136

JUSTICE ROSS: All right.

PN11137

MR MOORE: The second aspect of the scale effect to which Prof Borland refers is on the demand for output due to a decrease in price from an assumed reduction in price caused by a cut in wages. That's right?---Mm'hm.

PN11138

You accept Prof Borland's point, though, that any increased demand in one industry sector might be offset by a reduction in demand in another industry sector. You accept that?---Partly, yes.

PN11139

So for example, if there was an increase in demand for, let's say, restaurant meals because of a decrease in price due to a cut in wages, that might mean that consumers might buy more meals at the restaurant instead of buying their meals at the supermarket?---Possibly.

PN11140

So that would offset the increase in the restaurants because of the reduction in the retail sector?---There will be partially - - -

PN11141

In part?---Partial, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11142

As you say in your reply, your analysis related only to the specific industries referred to in your report. Your approach means that you're not able to take into account the broader effects across other industry sectors. That's right?---That's correct.

PN11143

There's also a reference to demand shifting. The issue with demand shifting is this, professor: if a reduction in penalty rates means that it's profitable to open on a day previously closed, one factor which will affect the size of the increase in demand for output caused by that is the extent to which consumers who weren't able to buy on that day because a business was closed, let's say, shifted their demand to the same day with another firm, or to the same firm on another day?---Yes.

PN11144

So if a shop opens on a Sunday and had previously been closed, if all of the consumers who now buy from another firm on the Sunday or the same firm on a different day, there would be a zero net effect on employment?---If, in fact, the patterns were exactly the same.

PN11145

Yes?---Yes.

PN11146

You make the point there's little empirical data on demand shifting. I think you refer to that in your reply?---That's correct, yes.

PN11147

You accept, though, that in some industries there would at least be some demand shifting that occurs?---Probably some, yes.

PN11148

But your model assumes no demand shifting?---That's correct. I make that point in the report.

PN11149

Yes. And to the extent that there is any demand shifting, your estimate then of the increased employment caused by reduction in penalty rates that would be an upper bound estimate, would it not?---That's correct, yes.

PN11150

In your reply you say in paragraphs 9 and 14 that your major interest was to show that the employment or demand for labour is responsive to wages. I direct your attention to - in the reply to Prof Borland - following his paragraph 9 in your comments you say:

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11151

Prof Borland seems to miss the point that the review of evidence from a range of studies at the economy level, at the firm level, and internationally, is to support the view that demand for labour is responsive to wages.

PN11152

And you make a similar point following paragraph 14 of Borland where you say:

PN11153

The major interest from the perspective of my report is that it indicates that employment is responsive to wages.

PN11154

That's what the major focus of your report was?---That's right, yes.

PN11155

But your report actually went much further than that, didn't it? Your report - you were sufficiently definitive to conclude that employment is much less than what would be the case if there were no penalty rates?---That's correct.

PN11156

And you also concluded that most businesses would choose, if they could, to employ no hired labour on Sundays or public holidays?---Yes.

PN11157

Are you saying, then, in your reply when you refer to your major interest being - in your report - was to indicate merely that employment is responsive to wages, are you acknowledging that in light of Prof Borland and Prof Quiggin's evidence, that there is in fact considerable uncertainty in the estimates you give?---There is some uncertainty. In fact, that's why I've used a range of estimates. There's no actual - not one number there, there are several.

PN11158

Your claim that most businesses would choose, if they could, to employ no hired labour on Sundays or public holidays, are you suggesting that there's some type of generalised commercial or economic coercion which overbears the will of all those shops and cafes that open up on a Sunday?---Well, there are certain businesses that have to open because they're part of shopping centres, and usually part of the lease arrangement is they have to be open.

PN11159

Put those to one side?---Okay. That's quite a large number.

PN11160

Are you saying that all of the businesses that - - -?---No. Then I say - - -

PN11161

- - - you're not suggesting that?---Then there are - for strategic business - for business strategy reasons they might feel compelled to open.

*** PHILLIP EDWIN THOMAS LEWIS

XXN MR MOORE

PN11162

Business strategy reasons would presumably be strategies which are formulated towards the objective of profit maximising, wouldn't they?---Well, profit maximising is also the same as loss minimising.

PN11163

Is that yes?---Yes.

PN11164

So can I suggest to you that your model is entirely divorced from reality because of the fact that unlike the conclusion you reach, the obvious reality out there in the economy and society is that firms do elect to open on Sundays and public holidays?---A lot don't, though, as well.

PN11165

Do you accept what I say to you, that it's divorced from reality?---No, it's not divorced from reality. I'm saying that they use far too much hired labour than they would - they use far too much family labour, and if they had the choice, they wouldn't open - they must have strategic reasons for staying open.

PN11166

I can tell you this, professor, the three major employer organisations - or three of the major employer organisations in the retail sector; The Australian Retailers Association, the National Retailers Association, and the Master Grocers Association - have submitted to this Commission, on the basis of the evidence they propose to call from actual retailers, that the Commission should conclude that Sunday is an important trading day, and its importance is increasing; that on a sales per hour basis, Sunday is one of the highest trading days; and that between 2010 and 2015 retailers did not reduce - or not significantly reduce the number of hours worked by their employees on Sundays, but instead reduced the hours on other days. Do you agree with me that in light of that submission advanced by reference to the evidence proposed to be called by retailers, that your conclusion that most businesses would choose, if they could, to employ no hired labour on Sundays or public holidays, is simply - bears no resemblance to the reality of the retail workforce - retail industry?---No, because if they could - if they could get by without hired labour on Sunday, they would.

PN11167

JUSTICE ROSS: Thanks, Mr Moore. Is there any further cross-examination for this witness by any other party? No? All right. We will adjourn till 2 pm.

<THE WITNESS WITHDREW [1.13 PM]

LUNCHEON ADJOURNMENT [1.13 PM]

RESUMED [2.03 PM]

<PHILLIP EDWIN THOMAS LEWIS, RECALLED ON FORMER OATH [2.04 PM]

EXAMINATION-IN-CHIEF BY JUSTICE ROSS [2.04 PM]

*** PHILLIP EDWIN THOMAS LEWIS

XN JUSTICE ROSS

PN11168

JUSTICE ROSS: I think we've completed cross-examination. Just before you re-examine there are some questions I want to put to the witness. Professor Lewis, can I take you to your main report prepared for these proceedings, which has been marked as Exhibit ADI3. Do you have that?---Yes.

PN11169

Can I take you to page 17 and the second-last sentence on that page. You see there that "The ACTU has somewhat higher percentages employed in restaurants and cafes, reflecting the relatively high average income population." Is there a relationship, then, between - generally that applies outside the ACT - between the numbers of people employed in restaurants and cafes and the average income of the relevant population?---There seems to be a detailed analysis. It certainly seems to be the case that where you have high average incomes you get more of a demand for the sort of goods, the cafes, restaurants have and, therefore, by head of population, you tend to get a higher employment.

PN11170

So is it sort of the proposition that there's a higher level of disposable income and these are discretionary expenditures and, therefore, they're more likely to make them if they've got more disposable income and away they go?---That's correct.

PN11171

Can I just take you to page 19, just at the last paragraph there, where you say in the second sentence, "Students make up almost 40 per cent of those employed in the hairdressing and beauty services." Then you note that that industry differs somewhat from the other two in that the workers are generally qualified trades persons or apprentices. When you say students make up almost 40 per cent of those employed in hairdressing and beauty, and you'll recall you were asked questions about this, it's really anyone who called themselves - described themselves as a student in the census?---That's right.

PN11172

Does that include apprentices employed - - -?---That's a very good point.

PN11173

- - - in that sector?---That's a very good point. It's the sort of thing I'd have to check on. I'm not sure how it's a question in the census. I think it's usually are you attending any form of - in which case you would. But I'd have to check on that.

PN11174

DEPUTY PRESIDENT ASBURY: Might it also be those school-based trainees and people who do - - -?---Yes, there's all sorts of - - -

PN11175

- - - those training placements in hairdressing?---That's correct, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XN JUSTICE ROSS

PN11176

JUSTICE ROSS: As it turns out, I was going to ask you for - you've got unpublished ABS data from the census, is that right, and that's what the charts in your 11 and 12 are based on?---Yes, that's correct.

PN11177

Would you be able to provide the tables that they're based on?---I could. It would take a little time to get my research assistant to do it, so I'll have to chase them up.

PN11178

There is no particular rush if you could, thank you. I take you to page 26, the last sentence there, "The best estimate suggests that a one per cent increase in youth wages could lead to a decrease in youth employment of between two and five per cent." That's - and all the elasticities for the demand of labour are expressed in real increases aren't they? So that's a one per cent increase in real wages?---That's right, yes.

PN11179

What account is taken of - in calculating those elasticities - of increases in labour productivity?---There isn't any, indeed, it's just assumed to be constant in what are called the production function.

PN11180

So if you had a real wage increase of one per cent and improvement in labour productivity of one per cent what impact would that have, and you've got an assumed elasticity?---Well, it's difficult to understand. In the short run it would actually, of course, reduce labour because you need less labour because they're more productive. But in the long run productivity changes would be passed on in lower prices.

PN11181

Well, you may not need less labour if output increases - - -?---That's what I'm saying, there'd be - - -

PN11182

- - - for the same given amount of labour?--- - - - and it will depend on, and to the extent, to which the output increases in response to the real work, yes.

PN11183

Can I take you to page 28, the first paragraph, the last sentence. You say, "It's highly likely that the inconvenience imposed on customers not being able to purchase goods and services at the time they prefer would reduce demand." I'm just thinking here of a simple example, but wouldn't that depend on the type of service, because if you look at hairdressing as an example, and probably not using myself as the best example of this, but people normally require a haircut at some point, so there would be a demand for services based on that. The fact that that service may not be available on a Sunday, for argument sake, wouldn't necessarily reduce demand because they have to access it at some point?---That's true, yes.

*** PHILLIP EDWIN THOMAS LEWIS

XN JUSTICE ROSS

PN11184

I accept that wouldn't be the case for, say, necessarily, for retail?---It could be that, for instance, in beauty products, nail and things, it would probably - could be postponed.

PN11185

I have got four daughters who might disagree with you but as far as I'm concerned they can be postponed?---Yes, a lot of it would depend - the elasticity demand for any particular day. It would of course depend on the extent to which you can change demand.

PN11186

I will go back to the tables of Table 4A and B, in a moment. Can I take you to page 31 and just the last sentence in the first paragraph there. When you're talking about - this is derived from the tables - when you're talking about the estimated reduction in demand for hire of labour being 80 per cent and 66 per cent you're there talking about on public holidays?---That's right, that's correct, yes.

PN11187

If I go back to the tables, the assumptions you made about the labour demand elasticity, are those range of elasticities, and you've gone through why you've picked those ones, are they based on studies that deal with labour demand elasticity in particular industries, or are they based on studies that deal with aggregate labour demand?---There are very few studies which actually deal with industries, they have to be - the elasticities, what I call the new (indistinct). I mean we've only really got reliable estimates for that for restaurants, because there's confused studies on that, mainly through - because a lot of people do research on tourism, and they find the elasticity of demand for the product to be quite high.

PN11188

For the others they're essentially - what's reflected there is the range in aggregate - the elasticities derived from aggregate studies?---That's correct, yes.

PN11189

You refer on page 31 there, in the third paragraph, the last sentence, you make a reference to the Commission decision to reduce penalty rates for some casual employees in cafes and restaurants. You say at the end, "It is estimated to have had significant positive employment effects." What is that a reference to?---I think the word "estimate" is probably the incorrect use. It probably should have been predicted or predict expected or - - -

PN11190

I see, all right?---Given that modelling.

PN11191

Yes, I see. But you're not there talking about a study?---No, no, unfortunately not.

*** PHILLIP EDWIN THOMAS LEWIS

XN JUSTICE ROSS

PN11192

Can I take you to page 39 and the last sentence on that page, "In a competitive industry most cost savings are eventually passed on to consumers in lower

prices." You say over the page that you think there'd be unambiguously more employment in the industries that we're looking at if turnover increased.

PN11193

So, does the proposition work this way, that a reduction in penalty rates would lower labour costs and those savings would be passed onto consumers in the form of lower prices, the lower prices, or the dropping of prices, would increase demand and it's through the increased demand you get the increase in employment?---That's correct.

PN11194

You recall you were asked questions about the substitution of owner/operators and their families. So, if you've got a circumstance where - we've heard evidence in this case, in the hospitality phase of the case, that there would be some business operators who work at the moment on a Sunday so they would chose to not work on a Sunday and employ a casual or hired labour in the event that the penalty rates were reduced.

PN11195

If you look at that scenario, though, where the owner of the business no longer works - chooses not to work on a Sunday because penalty rates have dropped and they hire someone - the point I am raising is a bit different to the point that's already been put to you - in that scenario, assume no change in opening hours, they're opening at the same times, they're just substituting their labour for hired labour, their costs wouldn't go down wouldn't they? Wouldn't they go up?---It would all depend on the magnitude of the fall, okay, but - - -

PN11196

Sure, but let's assume - my real point is not so much that they'd force them to put prices up but in that sort of scenario - let's assume they work four hours on a Sunday at the moment and they decide I'll employ a casual to do that and I won't, then there's no reduction in labour costs. So what can be passed on in a reduced price?---There will be because - assuming, yes. Currently there's a mixture of hired and family labour, and currently the hired labour costs a lot more than if it were without penalty rates. Now, the employer, when they take their - they're trying to profit maximise, so they take the difference between the costs and the revenue. The only relevant cost is the hired labour cost. So, that goes down per hour, and therefore the cost per unit of production goes up so that more is produced, therefore the cost per unit of output goes down.

PN11197

But that's assuming that they employ any hired labour, and it depends on the magnitude of the fall of the penalty rates?---Yes.

*** PHILLIP EDWIN THOMAS LEWIS

XN JUSTICE ROSS

PN11198

Certainly some witnesses have been cross-examined on the basis of, well, if the claim is adopted and the claims in some instances drop from, say, 175 per cent to 150 per cent on a Sunday, so it's at 25 per cent, and it's been put to witnesses that, well look, that's how much you'd save for that. I think the proposition you've put

to me sort of works if that saving is sufficient to cover the engagement of the additional person. But if it's not then the owner substituting their labour for a casual is not going to save labour costs?---So if the hired labour goes up then obviously there's going to be an increase in costs.

PN11199

Overall costs, yes?---So if the rate comes down there'd be a fall in cost, and therefore the price would be able to be passed onto consumer and there would be greater output.

PN11200

So it depends on the balancing between the two?---Yes, yes. It might mean the family member has to work a bit more perhaps because there's more customers. You can't really tell, all you can say is the mixture of hired and casual labour will change.

PN11201

I think because, as you say, there's no elasticity for that substitution that we - no study that would deal with that. Can I take you to ABI4 which is your response to Professor Quiggin's report, and to page 5 of that report. I think there's also a later reference to a similar proposition and, as you say in reply to that, that your statement isn't in the context in which it appears in paragraph 10 of Professor Quiggin's report, is really that the GFC was a massive shock. Not that wages are unimportant. You'll recall I think it appears later that, it's either Professor Quiggin or Professor Borland, puts the proposition that there are other factors that affect employment in some of these sectors and that they overwhelm the wages cost effect such as demand and the like.

PN11202

Accepting that it depends on, well, what's the wages effect we're talking about, the magnitude of it, but you said during the course of your evidence that demand was an important factor driving employment in the industries that we're talking about. Rather than saying that wages - you say that - you're not saying that wages are unimportant. I'm trying to get a feel for what's the relative importance of these factors, demand for the products that are being produced in, say, restaurants and cafes, as opposed to employment costs?---I suppose that's the sort of thing that would be great to be able find out. You really need a study to find out what we mean by the income elasticity dividend, so that when the national income (indistinct) goes up, what effect - what increase in demand that would be. Then you need to know the price elasticity demand, so when the prices change how it's - then finally you'd need to know what the elasticity substitution. So there's a lot of parameters. I would probably think that it might be a long time before we get the answer to that.

*** PHILLIP EDWIN THOMAS LEWIS

XN JUSTICE ROSS

PN11203

Can I take you to page 11 and I'm looking here at your answer to Professor Quiggin's statement at paragraph 21. This is this issue of the allocation of the week type of proposition, and what you've said about that. Is it legitimate to look at the savings you make on a Sunday, for example, if penalty rates fell? You're

suggesting that you only look at it on the Sunday to make a decision about whether you're going to employ additional labour.

PN11204

In terms of whether or not you're going to reduce prices we decide the sort of Sunday loading that sometimes occurs in some establishments - if you're looking to reduce your prices to consumers in, say, a retail business, don't you look at the percentage fall in labour costs averaged over the week? Because you're looking how much - how much of that saving are you going to pass on? Well then you look at it as a proportion don't you?---Well, again it all depends to what extent there's an extra price on Sunday because it's Sunday.

PN11205

Let's take retail where - I mean certainly accept that in restaurants that's a factor and in other parts of hospitality, for example, hotels and the like, that can be. But let's take retail. You don't often see that we're going to charge you 10 per cent more because it's a Sunday, unless I've never seen that. So, let's assume their prices are constant through the week and there's no loading for the Sunday, and you make a - there's a reduction in penalty rates on Sunday, which means your labour costs go down.

PN11206

But if you're working out whether you're going to pass - how much of that you're going to pass on, or what you were going to pass on in lower prices, don't you take that as a proportion over the week rather than just on the Sunday?---Well, it's an interesting point. When we talk about the price we sort of obviously have to bring everything down to very simple assumptions. But there are what we call price like movements. For instance, you don't offer the best service on a Sunday, so effectively there's an increase in price in the sense the customer has to hang around waiting for a shop assistant - - -

PN11207

There's a different experience on a Sunday?---Yes. That sort of adds to the price in terms of what the consumer has to pay in terms of their own time, because their own time is important, and anecdotal evidence suggests it often occurs on Sundays, you can't get served properly. So, if you like, that is a price effect which only occurs on a Sunday, not in the rest of the week.

PN11208

But if I'm going in to Coles to buy some butter and I'm going to use - which I always seem to have trouble with, but use the automatic checkouts on the way out, my experience isn't going to differ much. Is Coles going to reduce the price of goods because there's a reduction on a Sunday? If they want to do that because they're in a competitive market and margins are relatively low amongst their competitors as well, then, aren't they going to look at the amount they save on the Sunday and average it to see what their overall reduction is?---I think Coles could possibly be the best example because I think they have some arrangement where they don't pay penalty rates for certain work.

*** PHILLIP EDWIN THOMAS LEWIS

XN JUSTICE ROSS

PN11209

Sure, but let's assume they do?---Anyway, let's assume they do. Again what you'd notice is there'd be extra costs on the consumer. So, in my experience anyway on a Sunday, the checkout queues are huge. Again it's totally anecdotal - - -

PN11210

I'm using that automatic one?---You're using the automatic one, but even the automatic ones seem to get bigger queues because there's less staff to help them, and when the change runs out to the EFTPOS thing, so there's costs that go to the consumer on top of the actual mark-up price.

PN11211

Can I take you to page 12 of that document and your response to paragraph 24. I suspect the answer is you're at one end of it and Professor Quiggin is at the other, and there may not be an answer. But you say in the second-last paragraph of your response, "But there is little reason to think, with reduced penalty rates, that because family labour is reduced on Sundays and public holidays that families will increase work during the rest of the week."

PN11212

It's more likely they'll maintain a pattern of work which maintains their business, family wealth, et cetera. There will certainly be instances where the owner/operators are working seven days in event, so there might not be the capacity to increase their labour. But let's assume that if that's not the case, if they take a couple of days off during the week and they work on the weekends to reduce their costs to substitute for hired labour because of penalty rates, and then if penalty rates come down and they employ hired labour why wouldn't they take more hours Monday to Friday?

PN11213

In a profit maximising enterprise why wouldn't they do that? Because their labour is always going to be cheaper than hired labour, it's just a question of how cheaper, how much cheaper?---Family labour.

PN11214

No, the owner/operator. Family labour, that's a different perspective on it?---The owner/operator labour is actually quite costly because it's their own time and they're the ones that run the business, make the profits, et cetera. So actually replacing them is quite expensive. So obviously you need cheaper labour to make that incentive. I can't see a model that would explain why - if you're used to working the week and on the weekend - - -

*** PHILLIP EDWIN THOMAS LEWIS

XN JUSTICE ROSS

PN11215

No, I'm not positing that they - they might work five days a week but they have a day off during the week, then they take the day off on the Sunday because they can, more cheaply, substitute labour, why wouldn't they then work on the other day?---I think it's quite possible the owner/operator might do that, I'm not quite sure the rationale. But we're also talking about family labour which is incredibly important, and I'm not sure what would happen. It's very hard to work out exactly

what would - I can't see a theoretical model that would tell you the answer. But you can see there's intuitive things you can work out. But I'm not quite sure how that would work.

PN11216

Do you know of any data that talks about, in these industries, the amount of owner and family labour and when they work?---We know - we know from ABS statistics the total numbers and they're not particularly high, I forget - depending on the industry, but they're not as high as you would possibly think. Because they don't give you the hours. That's the problem.

PN11217

I see. Okay?---So - and then there's also a reporting problem in that you're classified as employed if you've work for one hour for paid work.

PN11218

Yes?---If you're an employee, even if you didn't actually work, okay? But if you're normally employed, you're still classified as employed. Whereas for a family (indistinct) you have to actually receive money to be classified as employed. So I suspect there might be - I didn't want to do it, I don't want to malign the ABS, but that may be the case.

PN11219

Thank you, Professor?---Thank you.

PN11220

Anything arising?

PN11221

MR DOWLING: No, Your Honour.

PN11222

MR MOORE: No, Your Honour.

RE-EXAMINATION BY MR IZZO

[2.31 PM]

PN11223

MR IZZO: Professor Lewis, you'll recall you were asked some questions by Mr Moore, the second person who cross-examined you, about a report from Dr Yu, and you mentioned you hadn't seen the report but Mr Moore went and told you a bit about the report?---M'mm.

PN11224

He told you about some of the effects of Dr Yu - I think it's Dr Yu, that Dr Yu found in relation to changes in employment since the introduction of modern awards in 2010 and he told you about - sorry, she, no sorry, he told you - - - ?---He.

*** PHILLIP EDWIN THOMAS LEWIS

RXN MR IZZO

PN11225

- - - about comparisons that Dr Yu had made between New South Wales and Victorian - the New South Wales and Victorian experiences, do you recall that?---Yes I do.

PN11226

Mr Moore then said to you that if you assumed that Dr Yu's methodology was correct and you assumed that she had controlled all the variables she needed to control, he put to you that Dr Yu's conclusions might seem to be inconsistent with some of the things that you say in your report, do you recall that?---Yes.

PN11227

In response to that you stated to Mr Moore that there were a multitude of variables that she'd have to control, and you mention that as kind of a qualification to one of the answers that you gave, do you recall that?---Yes I do.

PN11228

Can I ask you to give us just some examples of the types of things that might need to be controlled, that you were referring to?---If you were doing a comparison of New South Wales and Victoria, well, again, one would have to - I'd have to be sure what the industries were in particular because each industry's quite different. Okay. And there would be different demand patterns for different industries, and there might very well be different consumption patterns between Victoria and New South Wales, no disrespect, and there'd be differences in income, and there'd also be differences, for instance, in the age distribution, migration patterns. There's a whole - there's a whole stack of variables that could account for different - differences in consumption and hence employment. As I say, I'm not familiar with the study so I don't know how many of those have been controlled for. But then I say, one of the problems in economics is that there are so many variables, this is why we always argue so much because we always think you should have put that in and you should have put that in. And so, yes, I say, without actually seeing the study I don't know whether she did adequate controls for those variables or not.

PN11229

Thank you. I've got no other questions, Your Honour.

PN11230

JUSTICE ROSS: Nothing further for Professor Lewis? No? Thank you for your - - -?---Thank you.

PN11231

Sorry.

PN11232

MR WHEELAHAN: Can I ask a question, Your Honour? I just want to - - -

PN11233

JUSTICE ROSS: Sure. What role? Are you cross-examining, are you - - -

*** PHILLIP EDWIN THOMAS LEWIS

RXN MR IZZO

PN11234

MR WHEELAHAN: Well I just want to ask, on that last question he gave some examples, but rather than just some examples, if he could, to the best of his knowledge, list what he considers would be the types of variables that he was referring to when he said "The multitude of variables".

PN11235

JUSTICE ROSS: I thought that was what he did do. Is there anything, any other variables that you - -?---Could be more specific, if you like.

PN11236

No, no, well you've mentioned the ones - -?---Output - output of each industry, the mixture of the industries in each - the mixture of the demographics of the states, et cetera. Age patterns.

PN11237

So, for example, if there was over a five year period, there was a change in income between - within a particular state that wasn't replicated in another state, another state had an increase in income, average or per capita income went up, whereas it didn't go up to the same extent in the comparative state, then that's a fact you'd have to control for, is that - -?---Yes. I mean the classic case recently in Western Australia and Tasmania was they're quite different. I mean the other thing is there's been such a huge influx of overseas students into Victoria during that period. Not that I'm suggesting anything illegal, but I'm sure that would have had an effect on the - on the market, labour market for people in the retail sector.

PN11238

I think we'll take that as an additional question and out of fairness, if anyone wants to ask anything that follows from the answer, they can. No? All done? All right. Thank you for your evidence, Professor Lewis, you're excused?---Thank you.

<THE WITNESS WITHDREW

[2.36 PM]

PN11239

MR DOWLING: Thank you, Your Honour. I call Professor Quiggin.

PN11240

THE ASSOCIATE: Please state your full name and address for the Commission.

PN11241

MR QUIGGIN: John Charles Quiggin, (address supplied).

<JOHN CHARLES QUIGGIN, AFFIRMED

[2.38 PM]

EXAMINATION-IN-CHIEF BY MR DOWLING

[2.38 PM]

PN11242

WITNESS: Should I have some documents? No, documents?

*** JOHN CHARLES QUIGGIN

XN MR DOWLING

PN11243

MR DOWLING: We'll provide you with some documents in a moment, Professor Quiggin?---I see. Sorry.

PN11244

Can I ask you to repeat your full name, firstly?---John Charles Quiggin.

PN11245

Your occupation?---Economist.

PN11246

Address?---(Address supplied).

PN11247

Thank you. Now you have prepared a report for the purposes of this proceeding?---That's correct.

PN11248

I'm going to hand you a folder of documents?---Thank you.

PN11249

Can I ask you to turn to Tab 3 in that folder?---Yes.

PN11250

Is that a report prepared by you?---Yes.

PN11251

Is it correct that that report, as it was filed, also attached your curriculum vitae?---Yes.

PN11252

Does that report accurately set out the opinions formed by you based on your expertise?---Yes.

PN11253

I tender that, Your Honour.

EXHIBIT #UV24 Report by Professor Quiggin.

PN11254

MR DOWLING: Now that report was prepared by you in response to a report prepared by Professor Lewis, is that correct?---Yes.

PN11255

If you look behind Tab 1 of that folder, is that the report prepared by Professor Lewis to which you responded?---Yes.

PN11256

MR DOWLING: Is that the report prepared by Professor Lewis to which you responded?---Yes.

*** JOHN CHARLES QUIGGIN

XN MR DOWLING

PN11257

Now there is one other document in that folder, if I could ask you to look at it. You are aware that Professor Lewis has prepared a report replying to your report?---I am, yes.

PN11258

If you go to Tab 4 in that folder. Is that what you know to be the report prepared by Professor Lewis in response to your report?---Yes.

PN11259

Thank you. Your Honour, with leave, what I would like to do is take Professor Quiggin to seven matters raised in reply by Professor Lewis. They are each matters that I put to Professor Lewis, Professor Quiggin's position, and in my submission they simply complete the dialogue or the exchange between these two experts that's arisen as a result of the report, the reply report and the reply to it.

PN11260

JUSTICE ROSS: Any objection?

PN11261

MR IZZO: No objection, Your Honour.

PN11262

JUSTICE ROSS: All right.

PN11263

MR DOWLING: Now, if you can have open in front of you, then, Professor Quiggin, Professor Lewis' reply to you, which was the report behind Tab 4?---Yes.

PN11264

If I can ask you, please, to turn to paragraph 15 which appears on page 7. That's the paragraph that begins, "The summary of the Australian literature is similarly selective", do you see that?---I do, yes.

PN11265

Have you seen the response below it?---I have.

*** JOHN CHARLES QUIGGIN

XN MR DOWLING

PN11266

Can you say to the Commission what you say in reply to that response?---Yes. This response is both incorrect and, in my view, unresponsive. So if I could refer you to Appendix B in my report, page 20 and 21, numbered paragraphs 26 and 27 here. In those paragraphs I list nearly a dozen Australian studies of the elasticity of demand for labour. All of them give elasticities lower than the range asserted by Professor Lewis to be the range of all studies he's - he's looked at. So it seems to me the claim is incorrect. It's unresponsive in the sense that he gives no reason why the reports by eminent Australian columnists should be disregarded, what's wrong with any of those reports. Also doesn't respond to the explanation given in Appendix B, looking at the US case, why views of the elasticity of demand have declined over time, and of course, having said that, he asserts broadly that these

results are similar to other studies but doesn't add to the selection of his own studies, which are essentially the only evidence, with one exception, that he cites in his original report.

PN11267

Thank you. Could I ask you next to turn to, in the same document, paragraph 20. This paragraph is divided into four parts. There's 20(1) where he says, "In general, as shown in Appendix A, the effect on employment of legislated or arbitrated minimum wages and conditions is small." Do you see that?---I do, yes.

PN11268

Have you read the response set out by Professor Lewis?---I have.

PN11269

What do you say to that response?---I want to foreshadow the point that in my view his comments on the elasticity of substitution between hired and non-hired labour are excessive, but in this point what I'd like to refer to is that he can concede that the aggregate effects on employment are small, but makes a great deal of this question of whether hired labour is substituted for self-employment, the employment of operators. Now, in both economic terms and in terms of the objectives of the modern award system, I can't see that this is a matter of any relevance. The relevant objective, it seems to me, is the increase in labour force participation. There's nothing in the objectives of the Act or in the economic analysis underlying it that suggests that we should have a preference for encouraging hired labour at the expense of owner-operator labour, or the other way round. These are both perfectly valid forms of employment. There's no reason, conceded as it is, that the effect on total employment is small, why we should care particularly as to whether the employment takes the form of more hired labour and less operator labour or vice-versa.

PN11270

Thank you. Could you go to the second sub-paragraph in that same paragraph, where you say, "The effect of penalty rates is to increase modestly the average wage rate of employees over a full week." Again, have you seen the response that is there set out?---I have.

*** JOHN CHARLES QUIGGIN

XN MR DOWLING

PN11271

What do you say in reply to that response?---Well again there is no contest of the substantive point. So instead what's offered is, in my view, an incorrect piece of economic analysis suggesting that, to read the sentence, "A firm decision of how many hours to operate, whether open at all, how many workers to employ et cetera on a Sunday or public holiday are independent of what has already occurred during the rest of the week." Now that's simply an error in both economics and common sense, so in economics we're failing to distinguish between fixed costs and marginal costs, there are a set of costs associated with operating any business, including a restaurant, that arise simply by having the restaurant, and there are another set of costs that are the extra costs associated with opening up on a given day. So for example if you have a restaurant with 20 seats, obviously you can't supply 50 seats on a Sunday. Equally, it's very difficult to, say, rope off much of

the restaurant and say, "I'm only going to serve three tables on a Sunday"; the restaurant is set up to work in a way that depends precisely on what's happened on the other days of the week, exactly contrary to what's asserted here.

PN11272

Thank you. Can you next turn to the third sub-paragraph, the paragraph that begins, "Penalty rates represent compensation for working at times which are generally regarded as unsocial", and goes on. Have you seen and read the reply to meet that paragraph?---I have.

PN11273

What do you say in response to it?---Well the first sentence, I think, confirms, as has been previously. The first sentence doesn't contest the points made in substance. The second point isn't an observation at all about penalty rates but rather a general observation about the labour market, suggesting that late conditions are preventing expansion in employment from the - from the unskilled and youth. That, of course, is the claim about minimum wages which in other parts of his report, and particularly in his response to me, Professor Lewis has disavowed. So he's repeatedly backed away from any suggestion that minimum wage is a major cause of unemployment, but in this - in this throw-away sentence he essentially repeats that claim.

PN11274

Thank you. Lastly with respect to this paragraph is the sub-paragraph 4 that begins, "The primary avenue by which employment in the industry might be increased", do you see that paragraph?---I do.

PN11275

Have you read the response to it?---I have.

PN11276

What do you say in reply to that?---Well this is a mis-characterisation of notional substitution. So in general in economics we see closely-related goods or when goods to production have substitutes, that is if the price of one goes up he will substitute the other. Now there are two extreme cases. One is where they're perfect substitutes so you simply buy whichever is cheapest, and the other is where they're not substitutes at all, so that you have a fixed demand for one and you don't shift the other no matter what the price. Essentially Professor Lewis admits only those two possibilities and rejects the idea that if restaurant meals on Sunday become a little cheaper or a little dearer, that people will shift their pattern of demand; if Sunday meals are cheaper they'll eat more on Sunday and less on other days, if they're dearer they'll eat less on Sundays and more on other days. Professor Lewis only admits the two possibilities; either people don't care what day they eat on, or they won't change anything in response to - in response to prices. Neither of those two extreme cases are realistic.

*** JOHN CHARLES QUIGGIN

XN MR DOWLING

PN11277

Thank you. Now two last paragraphs. If I can ask you to turn to paragraph 24, please, which appears at page 12 of this document. You'll see there that is your

paragraph that reads, "There are several major problems with Professor Lewis' analysis", do you see that paragraph?---I do.

PN11278

Have you read the response he there sets out?---I have.

What do you say in reply to it?---Well first I think the same confusions about substitution are - are apparent here, as I mentioned in the previous paragraph, though now of course we're talking about inputs to production rather than - that is labour, rather than - rather than the consumption side. But second, I'd draw your attention to the final two sentences which are in direct contradiction with his other. So the second-last sentence says, "There is little reason to think that with reduced penalty rates it will increase on other days of the week", the immediately following sentence says, "It is more likely that operators and family will maintain a pattern of work which maintains their business, family wealth, consumption of goods, service and leisure." Now fairly obviously, if you reduce your work on Sunday and you want to maintain your level of leisure constant, you must increase it on other days. Similarly, if you reduce your income on Sundays by not working and paying somebody else to work, if you want to maintain your income, you must find a saving somewhere else, most obviously by doing more work on - on other days of the week. So the second - the final sentence, I think, is broadly correct, that broadly speaking we would expect to see, if penalty rates were reduced, that operators would work less on Sundays and more on other days, thereby maintaining, as the final sentence says, their current levels of wealth, consumption and leisure. So that sentence seems to be broadly correct, the previous sentence is in direct contradiction.

PN11279

The very last paragraph I want to take you to is paragraph 26. That is your paragraph that commences, "A further problem with the analysis presented by Professor Lewis is his assumption that employment of hired labour rather than total labour should be a primary concern." Have you read the response to that paragraph?---I have.

*** JOHN CHARLES QUIGGIN

XN MR DOWLING

PN11280

What do you say in reply to it?---Well first, as regard to the normative judgments, implicitly in the whole report it's normatively claimed that - that this effect of substituting hired labour for - substituting between hired labour and family labour is of great importance. If he doesn't want to make a normative judgment then the question of where the substitution takes place seems to me to be unimportant, and indeed that's my view. Secondly, I guess, there's - there seems to be a contradiction in the - in his reliance on the quoted paragraph which implies that weekend work is burdensome and that - and that operators - owner/operators would be glad to be free of it, are with the general tenor of, particularly his original report, which suggests that people don't really care about weekends at all, that the only reason that we had penalty rates was because people wanted to go to church and that now they don't they shouldn't care. So it seems that, you know, this report cites perfectly justified sensitivity to the wishes of owner/operators to have their weekends free, but - but that contradicts, as far as I can see, the whole

tenor of the rest of the report which suggests that hired workers shouldn't care about this.

PN11281

Thank you very much, Professor Quiggin. If you just wait there?---Thanks.

CROSS-EXAMINATION BY MR IZZO

[2.52 PM]

PN11282

MR IZZO: Professor Quiggin, if I could just make a request just as a preliminary matter. I had a little bit of difficulty hearing you earlier in some of your answers, so if you wouldn't mind speaking - - -?---Sure.

PN11283

- - - up, that would be greatly appreciated. I take it you have a copy of your report, Professor Quiggin, with you?---I do.

PN11284

I can't recall which tab it is but - - -?---Yes.

PN11285

- - - you've got it open. If I can take you to page 6 of - - -?---Excuse me.

PN11286

- - - of that report, Professor?---Yes.

PN11287

Paragraph 17. The last line of paragraph 17 you talk about the mainstream view in relation to the impact of minimum wages, do you see that?---I do.

PN11288

Do you accept that the many economists who you call mainstream, to borrow your term, considered that minimum wages do have some impact on labour demand?---I think the summary I presented is an accurate statement. The effect is small, some mainstream studies have found no impact

PN11289

Can I ask you that your view, or one of your main criticisms of Professor Lewis is that you say that rather than there being no impact on labour demand, it's more that he's overstated what the impact is?---I certainly take the view that he's overstated demand. As I say, the mainstream view, the dominant view is of a small impact. The - there's a substantial number of studies finding no impact at all. That's true of the US literature and also of the Australian literature I cite.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11290

When you talk about no impact, do you agree that if minimum wages aren't set at what the literature refers to as an appropriate level or a moderate level, then there will be impact and indeed that impact might be substantive?---Could I maybe ask you to spell out the relevance of this? I mean, Professor Lewis has suggested that

minimum wages aren't a critical consideration here and we're not talking about a change in minimum wages in the case. I mean - - -

PN11291

If there's a - - -

PN11292

JUSTICE ROSS: Professor Quiggin, if you just answer the questions?---Sure. Okay.

PN11293

If there's an objection on relevance it will be taken?---Yes. So certainly there is a level of minimum wages, there must be conceptually, at which they have a substantial impact. The evidence from the studies we're looking at suggest that minimum wages at the level they prevail are very clearly in the US and I think the preponderance of evidence for Australia is that the effect is small.

PN11294

MR IZZO: Accept that, but what I'm focusing on is that if the level of the minimum wage is not set at what the literature refers to as an appropriate level or a moderate level, then the impact might not be small it might be substantive?---It might be. The - the point is, of course, the empirical evidence is based on the actual setting of minimum wages so that it doesn't - obviously you can't project that out of the range of the data, so it's certainly possibly, hypothetically, that if wages were set at very different levels we'd get different numbers.

PN11295

Do you accept that the higher the increase to a minimum wage, the greater the potential for that to have an impact on employment?---Within a range, given the initial level, I would expect the effect to be broadly linear. That is, if we start with a given minimum wage I would expect the effects of a 10 per cent increase on minimum wage to be roughly twice the effect of a five per cent increase in minimum wage. If what you're referring to is a level of minimum wage that is well away from the current level, of course you might have different effects.

PN11296

Thank you. And, I apologise, one other request I might make. You are speaking quite quickly - - -?---Sorry. Yes I - - -

PN11297

- - - if you don't mind just slowing down so I can - - -?---Yes, okay. Sure.

PN11298

You don't have to go super-slowly, just a little bit slow, if you don't mind?---No.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11299

Now you talked about increases in minimum wages having, potentially, a small effect. Do you accept that if there is an increase in the minimum wage, to some extent rather than jobs being lost, it's possible that there's a substitution between

different types of hired labour, and I'll give you an example to illustrate what I mean. So if the minimum wage in this country was to go from - - -

PN11300

MR DOWLING: Sorry, Your Honour, I'm really not sure of the relevance of this question. This isn't a minimum wage case. Professor Lewis - - -

PN11301

JUSTICE ROSS: The substitution was a point that was addressed in Professor Lewis' evidence as well, between minimum wage and those above.

PN11302

MR DOWLING: Yes.

PN11303

JUSTICE ROSS: So - - -

PN11304

MR DOWLING: Thank you, Your Honour.

PN11305

MR IZZO: So I'll start the question again - - -?---Sure. yes.

PN11306

- - - and I'll go into the explanation. So what I wanted to ask you about is, if there's an increase in the minimum wages, is it true that to some extent, rather than jobs being lost there might be a substitution or there will be some substitution between different types of hired labour? And I was going to go on and explain what I'm referring to. So the minimum wage in this country approximates to around the \$17 mark, I can't recall the exact figure. If that was to be raised to \$20, rather than an employer in some cases simply not engaging a particular employee or class of employees, they may instead choose to employ someone at, say, \$23 with higher skills instead of that base level worker at 20 because they view that for a small increase they can get someone with higher skills than someone at the \$20 mark, and so what's happened is that the person on the minimum wage may have lost their job but that job's gone to someone with some more skills. Do you accept that that is the type of thing that might occur when there is an increase to the minimum wage?---It can occur. It depends on the nature of - of the work process. Whether - whether it's organised in such a way that there's a substantial return to skilled workers.

PN11307

If that does occur, instead of there being a nett effect on employment all that would have happened is a lower paid job's gone to a higher paid, and we don't have a total impact, would be your position?---That's correct. If all that happened was we had different workers being employed, then there's no nett impact on the total level of employment.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11308

Thank you. Now at paragraph 20 of your report, which is on page 7?---M'mm.

PN11309

At sub-paragraph 4 you talk about what might happen if penalty rates were lowered and you say that, "Even if there is greater expenditure on Sundays, such expenditure would come at the expense of other days of the week." Do you see that?---I do.

PN11310

So do I take it that you assume in your critique of Professor Lewis' report that the demand for restaurant services can be substituted across other days of the week?---Yes.

PN11311

So that assumes that if someone can't go out on a Sunday because the restaurant's closed, then they'll go out on a week day instead?---That's certainly - if they're closed or if it's more expensive, they are substitutes, that's correct.

PN11312

In forming that view and expressing it at paragraph 24, you don't actually cite any studies or empirical data to support that view, that's simply just an opinion you've put, is that right?---I think the - the existence of close substitution between closely related goods is such a standard point in economics I don't think - I find it hard to believe, for example, that anybody would be able to publish a journal article explaining that restaurant articles - restaurant meals on one day are a close substitute for restaurant meals on another. This is - the data isn't sufficient to drive such an estimate, but it's such an obvious proposition that I can't imagine that you would ever find any - anybody doing a (indistinct) study of it.

PN11313

When you talk about the fact that there's substitution between close - I can't recall the correct phrase you mentioned, but similar goods or - - -?---Yes.

PN11314

- - - closely related items. That's a general economic proposition, that's not necessarily an established proposition with respect to the restaurant meals itself?---Well I think it's essentially impossible in the nature of the data, I think, to - to ever - you know, to ever get down to such a level. It's assumed in most of the studies, in fact, that these are pretty much perfect substitutes in the way that these models are constructed, simply because there isn't sufficiently fine-grain data to possibly tell how you would ever estimate whether meals on a Wednesday will substitute for meals on Thursday. I can't imagine a study that will establish that fact. I also can't imagine an economist who would question it.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11315

Well I think there is an economist who questions it, for instance Professor Lewis is one that you've read who questions that fact?---In my belief Professor Lewis' report exhibits some confusion on the subject without denying it. He essentially, as I said in my reply in my evidence, suggests only the two possibilities of perfect substitution and no substitution gives reasons why you might not expect perfect substitution and jumps to no substitution. I don't believe that he has, and his

report certainly doesn't show, any study suggesting that there is no substitution relationship. I think he - he simply makes an analyst variable.

PN11316

I appreciate that. So your position is that, then, you're not aware of any studies to support the opinion or the assumption you make in 20(4) - - -?---Um - - -

PN11317

- - - about substitution with respect to the restaurant meals across days of the week?---I am certainly prepared to give my expert opinion that this is a proposition that no economist would question.

PN11318

That no economist?---Would question. This is - - -

PN11319

But that wasn't my question. My question is that there are no studies to support that or no empirical data that you can refer to - - -?---There are no studies either to support it or oppose it, and as I've said, I think there's no conceivable study based on the available - based on the evidence available to Australian economists which could possibly test this proposition.

PN11320

Now you say in that same paragraph that many establishments close on Mondays. Do you see that?---I do.

PN11321

You don't proffer a view as to why they close, and it may be that it's because you don't know, is that the case?---It's because, unlike the previous point, I have a view on the subject but it's not one on which I'm an expert. My view is that it's a matter of industry custom to which consumers have adapted rather than a response to an inherent preference of consumers to eat at home on Mondays.

PN11322

So your position is not that there's less demand on a Monday - - -?---My position - - -

PN11323

- - - for restaurant meals?---My view, which I add is not what - since I haven't put it forward, is not an expert one, is that the absence of demand on Monday is a consumer adaptation to industry practice of closing on Mondays rather than something inherent in the pattern of peoples' lives that leads them to want to go out on Tuesdays rather than Mondays. But I don't - I'm not aware of any - I'm only speculating there, I'm not giving an expert opinion.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11324

Basing your views on - or having made those comments about Mondays, you then go on to say that penalty rates aren't the primary reason for determining opening hours because you say, "Restaurants are shut on Monday therefore penalty rates

can't be the reason that impact upon operator decisions to shut or open"?---That's certainly evidence in that direction, yes.

PN11325

But in making that general opinion you are relying, are you not, on assuming that the reasons that restaurants don't open on Mondays are the same as the reasons that they might not open on a Sunday or a public holiday? It's the same factors motivating them?---Certainly this factor is present in both cases and the dominant factor would work in the same way in both cases.

PN11326

Sorry, you say "This factor is"?---Yes. The prevalence of penalty rates is a factor in one case and not in the other. If it was a - if it was a major factor determining - determining closing hours we wouldn't expect to see this big impact on Monday.

PN11327

What you've done is sought to extrapolate the reasons for why operators open or shut on Mondays and assume that that applies to the rest of the week, haven't you?---I've assumed that whatever factors make - determine their operating decisions are really constant through the week, yes.

PN11328

And you accept that penalty rates don't operate on Mondays other than perhaps for late night shifts?---That's correct. Which are also applicable on other week days.

PN11329

Sorry, I apologise?---Which are also applicable on other week days.

PN11330

The late night - - -?---Yes.

PN11331

- - - shifts?---Yes.

PN11332

Well I put it to you, Professor, that the factors associated with closing on Monday are not as a result of industry custom but are a direct response to customer demand. Would you agree or disagree with that proposition?---I don't think that's testable. I've given my - my view and I don't think anyone's studied it.

PN11333

And for that reason Monday is not a good substitute for restaurant meals on, say, Saturdays or Sundays or public holidays, for that matter?---It certainly isn't a perfect substitute. I think it's - my view is that it seems like a reasonably good substitute for meals on other week days.

PN11334

If we break the process down a little further, do you accept - sorry, I withdraw that. When we talk about restaurant meals we're generally talking about breakfast, lunch or dinner, I take it, do you accept that?---That's correct, yes.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11335

There may be some fourth category where - all day dining, but we might put that to the side for one moment?---Yes.

PN11336

If I can take lunch, do you accept that lunch on a Sunday or a public holiday can easily be substituted with a lunch in a restaurant on a Monday?---Well lunch on different days are substitutes. That's - it can be substituted, they're substitute meals, but the degree of substitution is probably greater for dinner than for lunch.

PN11337

Sorry?---The degree of substitution is probably greater for dinners than for lunch, but I - again, of course, this - these detailed fine-grain distinctions essentially are almost impossible to test with regard to that.

PN11338

At paragraph 21 you talk about the reduction sought in penalty rates at the beginning of the paragraph and then towards the last line on the page you come to a conclusion that, "The proposed cut by the employer parties will reduce the average wage by around 2.6 per cent", do you see that?---I do.

PN11339

Now, I take it that's the proposed cut in relation to the restaurant industry?---That's correct.

PN11340

In coming to that view you've averaged, I take it, the reduction in labour costs on a Sunday across the value of labour costs for the whole week to work out what the value of the reduction is in terms of a percentage of total labour costs?---That's correct.

PN11341

Then you go on to say, at paragraph 22, that you accordingly believe that the reduction in penalty rates will not have a substantial impact on employers offering longer hours as well?---That's correct.

PN11342

So inherent in your analysis is an assumption that the restaurants will assess the viability of their operating hours on an aggregate basis over a whole week?---That's correct.

PN11343

You don't cite any studies or data to support your assumption that that's how a restaurant operator or operators would assess operating hours, that's just your opinion that you've posited?---Can you clarify the question? Which hours are you referring to here?

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11344

Certainly. So I'd asked you just before that you assumed that restaurants assess the viability of the operating hours on an aggregate basis over a whole week, and

you'd agreed with me that you had adopted that assumption. My question to you is, or my statement that I put to you and I'd like to have your response to, is that you haven't cited any studies or data to support that the assumption that you made about assessing operating hours over - on aggregate basis over a whole week is how restaurant operators actually assess the viability of opening on particular days?---Well again, as with all these questions, to get data differentially by day on how - how firms make their employment decisions would require incredibly detailed studies and also actual variations of the kind tested - of a kind being tested here, simply don't exist. I think it's - the standard approach which any economist would take in assessing a change in costs, I think, would be to take it as the average change in costs and apply an estimate of an elasticity to get a very small number. I'd make the further point, of course, numbers are - are so small that even if - even if, for some reason, employers were more cost sensitive on Sundays than on other days, we would still end up with a very small number.

PN11345

When you talk about the complexity involved in trying to find out the answer to some - trying to find out someone's data, we're simply talking about how employers assess the viability of operating. Wouldn't a survey of a random sample of - a representative random sample of employers about how they assess their operations or how they look at their labour costs could be something that could give us an answer to that question?---Are you suggesting an opinion survey or - - -

PN11346

Well not necessarily an opinion survey, it would more be a survey of what they do in practice?---So you'd want their operating hours recorded for each day, the number of staff they employed on a daily basis, evidence on - evidence showing - giving some variation so that we would look at employers facing different costs on different days, and then a statistical study responding - taking days which showed variation across the days and showing how the daily operating hours responded to the - responded to the differential prices the employers were facing.

PN11347

If I can ask you this, Professor Quiggin. In relation to your analysis at paragraph 22 - sorry, I withdraw that. The analysis and conclusions that are set out at paragraph 22, they would not be valid, would they, for those restaurant operators who assessed the viability of opening on a day-to-day basis as opposed to as upon an aggregate over the week?---Well of course as I explained in my evidence, that would be an irrational thing to do. A large portion of your costs are fixed so that if you - if you simply ignored your fixed costs and disregarded all the decisions you'd made during the week as regard to the size of your restaurant, the nature of the menu and so forth and simply start on a Sunday and said, "Will I open today or not?" as if you had not made those previous decisions, you would certainly be out of business fairly quickly.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11348

I accept that you don't - that your opinion is that they wouldn't assess their business that way or assess operating - - -?---I don't think that's a matter of opinion. This is - - -

PN11349

Well what I'm putting to you is that for those operators who do - if you assume for the moment that there are operators who do assess the viability of ability of opening on a day-to-day basis, when it comes to how they allocate their labour, that the conclusions that you have set out in paragraph 22 would not be applicable to those types of operators?---I reject that assumption. I don't believe such operators exist and somebody attempting to operate in that business, they'll go out of business very fast.

PN11350

Thank you. You talked about fixed costs I think briefly in one of your answers just previously. My understanding is that capital, for instance, is a type of cost that is a fixed cost that is, you made an investment in capital and then that cost is somewhat difficult to change and hence is fixed in nature?---That's correct.

PN11351

Whereas labour costs is something that is variable?---Labour costs are variable typically, yes. Not completely variable in the way you might suppose but certainly more so than capital.

PN11352

Right. Having made an investment in capital, let's take a restaurant. Someone has their lease, they buy the tables and chairs, it's fit out, the investment is made in the capital. That's now fixed. In terms of what an operator can then do to respond to variations in demand, to attempt to reduce costs and increase profitability, it's much easier for them to adjust their variable costs than to adjust their fixed costs, isn't it?---I point out the primary margin of adjustment here is going to be in - in those capital investment decisions in the first place. So this is - the relevance of this calculation is that over the long run if the costs of running restaurants increases, then you'll see less restaurants establish and of course consumer demand will go in other areas, so the relevant calculation in the medium term is the total number of - is the total costs and the effect of a decision on total costs. The - the effect in the week after a decision is made might be different but the primary - the primary and relevant calculation is the one I've made here, which is the impact on the total cost of operation.

PN11353

And if I'm - and I take it you would agree with this, that if I'm setting up a business from scratch tomorrow - - -?---M'mm.

PN11354

- - - then certainly I'm going to look at capital and whether it's repayments, all those things that need to be made over a long term basis, I'm going to assess that against the variable costs before I set up and I'm going to make a decision, presumably on an aggregate basis before setting up?---Absolutely. Yes.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11355

But if I'm not setting up and I'm an existing operator, then my ability to make such assessment and respond to variations in demand by adjusting capital and other types of fixed cost is much more limited, isn't it?---If I can refer you to, I think it's Appendix A of my - sorry, I just need to find the location. It gives - it gives data on exits and entries for the industry and what it shows is that the - the rate of turnover in the industry is very large. I'm just trying to - I'll see if I can locate the
- - -

PN11356

JUSTICE ROSS: I think that's page 13 of your report?---Yes, that's correct. Page 13 is the - - -

PN11357

MR IZZO: Sorry, so you were saying the turnover is large?---Yes. So the two year survival rate is 55 per cent shown here, so that - that suggests that while there might be an effect in the very short term, when we can assume that the set of restaurants was - was fixed, the normal entry and exit unrelated to any decision of this kind is so large that we can reasonably take it that the primary margin of adjustment will be the aggregate - in response to aggregate costs, not - that is the relevant calculation when we want to look at the aggregate effect on employment.

PN11358

Yes, and I'm not sure, though, that directly answers the question. The question was if I am an existing operator, though, and I appreciate we've discussed about people who are about to set up. If I'm an existing operator, my ability, if I need to respond to changes in demand or revenue, my ability to respond by making total aggregate cost adjustments is much more limited than someone setting up?---It's true. That - that adjustment is primarily on the entry margin. So what we'd expect to see is precisely that the primary margin adjustment, because of the large role of fixed costs, will be on entry and exit, but that, as I've pointed out, that impact will be very small indeed.

PN11359

Thank you. Now you agreed with me earlier that one of the factors that mitigates against minimum wages creating a dis-employment effect is a level of substitution between hired labour, do you recall that discussion that we had?---Could you restate the question? I'm - - -

PN11360

Yes, certainly. You agreed earlier that one of the factors that might prevent minimum wages - sorry, minimum wage increases from having a dis-employment effect is a level of substitution between hired labour. We talked about - - -?---No, I think - to clarify, I said the effect was small and I agreed that we might see substitution effects which would have no nett effect. I haven't - I haven't immediately got a view on whether the existence of the substitution effects reduces - how that affects the aggregate effect, merely that any particular instance of substitution has no - no effect.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11361

Can I ask you this. In the case of penalty rates, if a penalty rate is to be imposed on employees on a Sunday, let's say?---Yes.

PN11362

That type of phenomenon of substitution between hired labour, that is from a low paid worker to a slightly higher paid worker, would not be as likely as is the case with an increase in minimum wages, and I might just give you an example to explain - - -?---Sure.

PN11363

- - - before I get you to respond. So, for example, I talked before about the employee on \$17, he or she goes up to \$20 and we talked about a potential substitution where the employer elects not to pay an employee - a low skilled employee at the \$20 minimum rate but instead chooses to pay a small amount higher to get someone who's more skilled, and if we adopt that example here with the penalty rate, we've got an employee on \$20 and \$23. If there's a penalty rate applicable to both then both of their rates will go up 100 per cent, 150 per cent, whatever the case may be, and in those circumstances the likelihood of a substitution occurring between the two is less?---I'm not closely familiar with the industry but I'm - I'm having a little difficulty in the sense that I would imagine for a number of the kinds of jobs we're talking about, that the higher paid worker with the premium for skill would be being paid above the Award?

PN11364

Well if the Award wage is \$20 and there's someone being paid \$23, it's possible they might be a couple of dollars above the Award, yes?---And in that case the rates aren't binding. The - in that case the penalty rates aren't binding, so that the - the question of - the question of the increase for the higher skilled worker isn't determined in that - in any way by the - by the penalty rates, the employer obviously could choose to - could choose to keep on that worker and - and take away some of their above award - or payment.

PN11365

So when you say that the penalty rates aren't binding on the higher paid worker, so you're assuming that the worker on \$23 an hour is not entitled to a penalty rate?---No. No, I'm simply assuming that, as in the hypothetical you said, that they're not entitled to \$23 plus time at 1.5 because the Award wage, as I understand it, is - is, in this example, is 17 or \$20. So if the Award goes - the Award minimum goes up by 50 per cent, the question of how much - whether the employer increases the above Award worker's wage by 50 per cent or by a smaller amount that would keep, for example, the absolute margin constant, appears to be a matter of discretion.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11366

But you accept that if the higher paid employee is at \$23, and let's say there's a hundred per cent penalty, the employer's going to have to increase - he or she is going to have increase the employee at \$23 at least some amount to ensure that they are paying at an Award-compliant level?---They certainly have - obviously

they all get - they all get the Award-compliant level, but the whole point of the hypothetical is that the higher paid employee is getting a premium bargained with the - bargained with the employer above the less skilled worker. So the question of that premium, my point is that premium isn't determined in the case of a worker who's receiving more than the Award by the penalty rate. The penalty rate merely ensures that the higher paid worker can't be reduced below the new wage for the lower paid worker.

PN11367

So is your position, in response to the question, when we talked about - my actual interest is in whether an increase in the level of the penalty - sorry, the existence of the penalty rate, and that is an increase in the minimum wage payable by 100 per cent or whatever it is, is likely to see a substitution between lower paid and higher paid workers? Do you have a view as to whether that substitution is more likely or less likely than in the case of an increase of the minimum wage?---So the issue arises, I think, potentially in the case where there are different classifications of workers, and so in principle we might see, if there are classes of waiters, for example, and some of them require more qualifications, and they all receive the increase, we would expect not to see a substantial substitution effect arising in that case because they're both receiving the Award increase. But in the hypothetical you were mentioning, the increase to the higher paid worker is - is discretionary so that the calculation of the effect I think is just much more difficult.

PN11368

Thank you. Now in paragraph 25 you talk about the Sunday surcharge?---Yes.

PN11369

Do you know the proportion of restaurants that charge surcharges on Sundays?---No.

PN11370

Do you know the extent to which the Sunday surcharge actually off-sets increases in labour costs within restaurants in the industry?---You can calculate the effect. I didn't perform the calculation here, but quick mental arithmetic suggests that it should roughly off-set that cost.

PN11371

That it should roughly?---Roughly off-set the cost. So a typical surcharge is 10 or 15 per cent, allowing for - allowing for labour at 30 per cent of cost of operation, I think that gets you about the right amount.

PN11372

So you haven't done that but that's your view, that that's what the calculation would show?---It roughly off-sets the extra cost of labour. Of course, in any individual case you have to look at the question of the mix of owner labour and hired labour, so that it's very difficult to actually do that calculation for particular cases, but my understanding would be that roughly speaking that off-sets that extra cost, yes.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11373

Now can I ask just about restaurant meals generally. Do you agree that they are - that the dining out, whether that be at a restaurant or - well if I focus on restaurant initially. That restaurant meals are complementary activities to leisure?---Well that's a complicated story because there are two large categories; business meals, which roughly speaking are complementary to work, and then family meals, so I think it would be very difficult to answer that question.

PN11374

So is it your position that a business meal is more complementary to work, whereas a family meal is more complementary to leisure?---Yes.

PN11375

I'd like to show you - can I ask you, Professor, and I only chuckle because the document I'm going to refer to has received a lot of attention in these proceedings already. I'm going to ask you whether you know of the existence of the Productivity Commission Draft Report that was released - - -?---I do.

PN11376

Thank you. And I've just lost my copy, apologies. Released in August this year. What I'd like to do is just posit some questions to you, but based on a couple of comments that are included in this report. I have copies of the documentation here, so I'll show you. Now this first document that I've shown you is the key findings, if you like, or key points that arise from Chapter 14 of the Draft Report, which talks about regulated weekend penalty rates for selected consumer services. The seventh bullet point in those key points says that, "Excessive penalty rates for Sundays reduce hours worked, mean unemployment is higher than it needs to be and reduce options for businesses and consumers. Trading hours are likely to be lower and capital under-utilised." If we skip the next bullet point and move to the one below it, "Lower rates would affect the incomes of employees currently working on Sundays in the relevant industries, however this would be partly off-set by higher demand for labour." Now, do I take it that you disagree with the comments that are contained in - in that, based on the views that you've expressed in your report?---A lot hangs on the word "partly" written - - -

PN11377

I'm sorry, I - - -?---I'm sorry. A lot hangs on the word "partly" here. It's - with the kinds of elasticities we're estimating the off-set would be, perhaps, with an elasticity 0.1, the off-set would be only 10 per cent of the lost income, so that while the effect might be present, it certainly would not change the finding that the workers in question would be very substantially worse off as a group.

PN11378

Thank you. I'll like to now take you to another excerpt.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11379

MR DOWLING: Well, your Honour, I'm really not sure what the utility of this exercise is. The witness is being asked to comment on a draft productivity report.

I'm not sure how that assists the Commission in the exercise that they are undertaking.

PN11380

MR IZZO: Your Honour, there are economic views expressed in the productivity report that parties may later wish to rely upon. My primary concern is that we are not later criticised that if the views expressed in the Productivity Commission report are contrary to views expressed by the relevant experts that they haven't had an opportunity to respond.

PN11381

JUSTICE ROSS: All right. No.

PN11382

MR IZZO: If that objection is not going to be taken, then I'm happy to curtail the examination, but I'm merely protecting my client's interests, your Honour.

PN11383

JUSTICE ROSS: Without – well, what do you want to say about it, Mr Dowling? I mean, without compromising the position you might take on admissibility for a moment, if the report was before us, are you going to take any point that it wasn't put to Professor Quiggin?

PN11384

MR DOWLING: Well, I'd have to reserve my right to do so, I think, your Honour.

PN11385

JUSTICE ROSS: Yes. Look, I suspect the quickest way is to – how many questions do you have on this issue?

PN11386

MR IZZO: There's not a lot, your Honour.

PN11387

JUSTICE ROSS: All right. Well, let's move on.

PN11388

MR IZZO: Thank you, your Honour. I'm going to hand you another document. There's only three, so this is the second of three. Now, I have to apologise, I'm not domiciled in Melbourne so that the version I have has some underlining in it?---That's fine.

PN11389

But that's the section I want to take you to anyway. Just before I do that, your Honour, I'm conscious that there's a question about the admissibility of the productivity report generally. In terms of whether these documents are tendered or not, I was initially planning on tendering them just so that the Bench has a record of what the questions been responded to.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11390

JUSTICE ROSS: Well, for that purpose they can be tendered, yes.

PN11391

MR IZZO: Okay. Well, I'd seek to tender the first document then.

PN11392

JUSTICE ROSS: ABI7.

**EXHIBIT #ABI7 EXCERPT FROM DRAFT PRODUCTIVITY
COMMISSION REPORT**

PN11393

MR IZZO: So in relation to this document, which is page 522 in the bottom left corner, the productivity Commission then expresses an overall view where it says:

PN11394

It's overall view informed largely by the reality that labour demand responds to wage rates is that as there is a significant differential between Saturday and Sunday penalty rates, their greater alignment is highly likely to have sizeable employment effects. The conclusion is not underpinned by the simple adoption of any assumption that employment is highly responsive to wage rates as in Lewis, nor by on critical acceptance of anecdotal surveys of business, though the latter has some value because business is other parties that make the decisions about whether to open or employ people. It rests primarily on the significant size of the wage differential between Saturday and Sunday.

PN11395

I take it, Professor, that you don't agree with that either?---So I agree with the criticism of the suggestion of Professor Lewis that the impact would be large. On the broader point I think the Productivity Commission is making the same error that I've identified previously. The existence of this differential certainly shifts demand and employment between Saturday and Sunday. Saturday and Sunday in consumption are days of closed substitution so that the assumption that because the people are eating more on Saturdays and less on Sundays that there will be a large net effect I think is mistaken, and there's certainly no evidence given for it.

PN11396

All right. Thank you. I would seek to tender that document, your Honour.

PN11397

JUSTICE ROSS: On the same basis?

PN11398

MR IZZO: On the same basis. Yes.

PN11399

JUSTICE ROSS: I'll mark that exhibit ABI8.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

**EXHIBIT #AB18 FURTHER EXCERPT FROM DRAFT
PRODUCTIVITY COMMISSION REPORT**

PN11400

MR MOORE: Your Honour, I understand that they're marked as - essentially as marked for identification.

PN11401

JUSTICE ROSS: That's exactly right. Yes.

PN11402

MR MOORE: Thank you.

PN11403

JUSTICE ROSS: So you can follow the cross-examination on the transcript.

PN11404

MR IZZO: Just bear with me. Apologies, one moment.

PN11405

JUSTICE ROSS: To the extent to which you think you're whispering, we're picking it all up so you might just bear that in mind.

PN11406

MR IZZO: Thank you, your Honour. Professor Quiggin, given – and I might have to take you industry by industry unfortunately so just bear with me one moment. I'll just give you some figures of the penalty rates. In the Restaurant Industry Award, you may be familiar with these, but I forget them from time to time, so I think you'd appreciate the refresher. In the Restaurant Industry Award, the Saturday penalty rate is 125 per cent whereas for casuals at the introductory level and some of the earlier grades the Sunday rate is 150, and for the higher grades of permanents and – sorry, I'll rephrase that – for permanents and higher grade casuals it goes up to 175 per cent. That's in the restaurant industry. So we have Saturday rate of 125, Sunday is either 150 or 175 depending on who you are effectively. That is a substantial increase in the rate of pay that is applicable between a Saturday and Sunday. That's the first thing I'd like you to respond to?---Yes.

PN11407

In relation to the Retail Award, the rate for everyone is 125 per cent on Saturday and 200 per cent on a Sunday. Again, I put it to you that's a substantial increase in the rate of pay applicable between those two days?---Yes.

PN11408

And in the Hair and Beauty Award it's 133 per cent on a Saturday and 200 per cent on a Sunday. Again, I put it to you that's a substantial increase?---Yes.

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11409

And that such is the size of that increase that when we go back to the mainstream discussions – sorry I'll withdraw that question. I'll start again. We earlier had a

discussion about the fact that in relation to minimum wages it is your view that provided there are appropriately moderately set the increases in minimum wages shouldn't have a substantial adverse employment effect?---Yes.

PN11410

But you agree that in the mainstream literature that position might not hold true if the increases are substantial to the minimum wage?---Yes, as regards to minimum wages, that's correct.

PN11411

And what I would like you to respond to is that in relation to the change of the rate between Saturday and Sunday, so high is the change in the rate that we are likely to see a substantial dis-employment effect much like would be the case for minimum wages?---We'll certainly see substantial lower employment on Sundays which is indeed the intention of the penalty rates to set aside Sunday in particular more than Saturday as a day when people aren't expected to work, but merely all of that employment loss would be made up by increased employment on other days of the week.

PN11412

Thank you. And also - just bear with me one moment. Professor, in relation to paragraph 24 of your report?---Yes.

PN11413

If I can direct you to the Professor Lewis reply, which you did have in one of your tabs?---Yes. I'll just take a moment on that.

PN11414

Tab 4, I believe, and page 12?---Yes, I've got it here.

PN11415

You were asked to respond to that, what had been put there by Professor Lewis, by Mr Dowling earlier. And you mentioned that because owners or owner/operators wish to maintain their level of income for instance, that they're likely to maintain their working hours. Do you recall saying that?---I do.

PN11416

You accept though that income for an owner, it's not necessarily derived from their working but it's derived from the business operating and generating the profit, and it may generate a profit from capital, hired labour, or potentially the owner's own hours?---All of those sources are relevant, though I would say in the restaurant industry looking certainly at owner/operated restaurants as opposed to chain restaurants that their surplus return on the capital employed is very small; that virtually all of the profit, in my view, can be seen as return to the managerial and work effort of the operators, so - - -

*** JOHN CHARLES QUIGGIN

XXN MR IZZO

PN11417

When you say "owner/operator" restaurant, that's a – what, a one-chef show or - - -?---No, I'm merely making the – I'm merely referring to the case of a single – a business owned by a single individual who works in the business as opposed, for

example, to a McDonalds type corporation, for example, although then we get into complications about franchising, but if we can imagine large scale restaurants where there is indeed a large volume of capital employed. If we look at a typical restaurant they have a leased – the capital is largely leased and then the operating capital financed by a loan so that the return capital in most cases would be quite small. The return, in my view, would be mostly regarded as return to the skill and effort of the operator.

PN11418

So when we're talking about an owner/operator restaurant, is your only test that there is an individual who owns the restaurant and they work in it, or is it that there are not many employees working in it and the majority of the labour in that restaurant is derived from the owner/operator?---No, I would apply that analysis broadly speaking to, you know, I mean, I – this is somewhat off the cuff but if we take a typical restaurant, you know, walked out on to Flinders Lane and looked at a typical restaurant of 15 seats perhaps, you know, 10 people employed, I will be judging that the return to the owner of that there's no significant return to capital. That return essentially after paying wages and food costs the owner/operator of those restaurants are getting a return which is essentially commensurate with the work, effort and skill they put into it.

PN11419

Thank you. Bear with me for one more moment. I have no further questions, your Honour.

PN11420

JUSTICE ROSS: Any other cross-examination?

CROSS-EXAMINATION BY MR DIXON

[3.43 PM]

PN11421

MR DIXON: Thank you, your Honour. Professor Quiggin, could you confirm that your qualifications are as an economist?---I have a PhD in economics, yes.

PN11422

And you have no study in the area of industrial relations?---No, that's incorrect. I've published a number of articles on employment industrial relations listed on my CV.

PN11423

You have no study on the issue of bargaining on equal terms between workers and employers?---I have a number of papers in leading economics journals on issues of bargaining between workers and employers.

*** JOHN CHARLES QUIGGIN

XXN MR DIXON

PN11424

And you have in your paper, I'm correct am I not, in an observation that you have not in any way provided any underpinning view in respect of what might happen in respect of bargaining on equal terms between workers and employers in particular circumstances?---Well, I suppose the premise of bargaining in equal terms I think is one that is broadly inconsistent with the entire framework of the

Fair Work Act which suggests that workers need the protection of Tribunals like this one in order to allay the inequality of bargaining that normally takes place between employers and employees.

PN11425

And so should we take it from that that, as I understood your answer, you proceed on the basis that there would be no bargaining on equal terms between workers and employers in the industry you have addressed?---In general I would say the assumption of equal terms is not one I would accept without challenge. Was the question about my research or about this equal terms issue?

PN11426

Just in relation to the equal terms issue?---Well, my view would be that the question of bargaining in equal terms is highly problematic just for that reason indeed that we have an award system.

PN11427

Did I understand you correctly in one of the earlier answers you gave the restaurant and café industry is not one that you're very familiar with?---It's not one that I've done a great deal of work on, no.

PN11428

You did mention, as I understood the answer you gave to a question earlier, that you would draw a distinction between the substitution of demand for restaurant services or meals between meals that were complimentary to leisure and those that were associated with business?---That's – there certainly is a distinction. The relevance of the distinction wasn't made clear to me. I was simply asked whether restaurant meals were a compliment to leisure and I said some were and some weren't.

PN11429

Yes. And in respect of those that are complimentary to leisure you do not suggest do you that there will be substitution for restaurant services from Saturday or Sunday to a weekday?---I do suggest that. It seems, speaking as a consumer of leisure, restaurant meals, I consume them both on weekends and on weekdays and relative cost and availability would be a factor, and I assume that's true for consumers in general.

PN11430

And if the price on a Sunday or the Saturday of the restaurant is the same as it is on the Wednesday, are you seriously suggesting that for leisure services a consumer will, on a Saturday say, "They might be paying penalty rates here I better go and eat on a Wednesday."?---Sorry, could you repeat the question?

*** JOHN CHARLES QUIGGIN

XXN MR DIXON

PN11431

Are you seriously suggesting that in respect of leisure consumption a potential consumer, where the prices for the restaurant are the same on the Saturday and the Sunday as they are on Wednesday, that the consumer, or potential consumer, is going to be interested at all in penalty rates and therefore going to consume on the

Wednesday?---No. Well, of course, if the restaurant absorbs the penalty rates then there'll be no effect on consumption patterns, so I wouldn't suggest the opposite of course.

PN11432

So your evidence in relation to that substitution was entirely based on the basis that the prices for the Saturday or the Sunday are higher than during the week; is that right?---Either the prices or the availability. Obviously if the restaurant has offered the same services unaffected by penalty rates, there could be no effect on consumers.

PN11433

Thank you.

PN11434

JUSTICE ROSS: Any further cross-examination?

CROSS-EXAMINATION BY MR SECK

[3.49 PM]

PN11435

MR SECK: Seck for the Pharmacy Guild, your Honour. Professor Quiggin, from the title of your report I gather you were only asked by United Voice to consider the effects of penalty rates in the restaurant sector; that's correct?---Yes.

PN11436

I have a copy of your letter of engagement dated 10 August 2015. I don't have a copy for you but I gather you did receive a letter of engagement from United Voice?---Yes, that's correct.

PN11437

Setting out what you were meant to do?---Yes.

PN11438

The background information, and the request that was made of you in preparing the report was initially to deal with a number of different awards and not limited to the restaurant industry; that's correct?---My understanding was that it was always the restaurant industry that I was engaged to work on.

PN11439

Now if I can take you to your report, Professor Quiggin. Your report is primarily to respond to matters raised in Professor Lewis' report. That's correct?---Yes.

PN11440

And you understood Professor Lewis' report addressed other industries besides the restaurant industry. That's correct?---That's correct. My understanding of my brief was that I should focus on the points that were either applicable to all industries or applicable specifically to the restaurant industry.

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11441

Right, can I take you to your responses to question 3 which starts at page 6 of your report, Professor Quiggin?---Yes.

PN11442

You'll see that the question which is stated at paragraph 18 on page 6 of your report is expressed in general terms and not limited to the restaurant industry. Do you see that?---I do.

PN11443

However can I take it from the answer given in paragraph 20 of your report on page 7 that your response was purely limited to the hospitality industry; that's correct?---That's correct. As I understood the brief, particularly the last sentence of it, the intended focus was on the restaurant industry.

PN11444

You used the term hospitality industry there but I'm assuming you're using that interchangeably with the restaurant industry?---I am. I haven't got the ANZSIC codes in front of me, I'm afraid.

PN11445

That's okay. Now do you acknowledge, Professor Quiggin, that there are obviously different industry characteristics that apply across different industries?---Certainly.

PN11446

And the characteristics of for example the community pharmacy industry would not be the same as the characteristics of the hospitality industry. That's right?---That's correct.

PN11447

So a number of the propositions that you set out in answer to question 3 of your report may not have any applicability to the community pharmacy industry. You would accept that?---I certainly haven't tested their applicability. There are certainly points in the report that are specific to the restaurant industry, other points that are general.

PN11448

And one of the fundamental premises contained in your answer to question 3 in your report is that the restaurant industry is primarily focused on discretionary and luxury expenditure. That's right?---That's right.

PN11449

And you would accept the proposition that spending in the community pharmacy industry is not considered luxury or discretionary expenditure?---That's true.

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11450

Would you also accept the proposition, Professor Quiggin, that whilst in the restaurant sector the labour that can be used by an owner operator or their family is largely unskilled labour; the labour involved in operating and working in a community pharmacy involves a degree of skill?---I think unskilled is too strong

but obviously - I don't know, I haven't studied the pharmacy industry but I understand that to operate, to dispense prescriptions you need a qualified pharmacist. Whereas of course there's no credential requirement in the restaurant industry. So while I wouldn't want to suggest that restaurant operators are unskilled, there's - certainly anybody who wants to can open a restaurant. That's not true of a pharmacy, as I'm sure you're aware.

PN11451

Professor Quiggin, in paragraph 20(iv) on page 7 of your report you say:

PN11452

The primary avenue by which employment in the industry might be increased is an increase in the number of establishments opening on Sunday and public holidays.

PN11453

Do you see that?---I do.

PN11454

Now do you assume in your report that the vast majority of restaurants in fact open on a Sunday?---No, the - there's evidence in the Productivity Commission report that shows that - I believe it's a majority but there is a substantial minority of restaurants are closed on both Sundays and Mondays.

PN11455

And of course if it was the case that - - -

PN11456

MR DOWLING: Your Honour, I thought there was intended to be some discussion between the employer representatives on this issue? This is clearly territory that has been covered before. I don't know why it is we're going over it again.

PN11457

JUSTICE ROSS: I don't think that issue has been covered before.

PN11458

MR DOWLING: That's not my recollection, your Honour, but - - -

PN11459

MR IZZO: From my understanding certainly the question about the number of restaurants open on Sunday.

PN11460

JUSTICE ROSS: Yes.

PN11461

MR IZZO: I did not ask about that.

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11462

JUSTICE ROSS: No. I think the answer raised the Productivity Commission report but it wasn't put in the question.

PN11463

Move on, Mr Seck.

PN11464

MR SECK: Thank you, your Honour.

PN11465

Now the factual basis upon which you say, Professor Quiggin, that a substantial minority of restaurants are closed on the weekend you say was based on the draft Productivity Commission report. That's right?---I undertook some research of my own which supported that view, but the Productivity Commission's study is more comprehensive so that's I think a useful basis on which to rely.

PN11466

All right, and of course you have no direct knowledge of the number of community pharmacies which open on a Sunday or public holiday, do you?---No.

PN11467

And assuming that a substantial majority of community pharmacies close on a Sunday or public holiday, you would agree that if penalty rates decreased so as to make it profitable - and I want you to assume this - to operate on a Sunday or public holiday, there would be according to your analysis an increase in employment in that industry. That's correct, isn't it?---I'm afraid my lack of knowledge of the specific industry are giving me difficulty here. For example I understand as we were discussing that a licensed credential pharmacist must be present at all times and I'm not aware whether that person is subject to penalty rates or not. So I think you're unfortunately asking me to speculate on points that because of my brief I haven't researched.

PN11468

Right, I want you to assume for the purpose of the question, Professor Quiggin, that pharmacists are in fact subject to penalty rates under the Pharmacy Industry Award. Could you answer the question?---So could you repeat the question now?

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11469

That assuming that a majority or a significant majority of community pharmacies are not operating on a Sunday or public holiday because it is unprofitable to do so due to penalty rates, if there was a reduction in penalty rates which made it profitable for a community pharmacy to operate on a Sunday or public holiday one would expect, based on your proposition in paragraph 20(iv), that there would be a significant increase in employment. That's correct, isn't it?---No, I think the point I made here is precisely that the question would depend on whether the services consumed on Sundays were additional or were substituted for other days. So if it's for example filling a routine prescription, I would expect that it would be more convenient to - perhaps to go on Sunday. But obviously if the rest - pharmacy were closed on Sunday I would go on another day and fill it. Other

services that might be offered might expand their demand on - because of the extra availability and that might lead to an increase in the total demand for pharmacy services and total employment. But again my lack of knowledge of the industry makes it very difficult for me to give you a good answer on that.

PN11470

And your comment about the ability to shift demand from a Sunday to another day during the week is based on the premise that there's an ability for a consumer or a need for a consumer - or sorry, that it doesn't matter to a consumer whether or not those services are consumed on a Sunday or a weekday. That's correct?---No, this is again the error made by Professor Lewis in his report. We can take the two extreme cases; the consumer doesn't care or the consumer can only consume on the Sunday and there is no other possibility. It's perfectly possible that the consumer would prefer Sunday to other days, but that if Sunday isn't available or is more expensive they will switch to a different day. That's the standard case of substitution.

PN11471

That would only apply in circumstances where there's an ability to shift it to another day. That's right, isn't it?---That's correct.

PN11472

And I'm going to use an example, and just assume this example is correct. If there is a medical misadventure and there is a need for medication on a particular day, assume it's a Sunday or public holidays, and that is required on that day, there wouldn't be an ability to shift it to another day. You would agree with that?---I would assume in those circumstances, putting myself in that position, that I would travel further to go to a different pharmacy.

PN11473

But you're making that assumption. That's correct, isn't it - - -?---Well, I suppose I'll state it more strongly. Having faced that situation my response has been to travel further and go to a pharmacy that's open.

PN11474

You're not of course aware of the ownership rules that apply in the community pharmacy industry, are you?---I am aware that ownership is restricted to pharmacists and that this is a matter of controversy, though I think yes.

PN11475

And you're also aware that there are restrictions in terms of geographic distribution of pharmacies, aren't you?---I am aware of that.

PN11476

That's correct?---Yes.

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11477

And that would be a relevant factor which may impact on the ability of a consumer to travel to another pharmacy, because there may not be one close by. That's correct, isn't it?---I - it's - I mean, we're possibly straying outside the

sphere. This is a view which I have looked at in other contexts but it's certainly true that those rules make substitution less convenient than it would be otherwise and pose significant difficulties to consumers. That fact has been well ventilated in the discussion over competition policy.

PN11478

Right. Can I deal with Sunday surcharges in paragraph 25 of your report, Professor Quiggin?---Yes.

PN11479

Of course you're only aware of surcharges applying in the café and restaurant industry. You're not aware of Sunday surcharges applying in the retail industry, are you?---No.

PN11480

And certainly not in the community pharmacy industry?---No.

PN11481

No further questions.

PN11482

JUSTICE ROSS: Any further cross-examination? No?

PN11483

Professor Quiggin, I want to address particular statements in your report where the basis for the opinion doesn't seem to be made express?---Sure.

PN11484

And to ask you what the basis is, okay?---Sure.

PN11485

Can I take you to paragraph 20 of your report?---Yes.

PN11486

And (iii), and the second sentence there commencing "It is therefore likely that". What's the basis for that opinion?---Well, in fact you can take this right back to Adam Smith's Wealth of Nations. In chapter 10 of that book which is on wages, the very first point mentioned is that wages for workers with day time work are higher than for workers of similar skill who have to work at night. So that point was I thought - you know, has been known since the beginning of modern economics and is very well established.

PN11487

All right. If I take you to (iv)?---Yes.

PN11488

The second sentence:

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11489

However any increase in consumer expenditure on such days would be likely to come at the expense of expenditure at other times.

PN11490

?---So again it's a very well established principle that goods which are similar in their characteristics are substituted in consumption. So we - that's again a proposition which is in some sense so standard that it's difficult to find somebody re-proving this point in the recent literature. But it's reflected in the practice of course of most statistical agencies in simply aggregating these into a single good. So from the point of view of for example the Australian Bureau of Statistics there's no difference at all between a restaurant meal consumed on a Sunday and a restaurant meal consumed on a Wednesday. They both appear in the output of the restaurant sector. That reflects the similarity of these commodities. So it's a very standard principle that very similar commodities are close substitutes.

PN11491

And the last sentence in (iv):

PN11492

Moreover the fact that many establishments close on Mondays when there are no penalty rates suggests that pay rates are not a primary determinant of opening hours.

PN11493

?---So this is I guess a basic principle of causality that if we assert that some factor is the primary cause of a phenomenon, take it away and see that the phenomenon is still present, we would normally infer that that - or at least we would tentatively infer at least that that - it was a mistaken claim that that was a crucial determinant. Of course it's possible that there's some other factor intervening or something, but in general if we take something away and nothing changes, we assume it doesn't have much of an effect.

PN11494

And in paragraph 24, can I take you to that, and it's the last sentence there:

PN11495

This change will be offset by an increase in the employment of operator family labour on days other than Sundays and a reduction in the employment of hired labour on those days.

PN11496

?---So we covered this of course in evidence and indeed Professor Lewis in his statement that operators would maintain their leisure and income is making essentially the identical point, although he did also make the opposite point.

PN11497

Paragraph 25, the last sentence:

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11498

There is little reason to suppose that total expenditure on café and restaurant services would increase substantially as a result of a shift of demand towards Sundays.

PN11499

?---Again this reflects the judgment that these are fairly close substitutes, and further that there's no compulsory expenditure which would lead - you know, would lead you having spent the money to - having spent more money on a Sunday to - not to change your consumption on other days. And that's - it's a combination of close substitution and discretionary spending I think is pretty important here.

PN11500

And paragraph 27, the last sentence?---So it draws on the previous part of that paragraph so it makes the point that implicitly in much of this analysis of substitution we assume that there's as much as you want of the substitute good available at the given wage. But if we're talking about an operator labour that clearly isn't the case. So if the operator - if we imagine for example a very large increase in penalty rates, the operator can't simply add more and more of their own hours. They're already typically working quite long hours so there's a - the elasticity changes as the number of hours increases. So we expect to see the operator, again as Professor Lewis observed in his final point, trying to maintain themselves roughly speaking in that kind of sweet spot where the additional disutility of working longer hours is offset by the additional earnings.

PN11501

And the last of these matters I wanted to take you to is in paragraph 9 of appendix A?---Appendix A?

PN11502

Yes?---Yes.

PN11503

On page 12?---Got that, yes.

PN11504

It's the last sentence commencing with the words:

PN11505

Since part-time employees are particularly likely to receive penalty rates.

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11506

?---So this is a very well established proposition in the US literature. Dr Presser of the Russell Sage Institute, Harriet Presser, is the primary source but there are many papers establishing this proposition in the US context. Again, you know, given the limited resource of the Australian economics profession we don't have the resources to re-establish propositions which are on their face obvious and supportable international evidence. So I think it's clear from common knowledge of the way working hours are that standard hours and full-time employment tend

to go together. But that proposition has been very firmly established in the US literature.

PN11507

Can I go to this question of substitution for a moment?---Sure.

PN11508

And you deal with this at the last sentence of paragraph 29 where you talk about much of the demand effects of penalty rates will shift the time at which restaurant meals are consumed and you make a similar point at paragraph 25?---Yes.

PN11509

And this substitutability, I understand the economic assumption but it does strike me as a little counter-intuitive in some circumstances, and that may go to the degree of substitutability, and I suppose like most of us you tend to look at this through the prism of your own experience. Well, let me put this to you, that on most Saturday mornings my wife and I have brunch with whatever daughter happens to be passing through our living arrangements at that time, and if for whatever reason cafés weren't open or didn't open because of penalty rates effects or something else on a Saturday, it's not an activity that we could easily transfer to another day of the week because we both work Monday to Friday. So I'm just - - - ?---Sure.

PN11510

Yes?---Well, I think the first point is of course that there's a lot of substitution between Sunday and Saturday in this context.

PN11511

Yes?---But the second point which - I mean I am you know, venturing out into to some extent economic sociology, is that these patterns themselves adapt and are reinforced by the structure. The whole point of the penalty rate system is to keep Sunday for all but essential workers as a day that we can all have off. And of course people when they plan their weekends obviously - you know, they don't plan to go to the bank on a Sunday for example because they know it won't be open and so - and similarly, you know, as I mentioned in my - the evidence, people don't plan restaurant meals on Monday because lots of their favourite restaurants are closed on that day. I don't - obviously we can't - this is an untestable hypothesis but there's no obvious reason why people want to stay home and watch TV on Monday and not on Tuesday. It's just that we know that Monday isn't a good day to go to restaurants and so typically we don't. And so my view would be that there's a very complex process of adaptation but that in the end the underlying economics is we've got a household budget, we've got a taste for consuming restaurant meals and we'll meet that in a way that meshes our schedules with those of the restaurant industry, and if they don't fit we'll adjust our patterns a bit.

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11512

And is that I suppose based in part on the fact that it's regarded as a luxury activity?---That's certainly part of it but obviously an essential commodity that

wasn't available on Sundays would be highly problematic. I mean in this context obviously if we had to call emergency services or something we'd always expect it to be provided as and when we need it. I mean it's interesting that that's an area that seems to be excluded from the idea that penalty rates shouldn't be paid, but in general for a discretionary type expenditure where, you know, the typical Australian consumption patterns, you know, I don't imagine many households would have more than one or two dinners out a week. So it's pretty easy to substitute those according to the times when your friends are available and of course the times when your preferred restaurants are open.

PN11513

Anything arising for the - - -

PN11514

DEPUTY PRESIDENT ASBURY: May I? Sorry.

PN11515

JUSTICE ROSS: Yes, certainly. Yes.

PN11516

DEPUTY PRESIDENT ASBURY: Professor Quiggin perhaps I didn't hear you properly so let me just put to you what I understood you said about a particular matter. It was with respect to your comments about restaurant owners or business owners who work in their own business substituting themselves by perhaps engaging a casual worker, and your proposition that if they did that they would simply work the hours on another day of the week and thereby displace a casual worker who might have been working on that day. Is that the - - -?---That's broadly speaking what I said, and as I pointed out, Professor Lewis made the same point.

PN11517

And you also made a comment that particular businesses who decided what they would do on a day to day basis in terms of opening, employing staff, in your view would not last very long or would have some viability problems?---That's correct. If you disregard your fixed costs and, you know - I mean I find it difficult to conceptualise how a business could do that, could disregard the fact that they have rent to pay and just decide in some sense separately each day of the week whether they feel like running a restaurant. It seems - because of the nature of the business it just seems to me that that - I couldn't really follow the premise of that question.

PN11518

I guess could I put to you that some of the evidence that we've heard from people who own businesses and restaurants has been to the effect that, "If I averaged it across a week I wouldn't have a viable business. I look at who I employ and when I employ them on a daily basis?---Well, it's - yes, sure.

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11519

Rather than if I save on a Sunday I'm not going to - - -?---Sure, if I could - yes. No, I think that's entirely correct reasoning. If I could refer you back to the original question it was to do with marginal and average costs, and so the question is not - it's certainly the case that when you're looking at whether you open on Sunday or not, you look at your marginal costs. My point is those marginal costs are themselves very dependent on the decisions you've made on other days of the week, and most importantly on the decision that's been made whether to enter the industry at all. So if we look at something which changes average costs by a small degree, the primary margin of adjustment in the long run is how many people decide to enter the industry at all. Once they're operating of course they make - they do indeed make day to day decisions. The point is that you can't, as was suggested in both Professor Lewis' report and I think put to me in cross-examination, treat that decision in isolation from the decisions. They're not - they're separate decisions of course. You can decide to open Saturday and not Sunday but the idea that that decision is uninfluenced by what happens at other times of the week is I think nonsensical.

PN11520

And perhaps I didn't understand your evidence but if you were saying that - I understood you to be saying that a restaurant owner who wanted to maintain or a business owner who wanted to maintain his or her lifestyle would work some additional hours through the week if they didn't work hours on the weekend?---That's I would say what the definition of maintaining your leisure hours is.

PN11521

Couldn't it also be the case that you're assuming that to maintain an income they're paid by the hour, rather than they simply might say "I'm not going to work on this Sunday. I'm going to get someone else to work on it and I'm not going to take an additional day off through the week"?---Well, that would be a decision not to maintain your existing leisure and income. That would be a decision to take additional leisure and a reduction in income. I was only saying - I was only - - -

PN11522

How would that reduce your income?---Well, if you pay an additional worker, your income is reduced. If you don't offset that in some way then you have a lower income and of course more leisure. Is that clear or am I?

PN11523

Yes. Thank you.

PN11524

JUSTICE ROSS: Anything arising for the cross-examiners?

PN11525

MR IZZO: I have two questions, your Honour.

PN11526

JUSTICE ROSS: Sure.

*** JOHN CHARLES QUIGGIN

XXN MR SECK

PN11527

MR IZZO: No, I'm happy for - I see Mr - - -

PN11528

MR DIXON: No.

PN11529

MR IZZO: No?

PN11530

JUSTICE ROSS: We could be here all afternoon.

PN11531

MR IZZO: I'm happy for Mr Dixon to go first.

PN11532

JUSTICE ROSS: Yes.

PN11533

MR IZZO: And then I'll go.

PN11534

JUSTICE ROSS: Yes, Mr Dixon, you go.

FURTHER CROSS-EXAMINATION BY MR DIXON

[4.17 PM]

PN11535

MR DIXON: I'm sorry, I could not see my learned friend. I didn't mean to go ahead of him.

PN11536

Professor Quiggin at the beginning of your cross-examination this afternoon you were asked questions in relation to paragraph 20(iv) on page 7 of your report?---Yes.

PN11537

Could you go to that please, and our notes about your answer in respect of the last sentence of that paragraph were to the effect that they were not expert views or opinions and they were simply your view and you were speculating and - - - ?---No, I think if I could - sorry, do you want to go on?

*** JOHN CHARLES QUIGGIN

FXXN MR DIXON

PN11538

You do not know of that earlier evidence, do you?---Sorry, I was asked two questions. One is whether this was relevant evidence in terms of the effect on penalty rates, which I think is standard economic reasoning. That if you take away the effect and don't see a change then you can assume that - then you can infer that the effect of penalty rates is small. The second question was why it is that Monday is chosen as the day that restaurants close and there I said that this wasn't an area that I had expertise on. But on the point made actually in para. 4

this is based on a very standard reasoning of causality in which economists are well trained.

PN11539

So can we just clarify that; in respect of what is in the last line of subparagraph (iv) where you say:

PN11540

It suggests that the rates are not a primary determinant of opening hours.

PN11541

That is not expert opinion and simply your view and you were speculative?---No, that's an expert opinion. The point I was making as to regards speculation was whether the closure on Monday was a reflection of consumer demand or industry custom, a point raised in cross-examination.

PN11542

Thank you.

FURTHER CROSS-EXAMINATION BY MR IZZO

[4.19 PM]

PN11543

MR IZZO: Professor, you were asked a question by his Honour President Ross in relation to substitution between weekend meals and weekday meals and you made a response in which you referred to ABS statistics and you referred to the fact that the ABS doesn't differentiate between a meal on a Saturday and a meal on a Sunday or a weekday and that they're all outputs, I think you referred to them as?---I think the question was about substitution in general, but yes.

PN11544

Yes. That doesn't mean though that there's no difference to a consumer between a meal on a Saturday or a meal on the Sunday. It's just that the ABS doesn't distinguish between the outputs?---Yes, it means I would say in the expert judgment of the ABS that the distinction is small enough to be disregarded in their decision as to which data to collect separately and which to aggregate.

PN11545

And the other thing that you mentioned, again in response to a question by his Honour Ross J, was that if there is a difference or if there is a change made to the operating hours of restaurants, for instance restaurants open on a Sunday when they were previously shut, you made a comment that the household budget is effectively what the household budget is. Restaurant consumption is somewhat of a luxury activity and therefore whether the restaurants are open more or open less, the level of consumption of the restaurant goods will likely remain the same because the household budget has let's say a hundred dollars a week as identified for dining, that's what they're going to spend?---Yes.

*** JOHN CHARLES QUIGGIN

FXN MR IZZO

PN11546

But if restaurants were to be closed at the times that consumers particularly might be available to use them, say a Sunday, is it not also - your response to that, sorry,

let me just clarify, is that that doesn't mean there will be a reduction in demand. The demand will just shift to other days?---That's correct.

PN11547

But isn't it also equally possible, just as possible if not more possible, that whilst a consumer might spend the same amount in their budget, due to the fact that the restaurants aren't open at the times that they so desire they may use the restaurant - they may consume restaurant products less frequently but spend the same amount?---That's possible. I would expect that the impact on employment would be negligible.

PN11548

Well, let me put this to you then. If you have a young professional couple that wish to dine out twice a week and one of their preferred choices of dining out Sunday is not available, instead of dining out twice a week they may only dine out once a week because that's all the time they have, but they will spend double the money. That is instead of spending a hundred dollars on a restaurant meal they'll spend \$200. That will have an impact on employment won't it?---Potentially a positive effect I would have thought. I mean, the capacity to eat food, the amount of food they eat has to decline. Their expenditure has increased and presumably most of that expenditure must therefore go to improved service. Instead of having one waitress or waiter attend the tables you go to a restaurant - if you're paying more you go to a restaurant with more service staff, more cooks and so forth. So I would have thought - I mean this is off the cuff but I would have thought the more you spend on a restaurant meal in general terms the greater is the labour share and the less is the food share.

PN11549

Or you converted two restaurant meals into one meal. One is of a higher quality, one may charge more, they may use similar levels of labour or the more expensive one might use a little bit more labour but certainly not double the amount of labour. In which case there would actually be an effect on employment?---Well, I mean this is just not economically sensible. I mean, if you can sell for \$200 - you know, you're implying that the expensive meal is making a massive profit. If that were the case obviously lots more people would enter the expensive meal business if roughly speaking, in a competitive industry, if you pay - you know, shall we say \$200 for a meal, the cost of that meal is going to be \$200 to provide. If the cost of the food doesn't go up a hundred per cent it must be that the other cost you're paying for are going up and the obvious cost - I mean the obvious cost to go up that's bearable is labour. So I would expect - and you know, this is my experience - the more you pay in a restaurant the more service you get. That's much more of a - obviously you also expect somewhat nicer ingredients but I would have thought that the more you spend the more labour you consume.

PN11550

But you know that labour is not the only cost in running a restaurant business obviously?---I've just mentioned food as the primary - - -

*** JOHN CHARLES QUIGGIN

FXXN MR IZZO

PN11551

And in fact are you aware that the average labour costs in a restaurant business - -
-

PN11552

MR DOWLING: Your Honour, I know it might be very broadly arising but this whole area was canvassed by Mr Izzo. It is correct that your Honour asked a question about it but that doesn't entitle Mr Izzo to have another go again at the very same topic just because your Honour asked a question about a broad topic.

PN11553

MR IZZO: If I might respond, your Honour. All the questions are directed towards one specific piece of evidence that was given, and that is that the household budget remains static and therefore no matter when the restaurants are open, demand is going to be the same. That wasn't put in any of the responses to me when I cross-examined and that's the only piece of evidence I'm testing at the moment.

PN11554

Are you aware that labour costs in the restaurant industry broadly approximate between 30 and 40 per cent of the total costs?---That's covered in mine and Professor Lewis' report.

PN11555

Yes, I can't recall the exact figure. If you have it?---It was raised. I have it. Do you want - - -

PN11556

It's somewhere between 30 and 40 per cent. Do you accept that?---That's correct, yes.

PN11557

So the other 60 to 70 per cent arises from the cost of capital, produce and other fixed and perhaps variable costs?---Of course that's an industry average. Those proportions are going to differ according to the type of restaurant, and the suggestion I've been making is that more expensive restaurants will typically have a larger labour share and a lower food share, since of course the total quantity of food is - - -

PN11558

But they will have higher produce costs as well, won't they, and higher capital costs?---They will. They'll have - so if it's a certain level you expect somewhat higher produce costs, that they would have better ingredients. But on the whole, given of course that the total amount of food consumed doesn't change very much, I would have thought the more you spend the greater the proportion of your costs are labour, and of course the same is true of tables and chairs and space in the restaurant. Just because you're going to a more expensive restaurant you don't need any more chairs. So I would have thought, you know, following your line of questioning, that if the effect of a policy was to have fewer but more expensive meals, that would increase net employment in the industry.

*** JOHN CHARLES QUIGGIN

FXXN MR IZZO

PN11559

And what I'm putting to you is that - well, I'll go back because I think this is quite a simple proposition. I'm really putting two points to you. The first is that if there are certain days that aren't available and I've got \$200 to spend on restaurant meals, I can go and eat out at times that the restaurant I choose is open - sorry, let me rephrase that. If I've got \$200 available and I want to dine twice a week and restaurants aren't open on Sunday, I can just go and dine out during the week. You agree that that's - - -?---That's certainly possible.

PN11560

That's something that's certainly possible. But equally, instead of dining out twice a week I might spend double the amount of money dining once a week, and you accept that that's possible?---Absolutely. I agree.

PN11561

But your position is that if I was to spend double the amount of money dining once a week, the place I would go to would employ double the number of people than - or sorry, would employ more people in total than two places combined?---Yes so that - - -

PN11562

Where I spend half my money at each place?---If - obviously I wouldn't be going to the same restaurant but, yes, that's the logic of the position is they would have to spend the same - - -

PN11563

Even though labour only - - -?---If I could continue?

PN11564

Yes. Yes?---They only obviously have to spend the same amount on floor space and chairs because I haven't got any bigger. They might spend more on ingredients, but I wouldn't have thought twice as much. So - and obviously the industry isn't one in which that - in which you can make super profits by putting your prices up. So I would expect that if I was paying twice as much for a meal that I would get most of that addition, or more than a proportional part of that addition, would be in the form of better service. That is more service staff, more people in the kitchen and so forth.

PN11565

All right, no further questions.

PN11566

JUSTICE ROSS: No further cross-examination, re-examination?

PN11567

MR DOWLING: No re-examination, your Honour.

PN11568

JUSTICE ROSS: Any reason the witness can't be excused?

*** JOHN CHARLES QUIGGIN

FXXN MR IZZO

PN11569

MR DOWLING: No.

PN11570

JUSTICE ROSS: No.

PN11571

MR DOWLING: If the witness could be excused, your Honour?

PN11572

JUSTICE ROSS: Thank you for your evidence, Professor Quiggin, you're excused.

<THE WITNESS WITHDREW [4.28 PM]

PN11573

JUSTICE ROSS: We might take a three to five minute break while you grab Professor Borland.

PN11574

MR DOWLING: Thank you.

SHORT ADJOURNMENT [4.28 PM]

RESUMED [4.38 PM]

PN11575

JUSTICE ROSS: The next witness?

PN11576

MR DOWLING: Thank you, your Honour, I call Professor Jeff Borland.

<JEFFREY IAN BORLAND, AFFIRMED [4.39 PM]

EXAMINATION-IN-CHIEF BY MR DOWLING [4.39 PM]

PN11577

Professor Borland, if you could please state your full name again?---Jeffrey Ian Borland.

PN11578

Your address?---(Address supplied.)

PN11579

Your occupation?---University professor.

PN11580

You have prepared a report for the purposes of this proceeding?---I have.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11581

Can I hand you a folder. If you turn to Tab 5 in that folder, is that a document headed "Report by Professor Jeff Borland Department of Economics, University of Melbourne"?---It is.

PN11582

Does that run for 26 pages, 26 pages, it has a date and your name at the very end 3 September 2015?---Yes.

PN11583

Is it true that you have also provided previously a copy of your curriculum vitae to the Commission?---I have.

PN11584

The report you have in front of you, does that report accurately set out the opinions formed by you based on your expertise?---It does.

PN11585

I tender that, your Honour.

PN11586

JUSTICE ROSS: I'll mark that Exhibit UB25.

**EXHIBIT #UV25 REPORT OF PROFESSOR J.I. BORLAND DATED
03/09/15**

PN11587

MR DOWLING: Could I tell you, Professor Borland, the folder you have in front of you, behind Tab 1, it has the report by Professor Lewis?---Yes.

PN11588

Is that the report to which you reply?---Yes, it looks like it.

PN11589

Behind the very last tab, Tab 6, you'll see a further report and that is headed "Penalty Rates in the Retail Café and Restaurant and Hairdressing and Beauty Industries, a reply to the report by Professor Jeff Borland of 3 September 2015." Do you have that document?---Yes.

PN11590

Have you seen that document before?---Yes.

PN11591

Your Honour, again with leave, there are just nine matters that I wish to take Professor Borland to on the same basis.

PN11592

MR IZZO: No objection.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11593

MR DOWLING: Professor Borland, if I could ask you to go to that part of that report that sets out your paragraph 8. It is the fourth page of the report?---Yes.

PN11594

You will see there your paragraph 8 begins, "Professor Lewis presents two main types of evidence on the elasticity of employment to a change in wages." Do you see that?---I do.

PN11595

Have you read the reply that Professor Lewis sets out beneath that paragraph?---I have.

PN11596

What do you say in response to that?---Well, I think the comments Professor Lewis has provided there go to the issue of determining the total effect of a wage change on employment, on the numbers employed. I guess we think of that as being the multiple of a percentage change in employment and the number of workers who are affected by the wage change.

PN11597

So I think one thing Professor Lewis is saying in that statement is that, for example, if there was a wage change that led to a 10 per cent change in employment, if there was 100 workers affected by that wage change, then the effect is going to be plus or minus 10 workers. But if there's a thousand workers affected then it's going to be plus or minus 100, and I agree with what I understand him to be saying in that regard.

PN11598

The part I disagree is where he says that, rather, the estimates of elasticities from minimum wage studies which are relevant. That pertains to the part of the formula which is to do with the percentage change in employment when you have a wage change. The percentage change in employment when you have a wage change is equal to the percentage change in the wage multiplied by the elasticity of employment with respect to the wage change.

PN11599

In my report I guess I'd argued that for understanding what the appropriate wage elasticity of employment was for thinking about penalty rates it was not relevant to rely on minimum wage elasticity estimates. The reason for that is that my argument is that wage elasticities are always context dependent. Wage elasticity isn't constituted by scale effects and substitution effects, both scale and substitution effects are always context dependent.

PN11600

For example, if we think of capital labour substitution, if we think at the moment of a personal care worker in an aged care home we don't think there's particularly large opportunities for substituting their work with capital. Whereas if we think of a numerical clerk we think of there being a large opportunity of substituting their work with computer-based capital.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11601

So when we looked at those two jobs we think that there were very different substitution effects and, other things equal, there'd be different wage elasticities. I make - - -

PN11602

JUSTICE ROSS: We just need to get the link back.

PN11603

MR GOTTING: Your Honour, it's Gotting in Sydney. We can see the witness and we can see a person in Canberra but, regrettably, we cannot see the Bench.

PN11604

JUSTICE ROSS: As long as you're able to get over your disappointment Mr Gotting.

PN11605

MR GOTTING: We are happy to keep going, your Honour.

PN11606

JUSTICE ROSS: All right, we'll proceed.

PN11607

MR GOTTING: But, in fairness to the witness and to everyone else, we've probably lost the last five minutes.

PN11608

JUSTICE ROSS: We haven't been saying anything, Mr Gotting, we've just been trying to re-establish the link.

PN11609

MR GOTTING: Thank you.

PN11610

MR DOWLING: Sorry, Professor Borland. I'm not sure the point at which - whether you can recall the point at which you were at?---Where I was up to was making the point that similarly the minimum wage - the wage elasticity for changes in the minimum wage, and the wage elasticity for changes in penalty rates, are both context dependent, they're different types of wage changes, they affect different groups of workers.

PN11611

The fact that they're both regulated wage changes is irrelevant. What matters is the type of wage change and the group of workers affected. So I disagree with Professor Lewis's response that a wage elasticity is a wage elasticity.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11612

Can I ask you to turn ahead in that document, Professor Lewis's reply to you, to the page where your paragraph 22 is set out, and your paragraph 22 commences,

"First, penalty rates are not entirely a regulatory addition to labour costs." Do you have that paragraph?---I do.

PN11613

Have you seen the response of Professor Lewis that appears beneath that paragraph?---I have.

PN11614

What do you say in response to that?---Well, the point I was making in my report there is that Professor Lewis in his original report, in the simulation exercise that he undertakes, he assumes that a \$1 change, increase, decrease, in penalty rates would feed through exactly to a \$1 change in wages of workers. For example, if you were to remove penalty rates, if that was a 50 per cent rate, he assumes in his approach that that would reduce wages paid to workers by 50 per cent.

PN11615

I made the point that Professor Lewis himself - I think on page 39 of his original report - acknowledges that some part of the penalty rate component is necessary compensation to workers to induce them to be willing to work on the days when penalty rates apply. So, it's impossible to think that if you, for example, doing the exercise Professor Lewis is doing, remove penalty rates completely that wages would fall by the full amount of the penalty rates, that wages would only fall as far as the willingness to work of the marginal worker, you would get to a new equilibrium market wage long before you got rid of all of the penalty rate component. So, therefore, because Professor Lewis is assuming in his exercise that you get rid of the whole of penalty rates, yet my argument was that his over-estimating the wage effect of removing penalty rates.

PN11616

In his response, I think in the first paragraph, he basically agrees with me, he agrees that some part of the penalty rates is representing an amount that you'd need to compensate workers. In the second paragraph he says that, well, it's okay, there's a whole lot of people who are unemployed and they are going to be willing to work for lower rates and that means that what I've done is okay.

PN11617

I guess Professor Lewis hasn't presented any evidence about the rates at which unemployed people would be willing to work on these days and, for his argument to be valid, those people would have to have completely different, for example, willingness to pay than the workers in the industry at the moment who were surveyed by Professor Rose. You would have to think the unemployed population that Professor Lewis refers to there had completely different willingness to pay than the rest of the population for his argument to be valid.

PN11618

So I don't believe that Professor Lewis has refuted the point that I made, which was that by assuming that if you remove penalty rates you reduce wages by the same amount that that over-estimates the true wage change that you'd get.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11619

MR DOWLING: Thank you, Professor Borland. Could I ask you to turn two pages on to where your paragraph 26 appears at the bottom of the page? Do you see that, it's under the heading "Assumption 2" and your paragraph 26 commences, "In my opinion the main issue in the specific assumption that the firm is operating for a single time period," do you see that?---I do.

PN11620

You'll see over the page at the conclusion of that paragraph Professor Lewis sets out a response in bold red beginning, "A firm's decision," do you see that?---I do.

PN11621

Have you read that response?---I have.

PN11622

What do you say in response to it?---Well, I think the issue here, and in sort of the immediately following pages of Professor Lewis's report, goes to the general issue of whether when you try to understand the effect of penalty rates on labour demand, whether it makes sense to do that in a model where you think of the economy just operating for sort of one day, or whether you believe it's more appropriate to have a model of the economy where you think of there being multiple days, and one of those days you've got penalty rates as a premium to the base wage and on the other day, for example, you've got just the base rate being paid.

PN11623

The particular issue that's been taken up here is with reference to the capital labour substitution, to what extent, because of penalty rates, will a business decide to substitute capital for labour to replace capital - replace labour with capital because of penalty rates. My argument is that when a firm - an economist would think of this issue in the following way: that when a firm decides on purchasing capital that capital is available to the business on every day that the business operates.

PN11624

Therefore, the way a business is going to think of that decision is they are going to think, well look, if I buy the capital that will cost me a particular amount but I'm going to save money on the labour that's substituted for by that capital across seven days of the week, because I've got capital that's available now to be used for seven days of the week.

PN11625

With respect to penalty rates, then, what's the effect of penalty rates on the incentive of business to substitute capital for labour, the question then becomes what's the effect of penalty rates on the average cost of labour across the whole week? Because when you're thinking about substituting capital it's the cost across the whole week that matters.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11626

So the point I was making was that I think the approach Professor Lewis uses is problematic because he takes a one day view of the labour market, and when you are doing that you are basically assuming that there is some penalty rate change and that change is applying to every hour of labour, that's every hour of labour that's worked.

PN11627

When you take the sort of multiple day approach you're saying, look, there are penalty rates, they apply on one day. But to work out the effect with respect to the average cost of labour you need to average that across the whole week, and that average effect is always going to be smaller than if you assume that it's every day of the week that it's applying.

PN11628

I think when Professor Lewis responds to this point his response, I think, misses the point because he talks about law of diminishing returns. But law of diminishing returns is a concept which applies when the amount of capital is fixed. So law of diminishing returns in economics is the question of if the amount of capital is fixed how much extra output is added by adding extra workers. But it's all about capital being fixed.

PN11629

But the question here about substitution effects is not at all holding capital fixed, it's about are you going to substitute capital for labour, are you going to change the amount of capital? So I don't believe Professor Lewis in his response has really come to grips with the key issue I was raising, which is that when you think about capital labour substitution that's a decision that is made on the basis of average labour costs over the week, compared to the cost of buying the capital.

PN11630

So penalty rates, you need to divide the penalty rates over the whole week to think about what the effect is on the incentives to substitute capital, but that doesn't happen when you use the one day approach that Professor Lewis uses.

PN11631

Thank you, Professor Borland. Could I ask you to turn the page to paragraph 29, your paragraph commencing, "First, I consider the substitution of paid labour with capital." Tell me if you haven't already deal with this?---That is what I've been - I've kind of dealt with those two points together because I think they go to the same point.

PN11632

Can I ask you to turn ahead to where your paragraph 33 appears. It's under the heading, "Scale effect" at the bottom of the page several pages on. Do you see your paragraph 33 commencing, "Consider the example of removing or reducing penalty rates," do you see that?---Yes, I do.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11633

Have you seen over the page the response to that that begins, "Monopolistic competition is a market structure," do you see that?---I have.

PN11634

Have you read Professor Lewis's response?---I have.

PN11635

What do you say to it?---I guess Professor Lewis is, most of his response there, is about sort of what type of industry it's appropriate to regard this industry as. I guess I was - I think I was trying to make a simpler point which was just that the simulation approach that Professor Lewis uses assumes that the product market in which producers operate is perfectly competitive.

PN11636

In that type of market - so that's a theoretical construct that economists use to think of a market type that's sort of ultra - the most competitive you could possibly have. In that type of market structure whenever there is, for example, reduction in costs that always gets passed on completely to consumers in prices. You know, that's the idea of it being ultra-competitive. If one firm doesn't pass on all of the decrease in costs then another firm can undercut it and attract all of the business.

PN11637

So in a perfectly competitive market any cost decrease is always going to get passed on completely to consumers because you're assuming this ultra-competitive market. My point was to say, look, this market is not perfectly competitive. We can argue about sort of where on the scale of competition it lies but clearly there's product differentiation. As soon as you move away from perfect competition then it doesn't follow that any cost decrease will be completely passed on to consumers, because you've got a less competitive market structure.

PN11638

So there's not the same impetus to pass on all the costs. You don't have the same competition driving price down. That really matters because that's at the heart of the scale effects which are part of the wage elasticity. The scale effect is the idea that if you have a decrease in wages that reduces costs, that allows firms to reduce prices, that leads to an increase in demand for the output being sold, that is the scale effect. When you assume a perfectly competitive market structure you really - you know, you're assuming the maximum reduction in prices in that sale effect. So my point, you know, wasn't to argue about whether monopolistic competition - where these industries exactly are on the spectrum, it was to say look, as soon as you move a bit away from that, then you're going to get a smaller scale effect than the effect that's implicit in the approach Professor Willis uses.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11639

Thank you, Professor Borland. Could I just ask you to turn over two pages until you come to your paragraph 34, that's the paragraph beginning, "The second

effect is on the demand for output due to a decrease in price”. Do you see that?---Yes.

PN11640

And over the page is the response of Professor Lewis beginning, “Professor Borland suggested any decrease on the wage rate on Sundays and public holidays would result in price falls”. Do you see that?---I do.

PN11641

Have you seen and read that reply of Professor Lewis?---I have.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11642

And what do you say in answer to it?---Well, I think there’s three points sort of in that reply. And so to take them in order of importance, which kind of to take the second point first, one of the points I was making was to point out that the employment change estimates that Professor Lewis produces are what an economist would call partial equilibrium. They’re just telling you the effect on the retail sector or on the restaurant and café sector. That is not the total effect on employment in the Australian economy because we’d always expect that if people are spending more in restaurants and cafes, for example, then they’re going to be, to some extent, reducing expenditure on other items. So for example, you know, if you think that reducing penalty rates means prices fall a bit and so people, you know, go out for an extra sort of meal at a restaurant or café on Sunday, then what that probably means is that, you know, they’re not buying as much fruit and vegetables or meat to cook their own meals on Sunday. So, you know, you might get an increase in employment in the restaurant and café sector, which is what Professor Lewis is estimating, but there’s going to be some decrease in employment, for example, in the local green grocers or local butcher shop because people are substituting restaurant expenditure, for example, making their own meals. So I guess I was just pointing out that it’s important to understand that these are employment estimates with respect to particular industries, not the effect on the overall Australian economy. And I think Professor Lewis basically agrees with me on that point and says that the appropriate way to analyse that would be a general equilibrium model which, I think, is what most economists would think. The second point there is to do with the issue of demand shifting. So that was the idea that look, maybe if you believe that an effect of the penalty rate regulations is that a restaurant or café doesn’t open on a particular day, then if you have a one day model of the economy, as Professor Lewis does, there’s basically – that’s it - if you close the business, then that’s it, you can’t go to that business. But, in fact, the reality is, and this is another reason for why I think it’s appropriate to think of a multiple day model, you know, potentially, if you don’t go on the Sunday because it’s closed, you can go on another day. Now, Professor Lewis says we don’t present any sort of empirical evidence on the extent of that demand shifting, and that’s exactly true. Neither of us have any evidence to present on that. But the important point is that with his approach, there’s absolutely no scope for demand shifting to occur. You know, if you believe that there is any demand shifting happening, then that’s only going to reduce the effect that Professor Lewis estimates, because his approach isn’t allowing for any demand shifting. The third issue, which is sort of the first issue he discusses, is to do with the issue

of whether, if there's a reduction in costs, the price changes would be all on the day that the penalty rates were reduced, or they'd be spread across the week. I think we're actually in agreement there. You know, neither of us has evidence about whether they would be spread across the week or whether they'd be concentrated on one day. But in fact, my point was to say that look, if they are spread across the week, then it's important to take that account in estimating the employment benefits of reducing penalty rates. If they're spread across the week, you really need to, you know – then the employer – if a reduction in costs causes a price decrease, but that price decrease is spread across the week, then you've got to think of the employment benefits of that coming from the whole week. So I don't think we're really in disagreement. We're both saying, look, you've got to measure the employment effects appropriately.

PN11643

Thank you, Professor Borland. If I could ask you to turn over three pages until you come to your paragraph 39. That's your paragraph commencing, "To illustrate this point, consider two examples"?---Yes.

PN11644

And you'll see the response below that. Have you read that response?---I have.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11645

What do you say in response to that?---Well, you know, I have two responses. So what we're talking about here is that the percentage change in employment equals the percentage change in the wage multiplied by the elasticity of labour demand. And so the first point I want to make is that what I was wanting to point out in my original report is that, you know, there are different ways to calculate that percentage, that percentage wage change. That the percentage wage change is always like the change in the wage divided by some, let's call it starting wage say. Now, so for example, as I talk about in my report, suppose you think the base wage is 100, the penalty rate is 100, so the overall wage is 200. You know, there's for example two ways then that you could calculate that percentage change. You could say look, the wage change, because of penalty rates, is 100 because we're assuming the penalty rates are 100. Then you could use, sort of as the starting wage, the actual base wage. So then it would be like 100 divided by 100, so you'd increase – you'd change the wage of 100 per cent. But the other thing you could do is you could treat the \$200, the base rate plus the penalty rate, as the starting wage, and arguably, that's the more appropriate thing to do if you're thinking that you're removing the penalty rates. If you do that, 100 divided by 200 is only 50 per cent. So when you do it one way, you get 100 per cent as the change in wage. When you do it the other way, you get 50 per cent as the change in the wage. So what I wanted to do in my report was to point out that first of all, there is this sensitivity. It doesn't exist if you have really small changes. If it was like \$100 and the penalty rate was one, the it's a tiny difference, depending on which way you do it. But with big changes that we're talking about there, it really matters. So first of all, I wanted to point that out. Secondly, I wanted to point out that Professor Lewis had used an approach by assuming that the penalty rates were being imposed, that gives the biggest possible percentage change in wages. If you choose as your starting wage, the

wage before penalty rates, then you're putting the smallest possible number in the denominator, so you're always going to get the biggest percentage, the biggest percentage change. So I was trying to illustrate that look, you know, if you go to the other extreme of assuming that it's the biggest possible number, then it really, really matters to the employment effects that Professor Lewis estimates. In his response, Professor Lewis says that we should use the – he acknowledges, I think, that he says the problem of interpretation of elasticity is well-known, so I believe he's acknowledging the point that I made, that there is this sensitivity, and he argues that the mid-point formula is the appropriate approach. And it is very important to say that, even with this mid-point approach, you still get - Professor Lewis' estimates in his report, are still substantially higher than you get using the mid-point. As he illustrates in his response, if you look at the Sunday penalty rates, if you use the mid-point approach rather than his approach, you reduce the estimates by a factor of one-fifth. So basically, Professor Lewis is saying look, if you use the – you should use the mid-point approach. And what follows from that is that you need to reduce every one of his numbers in table 4A and 4B that relates to Sunday penalty rates by a factor of one-fifth, if you're going to shift to the mid-point formula. What Professor Lewis doesn't do in his response is talk about the public holiday example. There, I've worked that out, and if you go to the mid-point, it turns out that the midpoint, you actually need to reduce the estimates in his table 4A and 4B by about 45 per cent, or about 9/20th. So you'd want to take every number in his report for public holidays, and even if you believed – even if you put aside all the other criticisms we've made - just on this one point alone, you would want to reduce all the public holiday numbers by 9/20ths. Saying that the mid-point formula is the approach we should be doing is not really getting in any way away from the fact that by using what I called upper bound approach, he has substantially overestimated sort of what I think a reasonable interpretation of the employment effects would be. The other thing to note, which he doesn't really reply to here, is his exercise, it's important to remember, is an exercise he does where he assumes the penalty rates are completely being removed. My understanding is that's not what is under consideration here, so you would then need to tailor those results in table 4(a) and 4(b) to take account of the fact that the scenario under consideration here is different to the scenario he has considered, which is complete removal of penalty rates if you wanted to get the employment effects.

PN11646

Professor Borland, can I ask you to turn a number of pages ahead until you come to your paragraph 53. It's the paragraph that commences, "Third, it follows that the conclusions reached by Prof Lewis are incorrect." Do you see that?---I do.

PN11647

You'll see over the page, Prof Lewis responds to that by saying, "It make sense to work with the average value of wages workers are willing to accept"?---I do.

PN11648

Have you read that response?---I have.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11649

What do you say in answer to it?---I disagree with that. I think, you know, if you have two things - if you first of all have heterogeneity in the amounts that individual workers need to be paid to be, you know, willing to say work on Sunday and if you think what economists call the law of one price holds, which is basically the idea that you've got to pay, you know, a common wage to everyone, then it absolutely follows that the relevant wage is the wage that you need to pay to attract the marginal worker rather than the average worker. I guess I tried to explain that with the numerical example in my report; that if you've got five workers who need to be paid - say one of them needs to be paid \$1 an hour, another one \$2 an hour, another one \$3, another one \$4 an hour, another one \$5 an hour, if you take the average wage of \$3, then you don't get five workers working for you for \$3 because two of the workers need to be paid \$4 and \$5. If you want to have five workers working for you, you need to pay a wage of \$5 so that the wage is above the wage that all the five workers are willing to work at. So we call that worker who needs to be paid \$5 the marginal worker; the last worker hired, the worker who has the highest amount they need to be paid. In a world where there is a common wage for everyone, determines the wage rate. That's just standard in the way we think about sort of labour markets operating in any sort of textbook. I mean, for Prof Lewis to say that the average is relevant, I don't think it is relevant. He says obviously some workers would require more, others work less, but the point is that you can't pay more or less to different workers. You can't tailor the wage exactly to the willingness - to the wage that every worker is willing to work at. As soon as you're in that situation, you really need to look at the wage that the marginal worker is willing to work at. I think, you know, what was really necessary here is to present say evidence on the distribution of the amounts that workers were willing to work at from Prof Rose's report and then look at, you know, what is the wage that that highest group of workers are willing to work at, because that would give you a much more appropriate indicator of what the wage necessary to attract the current workforce into the sector is.

PN11650

Thank you. Just one last matter. If you would turn to the very front of Prof Lewis's reply to your report, you will see there the last paragraph appearing on page 2. Prof Lewis there says:

PN11651

I have reproduced substantive parts of Prof Borland's report in full, with my responses to his comments in red bold type. I note that although Prof Borland's report purports to cover retail, cafe and restaurant, hairdressing and beauty industry, his report relates almost entirely to the cafe and restaurant industries.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11652

What do you say about the application of the matters you've just discussed in your evidence today to other industries?---Well, yes, I think the points I'm making are really generic points. None of them were specifically about the restaurant and cafe sector. For example, my point about Prof Lewis's approach of, you know, starting with the before penalty rate wage as the way of calculating the percentage change in wages, that applies equally to his calculations for the retail sector. It

applies equally to, you know, all the cases he considers. All the points that I make to do with the relevance of the minimum wage literature, to do with the appropriateness of thinking about penalty rates in the context of a multiple day model, the criticism of too high an estimate of the percentage change in wages and the criticism of his use of the Rose report, the same points apply absolutely equally to any of the sectors that are considered in his report.

PN11653

Thank you, Professor Borland.

PN11654

CROSS-EXAMINATION/MR IZZO/05:16 PM

PN11655

MR IZZO: Professor, you've got a copy of your report in front of you. If I could ask you to go to paragraph 9 of your report, please. It's at tab 5?---Yes.

PN11656

If I could ask you to read paragraph 9 or at least familiarise yourself with its content. In that paragraph, you draw a distinction between the application of minimum wages and the application of penalty rates. If you go to the top of page 6 of your report, you say that:

PN11657

The minimum wage must be paid on all days, but it only really applies to a subset of workers who would have otherwise earned less than the minimum.

PN11658

I take it you're saying the minimum wage is only really relevant for those people in the industry who would otherwise not have been paid the minimum wage; so the lowest paid in the industry. Is that right?---I guess I'm saying two things there. First of all, I'm saying that this is a wage change that for that group of workers applies to every hour they work; every hour they work across every one of the seven days that they could work on. Yes, I'm also saying that it applies to a particular group of workers whose wages are - for whom the minimum is binding or that is the way that they obtain wage - that's the way their wages are set.

PN11659

I take it that what you're saying is an increase in the minimum wage won't affect everyone in the industry. It's only going to affect those that are on the minimum wage?---That's right. Usually we would think that a change in the minimum wage - the effect of that is going to be, you know, primarily on the workers who are currently on the minimum wage or workers whose wage was sort of between the minimum wage and what the new minimum wages is.

*** JEFFREY IAN BORLAND

XN MR DOWLING

PN11660

Whereas you say penalty rates apply to everyone and therefore you draw a distinction between the two?---Again I guess I make two points, sort of. I say that, first of all, penalty rates only apply on particular days and, secondly, I say

that, yes, penalty rates apply again to a particular group of workers; like groups of workers who are covered by awards, agreements, that specify those penalty rates.

PN11661

I had understood you to be saying that penalty rates apply to all workers that are covered by the award or that work in the industry. Is that not what you're saying?---What I'm saying is that the populations are different. The populations are different, sort of. The penalty rates that - yes, you could be - I guess what I'm saying is you can be earning above them, you know, you can be earning above the minimum wage and you're going to be eligible for penalty rates, sort of. That's what I was meaning, that there's workers who are eligible to receive penalty rates who aren't workers whose base wage rate is directly affected, say, by, you know, the national minimum wage.

PN11662

At the bottom of page 5 you say penalty wages are an extra wage payment; their paid only on specific days is the first point you've already alluded to?---Yes.

PN11663

You say is paid to all workers covered by awards with penalty wage provisions, so I understood your position to be that the penalty rates are paid to all workers covered the awards. Is that the position that you still hold today?---Well, I guess the point I was making was that there's a more universal application of penalty rates, the more universal - - -

PN11664

Than the minimum wage?---Yes.

PN11665

You accept that not all workers covered by awards necessarily receive penalty rates though?---Yes, I guess the point I was trying to make was that there's a more universal - that there's a difference in the population, that there's, for example, a more universal coverage of penalty rates.

PN11666

And I understand that's the point you're trying to make, but if I can just ask you to answer the question, only because it will shorten the process. You accept that not all workers covered by awards in the industry receive penalty rate payments for weekends?

PN11667

MR DOWLING: I'm not sure if the question's very clear in the context of what it is Prof Borland has said, that all workers covered by awards with penalty wage provisions is the evidence?

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11668

MR IZZO: I'm happy to re-phrase the question. My question to the professor now is whether he accepts that there are people covered by the awards who do not receive penalty rate payments. That's the question that's being asked. I'm not sure how there's any unfairness in that here that agrees with the proposition or

disagrees?---Let me say, the point I was trying to make is the point that I said to you. If I haven't sort of expressed that precisely enough, because the fact of the matter is that there's awards with penalty wage provisions where some workers sort of aren't getting penalty rates, then that's fine; I guess the point I was trying to make was just that there's a completely different group of workers who are covered by, you know, penalty rates, the minimum wages.

PN11669

Are you aware, for instance, that the restaurant industry award has a provision which allows employers to pay 25 per cent above the minimum wage and therefore not specifically pay penalty rates on weekend days, provided that at the end of the year the employee's no worse off over an aggregate period, but that there is no requirement to pay the penalty rate to employees where there being paid 25 per cent greater than the minimum wage?---That's the idea of annualisation.

PN11670

Yes.---Yes, I've heard of that.

PN11671

Right, and even if it's not in the award, are you aware that some employers may adopt their own offsetting arrangements where they pay above the minimum award wage during the week so as to pay someone a flat rate throughout the whole week, and they don't necessarily pay penalty rates on the Saturday or the Sunday?---Well I'm not directly aware of that.

PN11672

Right, okay, thank you. So the point that I'd just like to test with you, Professor, is that it's not the case, is it, that penalty rate payments have a universal application in the industry or to employers covered by the awards?---Well, yes, you've given the example of annualisation, but I think, to be frank, it's irrelevant to the main point that I was trying to make there. The main point I'm making is that wage elasticities are context-dependant. That context is the type of wage, you know, change that you're talking about, and the group of workers who are being affected. Now, I think, you know, we can both agree, whether I've sort of misstated it being universal or not, that the minimum wage example, it's a completely different group of workers who are affected than the group of workers who are affected at penalty rates. Unless you have evidence to tell me that it just so happens that the group of workers who are on these annualisation arrangements, sort of, gets rid all of the workers in that industry, except the ones who are on the minimum wage, then my point still holds, which is that they're different populations of workers.

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11673

But you draw two distinctions, and one of the distinctions is that minimum wages only apply to a subset of the industry, whereas penalty wages apply to everyone in the industry. That distinction, I'm putting to you, doesn't really hold firm?---Well, yes, what I said is that - the point I was trying to make there is that there are different populations affected by them. You're saying that I was wrong to state it

as universal, and I'm willing to agree with that, but it doesn't change the main point which I'm making, which is that, as I said, unless you can demonstrate that what you're talking about gets rid of every worker except the minimum wage workers who have to be getting paid penalty rates, then my point holds.

PN11674

Right, thank you. If I can take you to paragraph 12 of your statement, which is on page 6, you commence a discussion about the impact of increases in minimum wages on employment. Do I take it that you accept that an increase in the minimum wage will have some impact on employment?---Well, paragraph 12 is actually about aggregate wage elasticity studies. Paragraph 12 is the first type of evidence that Prof Lewis cites, which is about, you know, macro level, the effect of the average wage on aggregate employment, so that's a different type of evidence. I think in paragraph 13 that's where I start to talk about the minimum wage studies.

PN11675

Do you accept that an increase in the minimum wage has some impact on employment?---I think we don't in Australia have a very good sort of evidentiary base to establish sort of what the employment effect of a minimum wage is. I think, you know, there are great difficulties in establishing that in Australia, so, yes, we think that - you know, all the theory tells us that when you have an increase in wages there's a negative relationship with employment, but the key issue of course is always what's the size of the effect sort of; that's what really matters, and I guess the big issue in Australia is that we just never really sort of had the complexity of the system, and the difficulties with data have meant that there's always been problems in getting, like, anywhere near as precise evidence as I think there is for example in the United States on minimum wage elasticities.

PN11676

Do I take it from you've said that you accept that if there is an increase in the minimum wage which is more than moderate or more than appropriate, and I use those terms because I see them a lot in literature, if there's an increase in the minimum wage that's more than moderate or appropriate that that might then start to have a substantive disemployment effect?---No, I think the word substantive goes to the issue that I said, which is we don't have a strong sense of what the wage elasticity of employment is, so, you know, it's always the interaction of the size of the wage change and the size of the wage elasticity that matters.

PN11677

I'd like to show you a document, Professor, that talks about this. I'm not going to ask you to read the whole document. (Pause/Asides) Professor, if I could please take you to page 17 of – firstly, can I just ask you, this document, it's titled OECD Employment Outlook 2015, do you recognise what this is?---I do, in fact I've read a couple of chapters on it already.

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11678

Thank you, and I take it it's the published views of the OECD, is that your understanding?---Well it's the published views of the staff who work I guess in the

employment secretariat there. The different chapters are basically done by individual people within the OECD, sort of, and they take responsibility for the section, although obviously there's collective oversight by a director of the employment section about what ends up being published.

PN11679

But you understand it to be the official position of the OECD is what's reflected in this report, I take it?--Yes, it reflects sort of a combination of the views of the staff who complete the particular chapters and that sort of being refereed by the director of their section, so to the extent that the director of the – you know, I've never been privy to the process - but to the extent that the director of the section is putting in what the view of the OECD is, I mean, yes. To say that there's an OECD view, I think, is probably a bit problematic as well. There's a lot of, if you meet people from the OECD, a lot of diverse views about sort of particular policy issues and that as well, so I think this reflects the views of the people in the OECD who compile them, you know, some of whom are quite senior.

PN11680

Certainly, that's set out on page 3. If I can take you to page 17, there's a reference to – the heading is: Minimum wages must be closely coordinated with tax benefit policies, is actually the heading, but then I'd like to take you to the second sentence. It says:

PN11681

Minimum wages can help underpin the income of low paid workers but this is conditional on two point factors. First, they should not be set too high, otherwise they can lead to job loss and loss of income for low paid workers.

PN11682

So I'd just like to direct your attention to that. I'm going to show you a couple of passages, and then I'll ask you a question, Professor. If I could now take you to page 21 and the last bullet point:

PN11683

At reasonable levels, increases in the minimum wage are unlikely to cause substantial job loss.

PN11684

Then if I can take you to page 46 of the report, there's a heading called Minimum Wages and Employment. Do you have that there?--Yes.

PN11685

In the first paragraph under that heading in the last sentence, it says:

PN11686

When assessing the employment effects of minimum wages it is important to stress first that the potential employment effect may well depend on the level and expected increase.

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11687

They're the passages I effectively want to draw your attention to.

PN11688

JUSTICE ROSS: Sorry, can you just take me to where the last one appears?

PN11689

MR IZZO: Sorry, so, your Honour, page 46, it's the beginning of the last sentence of the first paragraph under Minimum Wages and Employment: "When assessing the employment effects on minimum wages."

PN11690

JUSTICE ROSS: Yes.

PN11691

MR IZZO: What I want to put to you, Professor, is that the OECD report seems to be saying that there will be a small impact on unemployment by minimum wage increases provided that the increases are kept to a moderate, reasonable or appropriate level. Do you accept that?---I think all this is saying is that, like, if you read Prof Lewis's report and my report, what we say is that the percentage change in employment depends on the percentage change in the wage and the wage elasticity. What the OECD is saying is that the percentage change in employment depends on the size of the wage change. That's all it's -- like, yes, you don't need to look at OECD report to know that the higher the change in the wage the bigger the employment change, that's just there in the basic formula that both Prof Lewis and I used.

PN11692

So if there is a substantial increase in the wage then it is likely that there will be a disemployment effect that might be more than small?---But again it depends on the wage elasticity. It's the interaction of the size of the change in the wage and the employment elasticity that determines the percentage change in employment, but, holding constant, the wage elasticity, it's true, the bigger the employment change the bigger the percentage change is, but, you know, whether that's substantial or not, it depends on the interaction with the elasticity.

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11693

And noting your caveat, it depends on the interaction with elasticity, I take it that the bigger the increase the more potential there is for a disemployment effect?---Yes, I mean, I've written that formula several times in my report so I would be denying basic waiver economics if I wasn't to say that, you know, the formula's there, the percentage change in employment equals the percentage change in the wage times the elasticity. If you have a bigger wage change then there's going to be a bigger change on employment. Whether that's substantial or not depends on the elasticity, and, you know, that's where the action is in terms of thinking about -- I don't think there's any labour economist in the whole world who'd deny that the bigger the wage change -- you know, where the action is is, like, what's the elasticity, sort of, and, you know, that's where the action is in the minimum wage, but that's also where the action is in my report in terms of arguing

that minimum wage elasticities aren't relevant because they're different to the elasticity you'd expect from penalty rates.

PN11694

Okay, thank you. At paragraph 15, you talk about – we were talking about elasticities there – and you talk about finding of Lees – sorry, when I say paragraph 15, that's of your report on page 8.---Yes, sure.

PN11695

You talk about Lee's findings and that those findings about the level of elasticity - or the effect of the increase in the minimum wage on employment was subject to some scepticism by Newmark and Wascher – and I assume it's Wascher – in 2006? Newmark and Wascher, I understand, are advocates of a effectively economic theory that says that increases in minimum wage do have disemployment effects; that's their broad position in the debate, would you agree with that?---Yes, Newmark and Wascher I guess, you know, are regarded as two people who have argued for negative effects of minimum wage, but I actually think if you look at the US literature these days there's a diminishing gap between them and other sort of economists who are working on minimum wage effects, so I think there's a lot more consensus than there used to be in the early 1990s, so they're not kind of out there in any way.

PN11696

Okay, thank you, if I can ask you another question then? In terms of your reference to them then, the sole purpose of you referring to them is to cause some doubt on the level of elasticity expressed by Lee?---Yes, that's right, I guess, you know, I'm making two points in my report. In one point is that minimum wage elasticities are not relevant to thinking about the effects of penalty rates. The other point I make is that, regrettably, and, yes, it's not a criticism of the author sort of; like I said, it comes back to the complexity of the Australian system and the data limitations we have. I just don't think we've been able to do good studies of what the effect of the minimum wage are on employment here.

PN11697

Would you accept that the general thesis that is posited by Newmark and Wascher in their 2006 report is somewhat at odds with some of the views that you're expressing in your own report here?---As far as I know, Newmark and Wascher may be, yes. I'm not sure that they've worked on penalty rates. I mean, Newmark and Wascher are known for their work on minimum wages. I guess I keep saying that I don't see a discussion of minimum wage elasticities as being relevant to this case, and I'd explain that I think that's because it's a completely different context. You have different substitution effects, you have different scale effects, so I don't see myself expressing a view that really sort of overlaps with Newmark and Wascher because we're in different spaces.

PN11698

If I can now ask you, you talk at paragraph 24 - towards the bottom of paragraph 24 on page 12 - you talk about the regulatory effects of penalty rates. Specifically you say in the last third of that paragraph:

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11699

To the extent that firms are able to offset regulatory effects of penalty rates, this will reduce the extent to which reducing or removing penalty rates will reduce labour costs for firms.

PN11700

---Yes.

PN11701

Do you accept that if an employee's engaged at the minimum award levels then there is no ability to offset the effects of penalty rates?---Well there's no scope to offset the effect of penalty rates through adjusting downward the base wage, the base wage they're being paid; you know, the effects would be through changes in work effort or, you know, those elements.

PN11702

Changes in the work sorry?---Work effort, you know, changes in work effort, changes in unpaid time sort of, stuff like that, but no, I accept what you're saying, and it is important to say with respect to this point that I wasn't – and I think I'm very careful in the way I sort of state this; like I say, I present for example these data not to claim that there has definitely been downward adjustment in the base rate of pay due to penalty rates, but instead to show that there is sufficient flexibility in wages in the industry, certainly these days, for that adjustment to occur. So, yes, I agree completely that I haven't, because I say it there, that I haven't proved that there's been downward adjustment in base rates or anything like that. I'm raising that as a potential limitation of Prof Lewis's report that he didn't mention. I'm saying, look, the best I can do is present these data on the ordinary time earnings in the restaurant café industry to show that there seems to be flexibility in relative earnings between industries, certainly relative earnings in this industry, but I'm not claiming that I have evidence that there's been downward adjustment in base wages.

PN11703

And that's because, if we turn the page, because you've got your graphs there which show the average weekly earnings in the accommodation and food services industry compared to all industries.---Yes.

PN11704

You accept that it's possible that the reason for this downward trend is simply because the other industries are providing employers with increases to their wage rates that are beyond, say, the annual wage reviews, et cetera? There are broader levels of the increase in the other industries than there is in the restaurant industry; that could be an explanation for that trend you see there?---It could be, but in fact that would fit the argument that I'm making because of course these workers in the restaurant café industry are mobile, they can work in other sectors as well, so if other sectors are getting an adjustment upwards in their base and the base rate of these workers is just staying the same, then in effect that is - you know, it's a downward adjustment in the relative base rate that you're getting.

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11705

Not a downward adjustment in real wages they experience?---No, in relative – yes, in relative. I mean, the idea is overtime, workers expect to get a higher base rate of pay in line of cost of living increases; if workers in other industries are getting that but these workers aren't then that's a form of downward adjustment in the relative base rate. But yes, I want to say I'm not, like - as I said, I acknowledge that I'm not claiming I've got evidence of that. I'm raising it as a possibility, and saying that the wage flexibility data – I mean, you've just given exactly the reason why I put this data in, which is that the explanation you gave would be perfectly consistent with my explanation that there was this downward adjustment, so that's why I put it in, but I'm not saying I had definite evidence.

PN11706

If there is this downward relative adjustment, that doesn't mean that restaurant operators necessarily have some flexibility about avoiding penalty rate payments; it might be they just simply haven't been able to afford to pay more money to their staff compared to other industries?---Can you say that again?

PN11707

You seem to say that this shows that operators in the accommodation and food services industry have some level of flexibility about how they deal with regulatory effects, but those graphs don't necessarily show that they've got a flexible way of dealing with the regulation of penalty rates; it just shows that they haven't been able to pay as much as the other industries in terms of wage increase?---Well but, yes, one way of dealing with penalty rates is to try and hold down the rate of increase over time in the base wage. You don't have to reduce the base wage, or you don't have to pay less than the regulated base wage to be accommodating penalty rates through the base wage. If you're just not increasing the base wage in the same way that other industries are, then that's a form of accommodation to the penalty rates.

PN11708

If I could take you to paragraph 29 of your statement, which is page 15, you talk about substitution with capital. I take it it's elementary that capital is considered a fixed cost in a business, is that right?---Why, yes – components, yes; components of capital will always be considered fixed costs, yes.

PN11709

Okay, whereas labour is traditionally considered a variable cost, is that right?---Well it depends on the terms under which the labour is hired sort of, like, you know, if I hire you on a 1-year contract or that, then it's fixed for the 1 year sort of, so yes, you can never define what's fixed and variable without looking at the circumstances of the particular industry and labour market, but in the circumstances we're discussing here I was taking the approach that, yes, you want to think of capital as this fixed factor which once you have it you can apply it every day of the week that your business is operating, whereas potentially you have the flexibility to determine how much labour you would want to hire on a day-by-day basis.

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11710

And if once you have an operation that is already ongoing - you're not setting it up - you wish to look to make savings to address varying levels of demand, do you accept it's easier to adjust the variable costs than it is the fixed costs?---Easier to adjust the - - -?

PN11711

Perhaps let me re-phrase that - easier to reduce the variable costs than reduce the fixed costs?---The point is you've got to – that's always sort of with regards to the level of output that you want to produce. You can't just say oh this factor's costing more so I'm going to reduce here but I'm not going to adjust the other factor, because then your output's going to fall. I mean, when we break up into substitution and scale effects, the substitution effect is always holding output constant, so it's like, okay, suppose you knew that this café was going to serve 100 meals a week or something like that, the question that we're asking with the substitution effect is, if you introduce penalty rates or if you change penalty rates by some amount, given that you want to produce 100 meals a week, are penalty rates going to cause you to change the method of producing those 100 meals? Are they going to cause you to use more capital and less labour? So just to say, you know, you're going to change variable, that's the right way to think about substitution effect. The substitution effect is holding output constant. Then we have the scale effect, which is when we say okay now let's think about what the implications of the wage change for the scale of operations are, but you've got to think about the substitution effect holding constant the amount of outcome.

PN11712

So you would say that assuming output is held constant then it would be easier to reduce a fixed cost than to reduce a variable cost, you'd accept that proposition?---No. I mean, it depends on the particular – the technology of the industry sort of. No, the question that's being addressed here is the following: you want to produce, you know, 100 meals a week and you start off with a particular combination of capital, like, I don't know, you know, dishwashers and ovens and stuff like that, and a particular amount of labour. The question that you're asking is, suppose we then, you know, on one day of the week we increase the cost of employing the labour; the question that's being asked here is, is that increase in the cost of labour on one day of the week going to cause you to change the mix of capital or labour you're using; is it going to cause you to substitute between capital and labour? So, I mean, and the reason - you know what, fixed and variable costs that might, you know, in some circumstances it might be okay to later think about it, but here, you know, what we're talking about is Professor Lewis, having done an exercise where he comes up with effects on employment, okay, so the relevant way to think about this is capital labour substitution, because it's if you substitute capital for labour then employment changes, so fixed variable costs - I don't think that's the best way to think about it. The best way to think about it is to what extent are you going to substitute capital for labour if penalty rates change?

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11713

President, I appreciate that that might not be the best way you think we should think about it but I'm attempting to break this down so that we can move through it efficiently. The simple proposition I'm putting to you is that if output remained constant, if output was the same regardless of whether you were using a fixed cost or the variable cost, it would be easier to reduce the variable costs. That is, it would take less time. For instance, with the fixed cost, if it's a lease, if it's a suite of tables and chairs, things like that, you take - - -?---But you can't just – if you're producing efficiently – if you're producing efficiently then you're using just the amount of labour and capital that you need to produce the thousand meals. You can't just say, "I'm going to get rid of the variable factor", sort of, because it's easiest. Because then if you're producing efficiently, you can't produce the hundred meals any more. It's about substituting. It's about changing the labour for capital.

PN11714

I appreciate that's your view but I'm just trying to go to a much simpler question before we look at a broader picture and that is the time it takes or the ease with which you can reduce a fixed cost like a lease or other type – a dishwasher, whatever it is and dishwasher might not be the best example because that's something that can be perhaps more easily reduced, but some of the bigger items of capital. It takes longer to attempt to phase them out or somehow reduce them than labour which might be able to be moved around by an employer on a day to day basis. It's more of a long term proposition. Do you agree with that?---Like I said, it depends on the circumstances. It depends on the type of capital. It depends on, sort of, the conditions under which labour is employed. But you know, like I said, I think it's irrelevant to the point that I'm making in my report. You know, I have followed exactly the approach Professor Lewis followed which was an approach that where you look at the elasticity of employment with respect of wages. That depends on the scale effect, the substitution effect. Those are very precisely, you know, defined and so I think, you know, that's the way to have the discussion because otherwise you're having this discussion which isn't necessarily integrated in with what Professor Lewis has done in his report and with what I wanted to.

PN11715

Do you accept that in a restaurant or a café or a shop there is a minimum level of labour that is inelastic, and I'll just explain. So that is, to open on any particular day there's a minimum level that you just simply can't substitute, whether it's one chef, one retail shop assistant, perhaps one front-of-house staff? There is a minimum level of labour that is inelastic in each of those enterprises?---Yes, I'm not exactly sure about the use of the term "inelastic" but - - -

PN11716

Yes. That's my - - -?---But I agree that at the moment I haven't been to a restaurant or café that's run completely without humans in it so yes, I'd agree that there's - - -

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11717

So there's a point -- -?---Yes. That there's a minimum level of human presence needed in restaurants and cafes at the moment.

PN11718

Now you've talked extensively about the fact that restaurant operators would need to assess the viability of operating hours on an aggregate basis over a whole week, as opposed to on a day to day basis?---Not the -- no, no. That's not -- I mean, what I've said is that they would make the decision of whether to substitute capital for labour on the basis of realising that that capital, if they bought it, could be used across seven days of the week.

PN11719

But you're assuming then that that discussion, if I understand, assumes that the only thing being substituted here is labour for capital. That's the basis upon which you made these comments?---In point 29, that point is entirely about substitution of capital for labour. In point 30 I go on to discuss the substitution of labour for labour, the substitution of unpaid, for example -- well, not paid through the award system and that but the -- the labour of the proprietors or the paid labour who are going to receive penalty rates.

PN11720

When you say that operators are affected, or when one assesses the viability of operating hours on an aggregate basis, that's because you say that capital is assessed on an aggregate basis?---Yes, that a - - -

PN11721

That's why you say that restaurants are not really - - -?---Yes. I am saying that when you think of capital equipment, you know, that that capital equipment, the decision to purchase an item of capital equipment, that that capital equipment then is available to substitute for labour that would have otherwise done those tasks across every day that the restaurant's operating.

PN11722

But do you accept that -- well, I'm going to put two propositions to you. The first one is once the capital investment has been made and there are then fluctuations in demand, that it may not be possible to immediately move the capital and so you'd have to look to substitute with something else whether it be unpaid labour or anything else. It might not be possible to substitute labour with capital?---But that's the wrong thought exercise. The thought -- you're saying, oh, demand changes and that. That's not the thought exercise here. The thought exercise here is the change in penalty rates. The thought exercise here is how does it change in penalty rates? You know, does a change in penalty rates cause restaurants and cafes to substitute from labour towards capital? If you bring in sort of, oh, changes in demand and that, that's completely different. It's outside the scope of what we're considering here.

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11723

Professor, it is relevant and if it wasn't relevant then there'd be an objection to it so I think if you just listen to the question and answer it directly. I understand you're

putting thesis and you've got your view but it's important you answer the question directly that is put to you. So the question being put to you is, if you have a restaurant operation that has established itself, it has made its fixed – its investment, sorry, and capital, if there are fluctuations demands and an operator is attempting to respond to them promptly, it may not be possible to substitute labour with capital and so there will need to be other types of substitution that occur?---Well, what other types of substitution do you mean?

PN11724

Substitution with unpaid labour is an example. Because you can't substitute with the capital?---But why would a change in demand cause you to want to change the method of production, the balance of labour and capital that you're using? Can you give me an example, sort of?

PN11725

Well, it's more for me to ask the questions?---I'm just asking you to clarify it.

PN11726

If there is an operation that is – has made its investment and it is looking to reduce its costs in the immediate sense, it may not be able to do that by reducing the cost of capital. Do you accept that?---Yes, that – I mean, yes because I guess that's my – that's one of the points I'm making, that once you get capital it's there – it's there for the seven days of the week.

PN11727

Just bear with me one moment. Professor, if, and I'm just asking you to assume this, if there are restaurants out there or cafes out there that contrary to what you say, they assess the viability of opening each day based upon whether it is profitable to open on that day and that day alone, then the analysis and conclusions you proffer in paragraph 29 would not be applicable, would they?---That – no, that's not – that's not contrary at all to what I say. Again, it's a completely different point, sort of. Yes, once – yes, what you're asking there is, look, once you've got this restaurant that's sort of up and going and it's got particular capital equipment, sort of, you know, how's it – how's it going to decide, sort of, to operate, sort of? Does it have to decide to open for a whole week or not at all, or can it decide to operate, sort of, on a day to day basis? Of course. Once it's set up and running it can decide to operate on a day to day basis but that – you know, with respect, that's a completely – it's a completely, sort of, off beam point from the point which is to do with substitution effects. The point about, you know, substitution effects is all about the thought experiment of what happens if you change penalty rates. Does that induce employers to substitute labour for capital? No I don't disagree at all with the idea that once your business is up and running that it's going to – you know, it makes a decision about whether to operate on a day by day basis. Now you know, that's what sort of a text book account of firms maximizing profits would say. That's why I teach and interact in micro-economics. It's not at all consistent with what I say in 29 because 29 is a completely different – completely different sort of thought exercise

*** JEFFREY IAN BORLAND

XN MR IZZO

PN11728

JUSTICE ROSS: Mr Izzo, we need to adjourn for a couple of minutes to change some flight details.

PN11729

MR IZZO: Certainly, your Honour.

PN11730

JUSTICE ROSS: And keep the building open. How long are you likely to be?

PN11731

MR IZZO: Not long, your Honour. I'd be surprised if I was 10 minutes.

PN11732

JUSTICE ROSS: Is there any other cross-examination of this witness?

PN11733

UNIDENTIFIED SPEAKER: There is, your Honour. I'll be two minutes.

PN11734

UNIDENTIFIED SPEAKER: Not at this stage, your Honour.

PN11735

UNIDENTIFIED SPEAKER: I'll be, your Honour, probably about five to ten minutes from my end.

PN11736

JUSTICE ROSS: All right. Thanks. We'll be back shortly.

<THE WITNESS WITHDREW [6.01 PM]

SHORT ADJOURNMENT [6.01 PM]

RESUMED [6.05 PM]

<JEFFREY IAN BORLAND, RECALLED ON FORMER AFFIRMATION [6.05 PM]

CROSS-EXAMINATION BY MR IZZO [6.05 PM]

PN11737

MR IZZO: Professor, if I could take you forward to paragraph 34 of your report, which is on p.17. About half way down you start to say the impact of – sorry, you're talking here about the impact on demand relating to decreases in price and I think you're also discussing whether businesses are open the same or different opening days.

*** JEFFREY IAN BORLAND

XXN MR IZZO

PN11738

And you say, "The size of this effect will depend on the extent to which consumers who are not able to buy from the firm on the day in which it was not open, instead shift their demand to some other day". You go on a little bit lower

on today, "For example, when a firm opens for an extra day, all of the consumers who now buy from it on that day who previously bought from another firm on that day then there's zero net effect on employment".

PN11739

So your position is that even if penalty rates were lowered and even if this did result in greater expenditure on Sundays, such expense would come at the expense of other days of the week. Is that your view?---No. What I – I mean, if you go on the next sentence says, "There does not appear to be any empirical evidence regarding the extent to which consumers are able to shift their demand". So it is not my definite view that if you abolished penalty rates there'd be a zero effect because of this demand shifting. What I'm doing is making the point that demand shifting is a phenomenon that Professor Lewis was not able to take into account in his report because he adopts this one day model of the labour market and as I guess I said in response to Professor Lewis' response when I was responding to Mr Dowling before, the point I was trying to make here was that Professor Lewis assumes that there's no demand shifting. So we may not know the magnitude of demand shifting but to the extent that there's any demand shifting, that is another factor which would lower the employment effects estimated by Professor Lewis.

PN11740

But you can't say whether there is demand shifting or what extent that is?---No. I acknowledge and that, yes, as I said in the report.

PN11741

Now if I can take you to paragraph 52, you've got an example here of the discussion of the marginal wage?---Sorry, I missed what number you said.

PN11742

Paragraph 52 at p.23?---Fifty-two, sorry. Thanks. Thanks.

PN11743

This is part of your reply to Professor Rose?---Yes.

PN11744

I believe?---Yes. No, you're right.

*** JEFFREY IAN BORLAND

XXN MR IZZO

PN11745

Your criticism of the Rose report is that it doesn't identify the – you say the marginal wage that is required to pay the relevant participants in the survey and you criticised the report on that basis. That's right?---Yes. I say that the – well, Professor Lewis, I guess, cites the Rose report and Professor Lewis cites the date that it related to the average amount that participants in the survey stated that they would need to be paid to work on, you know, Sundays or public holidays. My criticism is that the average is not relevant to knowing the wage that you would need to pay to attract all of the existing workforce and it's really just quite a logical or definitional sort of – the idea is, look, if you've got – you know, if you've got people out there who say, "Look, I'm willing to work on Sunday for" – you know, "I'm working at the moment but I'm willing to work at, sort of, \$25",

another person says "\$30", another person says "\$35", then unless the wage rate is \$35, as long as the – you know, preferences elicited by Professor Rose are, you know, what people are really willing to work for, if we take that on face value, then unless you're paying \$35 which is the maximum, you're not going to get all those people to work for you.

PN11746

And do you accept that the Rose report does identify the marginal rate which the employee is required to work but that it represents what the average of those marginal wages are? Do you accept that?---I – yes, I accept that Professor – well, if you – so I'm not an expert on that type of survey and so I should put that caveat in, that other people might have problems with, you know, the survey method and the quality of the data. If you were to accept that the quality of the data is fine then yes, Professor Rose has collected data which would enable you to, you know, identify the wage at which the marginal worker was willing to work. So if you think that the sample of workers is representative and if you think that the data is collected of that, then yes. He hasn't reported those data. He hasn't reported them. He's reported the average and that's my criticism but he has – he has somewhere, I guess on his computer, data that would allow you to identify the marginal worker.

PN11747

But what I want to put to you specifically is, what is reported is the – each of the participants have indicated in the survey what the marginal rate is that they require. That's what he's modelling his identified – and what he's published is the average of each of those marginal rates?---No, no, you - - -

PN11748

Do you accept that?---No, no. We're using the term, "marginal", in different ways, okay? The way I'm using "marginal" is that it is the wage that the person with the highest, the highest, wage they need to be paid to be willing to work needs to be paid, okay? That's – "marginal", the way economists use "marginal", is sort of last. It's the wage that the last worker hired needs to be paid, so you know, that's not the sense in which I'm using "marginal". So I don't accept that he's reported the average of the marginals in the way that I'm using marginal or in the way that any labour economist would use marginal.

PN11749

You accept that Professor Rose's report doesn't analyse demand at all? The report only looks at supply site factors. Do you accept that?---Professor – yes, from – I mean, I'd have to go back. I mean, it's not an issue that I addressed in my report so I guess I'd have to, you know, go back and look at to be able to answer that question definitively but yes, what I can say is that my comments on Professor Rose's report relate to information which is about labour supply. Whether there's other stuff in the report, I'd have to go back and refresh my memory but it's certainly the case that my comments on Professor Rose's report relate to sections which are about labour supply. It's about the wage at which different people are willing to work on Sundays or public holidays. That's labour supply.

*** JEFFREY IAN BORLAND

XXN MR IZZO

PN11750

And you've got your example at paragraph 52, the simple example of five workers - - -?---Yes.

PN11751

Each earning a dollar, two dollars, three dollars, four dollars, five dollars. Can I put this question to you. If in your example the Commission was to set the minimum wage or the minimum rate of pay for that day at say, three dollars and you still had your five workers, what would conventional economic theory say that the employer would do in that circumstance where the employer requires five employees?---Well, conventional economic theory would say the employer would have to increase the wage to five dollars if they want five employees.

PN11752

And do you accept that the role of the Commission is not necessarily to set the wage at the marginal rate, at the five dollar figure?---Well, the – I mean, the point that I'm making here is that Professor Rose did something very - - -

PN11753

I don't think that's directed to my question, Professor. My question to you is, is the role of the Commission to separate at the marginal rate?---Well, that's not something I commented on in my reports.

PN11754

MR DOWLING: I'm not sure that's this witness' job to - - -

PN11755

MR IZZO: No, no, no. That's fine. That's fine. I'll rephrase the question.

PN11756

JUSTICE ROSS: You can ask us if you like.

PN11757

MR IZZO: But you accept that if the Commission doesn't set the minimum payment on a particular day at the marginal rate, then market forces will operate so as to ensure that supply meets demand?---Yes, that's the – that, I guess, is yes, is effective of what I said, I guess, in response to one of the first points that Mr, you know, Dowling raised with me, that Professor Lewis sort of says that if you get rid of penalty rates it reduces wages by the whole amount. I guess what I said in response to that is that wages would only fall back to an equilibrium which is where you're paying a wage sufficient to employ the marginal worker who's required. But the debate here is about sort of, you know, is the average – like, is the average telling you the wage that you need to pay to attract all of the current labour force in the industry to be willing to supply their labour. And the answer's no. It's the marginal wage which tells you that information. Professor Rose is saying that you could, you know, on the basis of average information that you could reduce the penalty rates to that amount. I guess I'm saying you can't. You can only reduce it to the marginal wage or - - -

*** JEFFREY IAN BORLAND

XXN MR IZZO

PN11758

I don't think Professor Rose is saying you can reduce the penalty rates. He's just saying, isn't he, that that's - - -?---Sorry - - -

PN11759

These are the marginal – these are the average that - - -?---Yes. Yes. I mis-spoke there. What I meant to say is Professor Lewis, I think, says that - - -

PN11760

Right?---That based on Professor Rose's evidence, this shows that you could reduce to that amount. And I guess I'm saying, no, the average is not the amount you'd - - -

PN11761

Can I ask you a question about something you asked earlier. You made some comments in response to examination by Mr Dowling that the markets we're talking about are not perfectly competitive and you say that because you criticise Professor Lewis' opinions because some of the formulae he's using are basing his assumption of a perfectly competitive market. Do you accept that there is a high level of competition in the restaurant and café industry, as well as the retail industry?---It's not something I've studied in detail. As I said in response to Mr Dowling, my point was simply that Professor Lewis has chosen – well, his approach implicitly assumes, you know, the very extreme case. You move, you know, one iota sort of away from that and you reduce the amount of competition and you no longer get past (indistinct). I think I said in response to Mr Dowling that, you know, I wasn't arguing that, sort of, this industry was like a monopoly or I wasn't arguing exactly where it is on the spectrum. I was saying, look, you know, there is clearly some product differentiation which makes it not perfectly competitive. So as soon as we move away from perfect competition then Professor Lewis – this is another factor where he's overestimating the effect.

PN11762

Thank you, Professor. I think you answered the question in the first sentence?---Okay. Sorry.

PN11763

And I think you have covered the background - - -?---Okay.

PN11764

So I'm just trying to keep things a bit more efficient, Professor. Do you accept that in an industry where there is a high level of competition but not perfectly competitive industry there will still be a substantial passing down of cost reductions to consumers?---Yes. You would expect – I mean, even in a monopoly the prediction is that if costs fall there's going to be some price reduction. So yes, you can't deny that – you know, that there's going to be some price – well, theory predicts that when costs fall there's going to be some price reduction. As I've said, my point was simply to say that I don't think it's perfectly competitive.

*** JEFFREY IAN BORLAND

XXN MR IZZO

PN11765

Sure. Now I just want to show you two documents, Professor. The first is ABI7?---Thank you.

PN11766

Before I ask you about this document, it's from the draft report of the Productivity Commission. I'm not sure if you've read that?---I have.

PN11767

Right. Okay. It has chapter 14. It's the front page of chapter 14. Do you see that?---Yes.

PN11768

I think there's some highlighting on your document. You can just ignore that. The seventh bullet point down expresses a view. It says, "Excessive penalty rates for Sundays reduce hours worked, mean unemployment is higher than it needs to be and reduces options for businesses and consumers. Trading hours are likely to be lower and capital under-utilised". And then I'll skip the next bullet point and go to the one below. "Lower rates would affect the incomes of employees currently working on Sundays in the relevant industries. However this would be partly offset by higher demand for labour". Do you agree with that proposition that's put there, or the two propositions I've taken you to?---No, I disagree with the analysis. As much respect as I have for the Productivity Commission, I disagree with their analysis in chapter 14. I think that their analysis has some of the same errors that I've identified in Professor Lewis' report. For example, the Productivity Commission in this chapter, you know, never recognised the fact that it's not appropriate to think of the labour market as a one-day labour market. I mean, if you read that chapter they kind of say, "Well, look, it's a big amount, penalty rates, so even if it's a small wage elasticity there's going to be a big effect". They're falling into exactly the same trap that Professor Lewis did of not thinking through the fact that penalty rates are just wage changes on one day of the week and so you either need to recognise that there's a much smaller elasticity than, you know, you would expect say for minimum wage changes or something like that, or you've got to basically divide the penalty rate amount by the fact that it's only one day of the week, sort of. So I think that they've overestimated the consequences and I think their reasoning sort of is – I mean, I can't give you a completely detailed perspective on what I think but I'm just giving you an example that I think one reason they've overestimated the effects is that they've failed to take account of the multiple day aspect of this issue as well as, sort of, a variety of other issues.

*** JEFFREY IAN BORLAND

XXN MR IZZO

PN11769

I'd like to show you one further document, ABI8. There's some underlying on the document and that's actually the paragraph I'm going to show you. It says, "The Productivity Commission's overall view informed largely by the reality that labour demand response to wage rates is that as there is a significant differential between Saturday and Sunday penalty rates, their greater alignment is highly likely to have sizeable employment effects. This conclusion is not underpinned by the simple adoption of any assumption - employment is highly responsive to wage rates, as in Lewis 2014 – nor by uncritical acceptance of anecdotal survey or surveys of

businesses that will later have some value. Because businesses are the parties to make the decisions about whether to open or employ people it rests primarily on the significant size of the wage differential between Saturday and Sunday". Do you agree with that statement?---No, I don't. In fact, that was exactly the – it's very good you produced this because this is exactly the statement in this chapter that I was referring to when I answered your previous question, that their belief that you're going to get large employment effects comes from the fact that they're saying that this is a large – that this is a large wage change. I think they haven't taken into account that this is a wage change on one day of the week so – I mean, I guess I'm saying this ad nauseam but as I said in my report, you know, you've got to take account of the fact that penalty rates are sort of what – you know, that this effect we're talking about is one day of the week. So you've either got to average the wage change you're talking about, you know, across the seven days of the week, in which case it's no longer a large wage change, or you've got to change the elasticity of labour demand that you're talking about. So yes, I think the Productivity Commission's reasoning, you know, this is – and this is as good as their reasoning gets, you know. It's the, "Wow, this is a large wage change so we think that there's going to be a big employment effect". Well, yes, the problem is it's a large wage change on one day but when you think it through, this is an issue where you've really got to think about it across the seven days of the week.

PN11770

Just bear with me for one moment. No further questions, Your Honour.

PN11771

JUSTICE ROSS: Mr Wheelahan?

CROSS-EXAMINATION BY MR WHEELAHAN

[6.25 PM]

PN11772

MR WHEELAHAN: Thank you. Professor, my learned friend, Mr Dowling, took you to the reply report of Mr Lewis of 3 September 2015, page 2 where he said your report relates almost entirely to the café and restaurant industries, you accept that proposition save that you say your report contains general principles. Is that right?---Yes. My understanding, I guess, from my letter of instruction was that I – sorry - - -

PN11773

No, no, it's not about your instructions?---Sorry. My understanding from my letter of – sorry?

PN11774

Sorry, I couldn't hear at the same time?---Sorry. My understanding from my letter of instruction was that I was to focus on, sort of, the industry sector represented by the union and so that's why I kind of talk about restaurant and cafes throughout. But you know, I think as you've just said and as I said to Mr Dowling, I think what I consider are the four main points in my report, they're generic.

*** JEFFREY IAN BORLAND

XXN MR WHEELAHAN

PN11775

All right, so it's correct though that you haven't in your report, applied these generic principles to the retail industry?---Well, yes, for example, I – but it's not very – the - - -

PN11776

In your report - - -?---Well, but in a lot of places I don't even apply it to the - - -

PN11777

You haven't gone through the process - - -?---In a lot of places I state them as generic principles, sort of. So for example, if you look at my discussion of the point to do with calculating the percentage change in wages, I don't think I actually mentioned, you know, the restaurant, café sector there.

PN11778

Yes?---I just make the point that, "Look, Professor Lewis has done all these simulations in this particular way". So I think I – I agree that when I have mentioned particular sectors I mention the restaurant and café sector to illustrate my arguments. But I think, you know, a lot of the points I discuss, I discuss without making reference to any sectors.

PN11779

Yes. So just a short question. You've said that matters such as scale and substitution were context dependent, correct?---That's right.

PN11780

You've said that. Now in your report though you haven't specifically explored the retail context in your report in applying any general principles, have you?---But the point – by "context dependent", I mean, what I meant is that penalty rates are a particular type of wage change. Penalty rates are a wage increase on one day of the week or, you know, public holidays so that's what I mean by, "context dependent". That yes, I mean, of course there's an extra layer on this that if you really wanted to know what the elasticity of labour demand was, it would probably vary between those industries as well. But I'm not trying to say, "Look, you know, I know what the labour demand elasticity is in the restaurant and café sector". What I'm saying is that if you want to think about that elasticity in the context of penalty rates, that you need to take account of the fact that penalty rates are a particular type of wage change and that point applies equally across all sectors.

PN11781

Yes. And I'll just put it again. You haven't gone through the process in your report of applying any of those principles specifically to the retail industry. That's the question?---Well, I don't think I do that but I use examples from the restaurant and café industry to illustrate my answer. I think the answer to your question is, you could make the same point about the restaurant and café sector because I'm applying – you know, I'm applying principles generically and I'm using examples from one sector to illustrate those points.

*** JEFFREY IAN BORLAND

XXN MR WHEELAHAN

PN11782

Thank you.

PN11783

JUSTICE ROSS: In Sydney?

CROSS-EXAMINATION BY MR SECK

[6.29 PM]

PN11784

MR SECK: Yes. Professor Borland, my name's Seck. I appear for the Pharmacy Guild of Australia. I just wanted to pick up on some of the questions that have just been asked of you by the counsel for the retailers. When you say, Professor Borland, that you were simply using examples from the restaurant and hospitality industry which had general application, it's true to say that in making those points you rely upon data that applies specifically to the hospitality and restaurant industry. That's right, isn't it?---Yes. For example, I guess when I talk about labour/labour substitution I think I say about 11.6 of labour is supplied by owners. That's an example.

PN11785

And you use numerous examples by reference to the restaurant and hospitality industry which might differ when you look at other industries such as the community pharmacy industry. That's correct, isn't it?---The details could differ. The extent of some of the phenomena that I'm talking about could differ but the general points are the same. You know, for example, you know, in every one of the industry sectors that Professor Lewis considers in tables 4(a) and 4(b), he makes the assumption that the percentage wage change is the maximum possible wage change. So you know, that comment applies equally to every one of the industries in tables 4(a) and 4(b).

PN11786

Can I take you to just some specific examples in your report, Professor Borland. Can you go to paragraph 24 of your report on page 12. Now do you see in the first sentence there that you used the specific example of the case of restaurant workers in Australia? Do you see that? That's in the first sentence. Do you see that, Professor Borland, paragraph 24 and - - -?---I – this paragraph 55?

PN11787

No, sorry, paragraph – it mightn't be coming clearly from Sydney. Paragraph 24 - - -?---Twenty-four, sorry. I went to page 24.

PN11788

That's all right. Paragraph 24 on page 12?---Yes.

PN11789

If you go to the first sentence you're plainly referring there to the case of restaurant workers in Australia. That's correct, isn't it?---Yes.

*** JEFFREY IAN BORLAND

XXN MR SECK

PN11790

And in making your point you do it by reference to data that applies only to the accommodation and food services industry. That's correct?---Yes.

PN11791

And if you go down about half way down that paragraph you say, "I present these data not to claim that there has definitely been a downward adjustment in the base rate of pay in the restaurant industry due to penalty rates but instead to show there is certainly sufficient flexibility in wages in the industry for that adjustment to occur". Now you would agree with me the proposition you're advancing there is solely based on data that's applicable to the hospitality and restaurant industry, that's correct, isn't it?---Yes.

PN11792

Now can I then take you to, I think this is the example you used, paragraph 30 on page 15 of your report and you use the figure of "11.6 per cent of total labour is supplied by owners and family members in the accommodation and food services industry". Do you see that?---Yes.

PN11793

You would acknowledge, wouldn't you, that in the accommodation and food services industry it's largely an unskilled or low skilled industry in terms of the work performed?---Yes, I – I mean, that's not something that I discussed in my report. I would have thought, you know, usually the chefs are reasonably qualified when they go to a restaurant so yes, I'm not sure what you mean by "largely unskilled".

PN11794

Well, when I said, "a large" – would you accept that a large proportion of the employees working in the accommodation and food services industry are either unskilled or low skilled employees?---Yes. I can't answer that without going and looking at the data which is – you know, you'd have to look at the occupational profile within that industry to make a conclusion about it.

PN11795

And picking up on that point, looking at the occupational profile, the occupational profile for the community pharmacy industry, you would acknowledge, wouldn't be exactly the same as that of the accommodation and food services industry, that's right?---No, I wouldn't – I wouldn't want to make a comment on that until I'd been and looked at the ABS data.

PN11796

Of course. And therefore you can't really draw any general conclusions from the propositions that you set out in paragraph 30 because you can't draw any conclusions without looking at the data specifically in relation to the community pharmacy industry. That's correct, isn't it?---Well, but I mean paragraph 20, I guess, is about the – it's not the - - -

PN11797

Paragraph 30, sorry?---Yes. Sorry, I missed - - -

*** JEFFREY IAN BORLAND

XXN MR SECK

PN11798

Paragraph 30?---Yes, yes. Sorry, I am on paragraph 30. I was just misreading it. I mean, that's about substitution of unpaid or paid labour, basically substitution of the, you know, the proprietor's labour for the labour of workers whatever job it is they're doing. So yes, to the extent that the percentage of labour supplied by proprietors differs between those, you know, different sectors, then there's going to be different scope for labour/labour substitution. But the Productivity Commission report lists them all and they're all, you know, relatively around the same amount.

PN11799

It will differ, for example, if the positions which are required to be worked in a particular industry require minimum qualifications. So for example, using the community pharmacy industry, a number of the classifications require qualifications in terms of certifications. It wouldn't be the case that family members could substitute their labour for paid labour if they didn't have those qualifications or certifications. That's right, isn't it?---Yes, of course. You can only substitute labour for labour if they, I guess, have the skills and, yes, if there's regulatory requirements, as well, that they satisfy those.

PN11800

And that's an example or a proposition which will depend upon a specific industry and it doesn't necessarily have generic application, you would agree with that, Professor Borland?---Yes, the details are going to – the details of particular, you know, aspects are going to differ but the point that doesn't differ is the idea that it's appropriate to think about the substitution effect when you change penalty rates with a multiple day model rather than a one day model.

PN11801

But the degree of those substitution effects may be negligible depending on the occupational profile of that industry. That's correct, isn't it?---Yes, well, if you – but if the degree of the substitution effects is negligible what you're saying is that there's very small effect of penalty rates on employment.

PN11802

Unless it can be demonstrated, Professor Borland, that penalty rates result in businesses not opening on Sundays or public holidays because it's unprofitable to do so on those days?---Well, yes, that's the – that - - -

PN11803

If there was an increase in penalty rates that made it profitable to operate, standard economic theory would tell you, wouldn't it, that businesses would open on those days?---So yes, I guess I talked about that in my report as one possible effect of penalty rates being – you know, one of the possible scale effects being an effect on the range of opening days.

*** JEFFREY IAN BORLAND

XXN MR SECK

PN11804

Now can I take you to paragraph 33 of your report, Professor Borland, on page 16. In that paragraph you there talk about whether or not a firm operates in a perfectly competitive product market. Do you see that?---Yes.

PN11805

You would agree that the degree of competition within a market for any particular industry is going to differ. That's right?---That's – yes.

PN11806

As a matter of general proposition?---Yes, yes. You've got to look at any particular industry to understand the degree of competition.

PN11807

And I think you talked about – in answer to one of the questions you were asked earlier on, Professor Borland, you said there's a spectrum of competition within any industry. That's correct?---No. What I said is that - well, economists think of there being a spectrum of sort of possible types of competition from monopoly through to perfect competition. Professor Lewis' method assumes perfect competition. So as soon as you move away from that by, you know, some degree then you're no longer getting complete pass-through of costs to prices in the same way that you get if there's perfect competition. You know, unless you are arguing that there's an industry that is perfectly competitive then that same point applies equally sort of to any industry sector.

PN11808

You accept, however, the high degree of competition within a market, the more likely that the scale effect will be greater?---Yes, the other things equal - other things equal, the higher degree of competition, the bigger effect of pass-through from any cost reduction to prices will be, and so yes, the – given whatever the demand is, the bigger the effect on demand will be.

PN11809

Looking at the example that you used in paragraph 33, Professor Borland, you refer to the restaurant market there in the second half of paragraph 33. Do you see that?---Yes.

PN11810

And you look at different characteristics which would suggest that there is product differentiation and provide some degree of market power to individual restaurants?---Yes.

PN11811

Do you see that?---Yes.

*** JEFFREY IAN BORLAND

XXN MR SECK

PN11812

Now you refer to, I think, quite standard characteristics such as style, quality cuisine, brand name, et cetera, and those are obvious product differentiated that would exist in the restaurant industry. But that wouldn't necessarily apply to all industries, you would agree?---Well, any – yes, we think of, you know – most industries we think of, sort of, if they're not monopolies, are going to have the

characteristics of monopolistic competition so there's going to be some type of product differentiation. Otherwise they'd be perfectly competitive. The type of product - - -

PN11813

But - - -?---Well, yes, just let me finish. The type of product differentiation that exists and the extent of product differentiation, that is going to vary between industries.

PN11814

And the quantum of the scale effect will differ between industries depending on the product differentiation, I think you agreed with me beforehand?---Yes because product differentiation – again, other things equal product differentiation is one thing that we think determines the extent of competition. You know, the close two products are or two sort of – the products of two firms are to being substitutes then the more they're competing with each other and the more you're going to get pass through of costs to prices so yes, the effects are going to vary on the effect on price and hence the scale effect's going to depend on the degree of competition.

PN11815

And would you agree with me, Professor Borland, that the degree of market power can also be affected by government regulation of prices?---Yes, market power, I guess, we – yes, we usually think of as the capacity to the – market power is the capacity you have to increase prices above what would exist in a hypothetical, perfectly competitive market and that market power is going to depend on barriers to entry and doing to depend on the extent of product differentiation. I guess if you've got government – so it depends which type of government regulation you're talking about. If you're talking about, say, government regulation of prices then the way I'd probably put it is that government regulation of prices can affect the scope that a business has to exercise its market power and to take advantage of market power to increase prices.

PN11816

Let me use specific example relevant to the community pharmacy industry. The pharmaceutical benefits scheme to the best of your knowledge prescribes the prices which can be charged by pharmacies for the dispensation of medication on the scheme list. You know that's correct, Professor Borland?---Yes.

*** JEFFREY IAN BORLAND

XXN MR SECK

PN11817

And that it's likely that the product differentiation involved in the dispensation of medication on the PBS price list is not going to differ from pharmacy to pharmacy because the type of medicine that can be prescribed will be on the list. That's right, isn't it?---Well, I mean, yes, I don't want to give a definite, you know, judgment about that. You know, you'd have to look at the industry. I mean, you know, anecdotally there are, you know, a lot of services that, you know, pharmacies provided associated with the, you know, dispensation of that medicine that can affect the quality of service that can affect that – you know, can be a source of product, you know, differentiation. Like, you know, I know, you know,

my father, they make – the chemist makes up the prescriptions into, like, this thing they call the "Webster pack" and that, and so that's a reason for going to that particular chemist because they provide that extra, sort of, service. So I think you'd – yes, you'd have to – I don't want to say one industry is more competitive than another industry, sort of. Because it's not really my main point here.

PN11818

Yes?---My main point was just to say that these industries aren't perfectly competitive.

PN11819

Yes. The only point I'm making to you, Professor Borland, is this, that ultimately if it's not perfectly competitive but the industry is highly competitive due to the inability or the restrictions placed on a proprietor or business to exercise market power, then the size of the scale effects are likely to still be significant. That's correct, isn't it?---Well, other things are equal because, you know, there's a series of points I guess I make about, you know, these effects and that but yes, I – yes, I've agreed several times, I think, with the idea that the more competitive an industry, without making any judgment on, you know, what the degree of competition in the industries you're talking about here is. I agree completely that the more competitive an industry, the more pass through you'd expect there to be of costs to prices and therefore the bigger the scale effect.

PN11820

Can I take you to paragraph 34 of page 17, Professor Borland. You talk about there the substitution effect. Sorry, not the substitution effect, the concept of demand shifting?---Yes.

PN11821

It's about half way down the page, that's right. Starting, "The size of this effect will depend on the extent to which consumers who were not able to buy from a firm on the day on which it was not open instead shifted their demand to the same firm on another day or shifted their demand to an alternative firm which was already open on that day". Do you see that?---Yes.

PN11822

Would you agree that the capacity for demand shifting will depend very much on the particular industry?---Yes. To some extent, yes, I'm sure it will.

PN11823

And that's probably going to be more relevant in circumstances where the particular service or good is expressionary in nature?---Can - - -

*** JEFFREY IAN BORLAND

XXN MR SECK

PN11824

To use an example, in the cafe – in the restaurant industry, you can shift a meal perhaps from one day to another day? That's an example?---Well, I guess what I'd say is that that demand shifting, it depends on the extent to which consuming that good or service on another day, how close a substitute that is for consuming it on the day that the store is closed. So you could say that it doesn't matter whether

you get your prescription medicine filled on, sort of, Friday or Sunday because you're still getting the same service of having the prescription, you know, medicine filled. You could say that having a meal on Friday night is the same as having a meal on Sunday as long as it's from the same restaurant. I think the key thing is not so much whether it's discretionary, the key thing is the extent to which consuming the service on another day of the week is a close substitute for consuming it on the day on which the supply is closed.

PN11825

So to use an example in the community pharmacy industry, if someone is sick on a particular day and needs medication on that particular day but the pharmacy is closed and it's a matter of urgency, the ability to substitute another day for consuming that service is going to be much more limited than, for example, having a meal on a different day. You would agree with that?---Yes, I – well, it's hard to compare with the restaurant example but I would agree with you that if someone, you know, has an illness or condition which has a sudden onset then – and they're prescribed medication and they need to fulfil that medication that there's not as much substitute ability between buying the medicine on the day when you, you know, become ill and other days versus, say, blood pressure medicine where, you know, you've got this chronic condition and you know, you've got your new prescription. It doesn't matter whether you buy it, sort of, on Monday or Tuesday or whatever. So I think it comes back to the point I made about the degree of substitutability. That's what determines it.

PN11826

Yes. And then just going to paragraph 36, Professor Borland, about five lines down you initially make a criticism in the multiple day model and then you say, "In my opinion the elasticity of substitution in the restaurant industry is likely to be lower than the lowest size assumed by Professor Lewis and the price elasticity of demand is likely to be the lower end of the values assumed by Professor Lewis". Now you would agree with me the opinion that you expressed in paragraph 36 in relation to the elasticity of substitution in the restaurant industry is based on the premises that are set out in the earlier paragraphs in your report from about paragraph 25 onwards, that's right?---Well, really from paragraph 17 onwards, I guess.

PN11827

Yes. No, I think you're right. That deals with assumption 1. Pardon me, you're right, Professor Borland?---Yes.

PN11828

And as I've taken you through it, the analysis that you undertake in relation to the assumptions made by Professor Lewis are very much dependent upon examples and data that only apply to the restaurant and café industry. You would agree with that?---No, I'd disagree with that.

*** JEFFREY IAN BORLAND

XXN MR SECK

PN11829

And the conclusion, the opinion that you expressed there in terms of a specific elasticity of substitution, it's only applicable to the restaurant industry and cannot

be, in terms of the values that you set out there, applicable to any other industry?---I disagree with that, I guess for the reasons I explained in response to Mr Dowling's last question and which I guess I've expressed several times.

PN11830

You say that general principles apply in the same way but then you say in paragraph 36, Professor Borland, "In my opinion the elasticity of substitution in the restaurant industry is likely to be lower than the lowest size assumed by Professor Lewis and the price of elasticity of demand is likely to be at the lower end of the values assumed by Professor Lewis". Now in expressing your views about the elasticity of substitution being at a particular end of the scale you are expressing your opinion based on the reasoning set out in the earlier paragraphs which are based on the restaurant and café industry, aren't they?---As I've explained before, they're based on points which apply, you know, to – it might not even be one of the industry sectors we're talking about here. The same points would apply equally if we were talking about hourly rates in those sectors. Like, you know, for example again, you know, the point that if you're going to think about substitution effects, whenever you talk about, you know, penalty rates you've got to recognise that that's a wage change that just applies on the one or, you know, couple of days of the week compared to the regular sort of wage change which Professor Lewis is assuming in his approach which is a wage change that applies for every sort of hour worked to every day of the week. So yes, if I didn't think that – so I acknowledge completely that this is stated in terms of, you know, examples about that sector. But I've explained why I think that the same principles apply across other sectors. And you know, if Professor Lewis had used that approach, as I said, for sectors that we're not even considering here, then the same principles would apply.

PN11831

No further questions.

PN11832

JUSTICE ROSS: Any further cross-examination?

PN11833

MR MOORE: I do, your Honour. It's been a long day.

PN11834

JUSTICE ROSS: Remember the caution that - - -

PN11835

MR MOORE: I do.

PN11836

JUSTICE ROSS: All right.

CROSS-EXAMINATION BY MR MOORE

[6.54 PM]

*** JEFFREY IAN BORLAND

XXN MR MOORE

PN11837

MR MOORE: Professor Borland, in paragraph 33 of your statement at about the fifth last line you say, "Individual restaurants will have some degree of market power due to product differentiation. That product differentiation might derive from their location, style or quality of cuisine or brand name". Can you tell me this. From what characteristics might product differentiation be derived in the retail industry?---Well, yes, in – I mean, I guess, you know, that's a broad sector, sort of. I think probably you'd want to, you know, think about particular segments of the retail sector, I think, because my, you know, understanding would be that the sources of product differentiation, you know, differ between sort of different segments of the retail sector. But yes, again, it could be on, you know, location, quality of service, the identification of the brand name of the retailer. You know, it could be to do with sort of the range of goods that you can buy from a particular retailer. If there's one retailer in, I don't know, sports goods, who's selling a narrow range versus another one that's a larger range, that could be something that's attractive to consumers. It could be whether you've got the, you know, most up to date or most fashionable type of whatever good it is that you're retailing.

PN11838

Thank you. And from what characteristics might product differentiation be derived in the community pharmacy sector?---Well - - -

PN11839

MR SECK: Objection. Objection. I don't think Professor Borland has been qualified as an expert in terms of product differentiation in the community pharmacy industry. He has no qualification to express that.

PN11840

MR MOORE: I think my learned friend - - -

PN11841

MR SECK: In fact I think Professor Borland said he wasn't familiar with the industry.

PN11842

MR MOORE: I think my friend asked the witness numerous questions about the community pharmacy industry.

PN11843

JUSTICE ROSS: Yes, you did, Mr Seck.

PN11844

MR SECK: And I think the response of Professor Borland was that he wasn't familiar with the industry so he couldn't comment too much.

PN11845

MR MOORE: It didn't impede my friend from continuing to pursue lines of questioning at some length about the sector.

*** JEFFREY IAN BORLAND

XXN MR MOORE

PN11846

MR SECK: And there was no objection to that.

PN11847

MR MOORE: If I can be heard. It didn't impede my friend from pursuing at some length, question of the witness applied and directed in particular to that sector. In fact, I think that was all my friend directed his questioning at.

PN11848

MR SECK: My questions were very specific in nature and they weren't directed to asking Professor Borland what product differentiators may exist in the community pharmacy industry. The questions were asked based on particular assumptions or to ask Professor Borland to accept certain propositions. I didn't ask him any questions about what product differentiation characteristics may exist in a particular industry. That was never a question I asked Professor Borland.

PN11849

JUSTICE ROSS: We think the door is open, Mr Moore, but Mr Seck, if there's anything arising from these questions that you wish to further cross-examine on you'll be given leave to do that.

PN11850

MR SECK: May it please your Honour.

PN11851

MR MOORE: Thank you, your Honour. Professor Borland, from what characteristics might product differentiation be derived in the community pharmacy sector?---Yes, maybe I can help by just saying again, the context in which I was, you know, making this point was simply to say that Professor Lewis assumes perfect competition. And I'm saying, look, you know, I don't claim to be an expert on the details of competitively managing the restaurant sector of the pharmacy sector or the – but I do know enough about those sectors to see that they're not perfectly competitive. You know, all I'm saying is that in each of those sectors it's clear that there's a basis for product differentiation. That's what I expressed about the restaurant, you know, sector. So with the pharmacy sector, yes, I guess it's to do with the quality of service provided. That's a basis for differentiation. You know, for example, the example I gave of the way you, you know, provide (indistinct) to customers. You know, it's about the variety of other services that you provide, sort of, together with providing the pharmaceuticals. It's about location again. So there's the same set of factors and I guess, you know, I don't feel like you need to be an expert on the detail of competitive advantage in those industries to make the point that, look, they exhibit features of product differentiation. And that's all I was trying to say, that because there's product differentiation they're not perfectly competitive. Therefore the scale effect is over-estimated.

PN11852

Thank you, Professor Borland. One last question. It's a repeat of the last one, save that it's directed at the fast food industry. From what characteristics might product - - -

*** JEFFREY IAN BORLAND

XXN MR MOORE

PN11853

MR DIXON: I object.

PN11854

JUSTICE ROSS: Yes.

PN11855

MR DIXON: Your Honour, my objection is that there has been no evidence given by any of the experts directed at the fast food industry. There is no material of the statistical basis upon which any of these questions might be answered. Professor Borland has very fairly stated that he was directed to deal with the – or requested to deal with the report by Professor Lewis which does not deal with the fast food industry and what Professor Borland, in my respectful submission, very fairly has repeatedly said is that he has not carried out any individual analysis of any of these other industries. He's simply making some points about what Professor Lewis did not do and Professor Lewis did not do anything in respect to the fast food industry.

PN11856

May I also raise one other matter and I do so reluctantly because I accept that the interest of the unions might be common interests but it seems to me that my learned friend is now straying beyond what the complaint was when we asked a few questions of a witness that was a common witness, directed against the interests of all the employers.

PN11857

JUSTICE ROSS: I'm not sure that Mr Moore is offending that principle but from my own perspective I am struggling to understand, bearing in mind what Professor Borland said about the context in which he's putting this, that is, it's to make the point in relation to Professor Lewis' report that to the extent you stray from perfect competition you're going to have an impact on the price flow on effect.

PN11858

MR DIXON: Yes.

PN11859

JUSTICE ROSS: Well, Professor Lewis doesn't say anything about the fast food industry.

PN11860

MR MOORE: That is so, your Honour. However, what Professor Borland has said a number of times this afternoon is that his evidence in many respects is directed at all sectors and that some of his evidence is, I think, one word he used was "generic" in relation to economy wide sectors.

PN11861

JUSTICE ROSS: He's expressed the general proposition that to the extent you stray from perfect completion, there's not going to be a complete flow through of -
- -

*** JEFFREY IAN BORLAND

XXN MR MOORE

PN11862

MR MOORE: That's so.

PN11863

JUSTICE ROSS: Well, that applies to all sectors.

PN11864

MR MOORE: Yes, it does and what he does - - -

PN11865

JUSTICE ROSS: No-one is suggesting that the fast food industry exhibits perfect competition.

PN11866

MR MOORE: No.

PN11867

JUSTICE ROSS: No sector of the Australian economy.

PN11868

MR MOORE: No.

PN11869

JUSTICE ROSS: Well, I suppose it's sometimes put that parts of the fruit and vegetable market does but that's not what we're talking about here.

PN11870

MR MOORE: No. Well, in paragraph 33 it's important to emphasise that the word that Professor Borland uses is he states that product differentiation might derive.

PN11871

JUSTICE ROSS: Yes.

PN11872

MR MOORE: And given that Professor Borland's observations on this point are not confined to the specific industries in my respectful submission I'm entitled to ask him the same question that I asked in relation to the other industries in respect of another relevant industry.

PN11873

The union, my client, relies upon Professor Borland's evidence in respect of the fast food award. It's obviously relevant to the proceeding. It's neither here nor there, in my respectful submission, that his evidence is presented as being responsive to Professor Lewis. It's a relevant issue in the case as to what one makes of, if I can say, the evidence generally of the labour economists in relation to all of the awards that are under the review in respect of penalty rates.

*** JEFFREY IAN BORLAND

XXN MR MOORE

PN11874

JUSTICE ROSS: We'll allow the question, Mr Moore, and Mr Dixon, you can cross-examine in relation to the matters that might arise from the answer.

PN11875

MR DIXON: If the Commissioner pleases.

PN11876

MR MOORE: Professor Borland, from what characteristics might product differentiation be derived from the fast food industry?---Well, yes, again, if the (indistinct) – and I'm not saying that I'm an expert on competitive advantage in that sector but I mean, yes, you would think that it derives from the type of food, the location of the – you know, the particular outlets, perceptions of the quality of the food, you know, other activities that you can do, sort of, at the outlets where you purchase the fast food, so differentiation of service. But again, yes, and I don't want to make it look like I'm claiming – I think the President expressed it very well – all I'm trying to do is just say that this isn't perfectly competitive and I don't think you need to be an expert on competitive strategies, sort of, to know that that's my point. And as he said, you know, that then applies equally across all sort of industry sectors, the issues, the extent of the competition because that then determines, sort of, the extent of pass through and the size of the scale effect.

PN11877

Thank you, Professor Borland, nothing further.

PN11878

JUSTICE ROSS: Anything arising from either counsel for AR Group or for the pharmaceutical group?

PN11879

MR WHEELAHAN: Not from us, thank you, your Honour.

PN11880

MR SECK: Not from the Pharmacy Guild, your Honour.

PN11881

JUSTICE ROSS: Thank you. Any further cross-examination of this witness? No? No re-examination?

PN11882

MR DOWLING: No re-examination.

PN11883

JUSTICE ROSS: Thank you for your evidence, Professor Borland. Sorry to have kept you?---No, no, that's fine. Thank you very much. Anything further? Well, we'll adjourn until 14 October.

<THE WITNESS WITHDREW

[7.07 PM]

ADJOURNED UNTIL WEDNESDAY, 14 OCTOBER 2015

[7.07 PM]

*** JEFFREY IAN BORLAND

XXN MR MOORE

LIST OF WITNESSES, EXHIBITS AND MFIs

PHILLIP EDWIN THOMAS LEWIS, SWORN	PN10552
EXAMINATION-IN-CHIEF BY MR IZZO.....	PN10552
EXHIBIT #ABI3 REPORT TITLED "PENALTY RATES IN THE RETAIL, CAFE, RESTAURANT AND HAIRDRESSING AND BEAUTY INDUSTRIES"	PN10566
EXHIBIT #ABI4 REPORT TITLED "A REPLY TO THE REPORT. EFFECTS OF PENALTY RATES IN THE RESTAURANT SECTOR BY PROFESSOR JOHN QUIGGIN, UNIVERSITY OF QUEENSLAND"	PN10566
EXHIBIT #ABI5 REPORT TITLED "PENALTY RATES IN THE RETAIL, CAFE, RESTAURANT AND HAIRDRESSING AND BEAUTY INDUSTRIES. A REPLY TO A REPORT BY PROFESSOR JEFF BORLAND" DATED 3 SEPTEMBER.....	PN10566
EXHIBIT #ABI6 REPORT COMPRISING ONE PAGE AND DATED 20/09/2015	PN10566
CROSS-EXAMINATION BY MR DOWLING.....	PN10569
THE WITNESS WITHDREW	PN10638
PHILLIP EDWIN THOMAS LEWIS, RECALLED ON FORMER OATH.....	PN10663
CROSS-EXAMINATION BY MR DOWLING, CONTINUING	PN10663
EXHIBIT #UV21 EMAIL FROM MR IZZO TO PROFESSOR LEWIS DATED 04/06/2015	PN10795
EXHIBIT #UV22 PROFESSOR LEWIS' REPORT REPLICATING 2012 REPORT	PN10802
EXHIBIT #UV23 PROFESSOR LEWIS' 2012 REPORT.....	PN10804
THE WITNESS WITHDREW	PN10882
PHILLIP EDWIN THOMAS LEWIS, RECALLED ON FORMER OATH.....	PN10905
CROSS-EXAMINATION BY MR DOWLING, CONTINUING	PN10905
CROSS-EXAMINATION BY MR MOORE	PN11038
THE WITNESS WITHDREW	PN11167
PHILLIP EDWIN THOMAS LEWIS, RECALLED ON FORMER OATH.....	PN11167
EXAMINATION-IN-CHIEF BY JUSTICE ROSS.....	PN11167

RE-EXAMINATION BY MR IZZO.....	PN11222
THE WITNESS WITHDREW	PN11238
JOHN CHARLES QUIGGIN, AFFIRMED	PN11241
EXAMINATION-IN-CHIEF BY MR DOWLING	PN11241
EXHIBIT #UV24 REPORT BY PROFESSOR QUIGGIN.....	PN11253
CROSS-EXAMINATION BY MR IZZO.....	PN11281
EXHIBIT #ABI7 EXCERPT FROM DRAFT PRODUCTIVITY COMMISSION REPORT.....	PN11392
EXHIBIT #ABI8 FURTHER EXCERPT FROM DRAFT PRODUCTIVITY COMMISSION REPORT.....	PN11399
CROSS-EXAMINATION BY MR DIXON	PN11420
CROSS-EXAMINATION BY MR SECK.....	PN11434
FURTHER CROSS-EXAMINATION BY MR DIXON.....	PN11534
FURTHER CROSS-EXAMINATION BY MR IZZO	PN11542
THE WITNESS WITHDREW	PN11572
JEFFREY IAN BORLAND, AFFIRMED.....	PN11576
EXAMINATION-IN-CHIEF BY MR DOWLING	PN11576
EXHIBIT #UV25 REPORT OF PROFESSOR G.I. BORLAND DATED 03/09/15	PN11586
THE WITNESS WITHDREW	PN11736
JEFFREY IAN BORLAND, RECALLED ON FORMER AFFIRMATION.....	PN11736
CROSS-EXAMINATION BY MR IZZO.....	PN11736
CROSS-EXAMINATION BY MR WHEELAHAN.....	PN11771
CROSS-EXAMINATION BY MR SECK.....	PN11783
CROSS-EXAMINATION BY MR MOORE	PN11836
THE WITNESS WITHDREW	PN11883