

# The Treasury

## Advice on Public Sector Pay Adjustment (PSPA) Information Release

March 2023

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[36] 9(2)(h) - to maintain legal professional privilege

[38] 9(2)(j) - to enable the Crown to negotiate without disadvantage or prejudice

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Office of the Minister of Finance  
Office of the Minister for the Public Service  
Chair, Cabinet

## **PUBLIC SERVICE PAY ADJUSTMENT (PSPA)**

### **Proposal**

1. This paper proposes that Cabinet agrees that officials proceed with formal negotiations with the NZCTU and its affiliates for a PSPA and sets a fiscal envelope to support these negotiations.

### **Executive Summary**

2. The New Zealand Council of Trade Unions' (NZCTU) has put forward a proposal for a PSPA to be negotiated on a uniform basis across defined parts of the public sector.
3. We consider that there are efficiency and equity benefits at this time for coordination and alignment in bargaining and employment relations outcomes across the system. In advancing the PSPA proposal, we are seeking to provide certainty in volatile and inflationary times. We also hope to avoid what might otherwise become a period of unrest in workplace relations.
4. We propose that the PSPA be for a minimum two-year term and that it prioritise the needs of the lowest paid employees, probably through a flat rate adjustment i.e. all employees within the scope of the PSPA receive the same dollar sum increases.  
[33], [38]
5. We also propose that the negotiations cover employees in the Public Service, state and state-integrated schools, kindergarten teachers, the Health sector and other Crown Agents.
6. It would be an 'opt-in' proposal, which places a heavy requirement for all parties involved to stay at the table and agree to the terms set out by the PSPA. In other words, the Government sets the fiscal envelope and employers make an offer, and Unions will need to agree that the offer is sufficient.
7. [33]

8. There are risks with a PSPA, attached to both the process of reaching an agreement and in its implementation:
  - 8.1. The current high inflation environment and heightened union expectations could well mean that the funding available for a PSPA is insufficient.
  - 8.2. Some will perceive the PSPA as a guaranteed minimum increase, not a maximum and it could become a “floor” in current or future bargaining activity.
  - 8.3. The process for negotiating and agreeing a PSPA would be complex with a wide range of moving parts and no precedent to draw upon. While the PSPA intention is relatively simple, the complexity and sheer scale and size of engagement between unions and employers to negotiate a PSPA settlement is unprecedented as a bargaining exercise.
  - 8.4. Although public sector wage inflation is likely to accelerate more than previously assumed with or without a PSPA, a PSPA would likely bring forward and amplify some of the increases and spill over into wages in the private and wider public sectors.
9. In relation to this last point, Treasury modelling suggests that total public sector wage inflation, including the proposed PSPA, partly funded through increased operating allowances could push up inflation and could add pressure to the Official Cash Rate in the second half of 2023. Conversely, if all public sector wage inflation is funded from within existing allowances, thus largely exhausting scope for any other initiatives, there would be little impact on interest rates because the higher wages would be offset by less government-funded activity. It should also be noted that, realistically, the counterfactual to agreeing a PSPA is still likely to involve public sector wage inflation above Budget 2022 forecasts.
10. Officials have sought legal advice including on the process for negotiations to ensure compliance with the Employment Relations Act 2000 (ERA), and its requirements for conducting bargaining in good faith and in relation to union preference. The process requires opt-in by any registered union, ratification of proposed settlements by union members, and incorporation of any agreed PSPA into collective agreements following bargaining between employers and unions. Legal comment is included in this paper.
11. Risks with the PSPA can be mitigated by having clear parameters for negotiation and alignment of bargaining. The Public Service Commissioner would take direct responsibility for bringing all Public Service bargaining into a framework of simultaneous negotiation. Relevant bargaining in the education sector is already aligned, while the health sector would be the responsibility of Te Whatu Ora. Te Kawa Mataaho the Public Service Commission (the Commission) would support other Crown agents to appoint representatives to bargain on their behalf.
12. Ministers will write to the NZCTU informing them of the framework for the PSPA set out in this paper. After that the affiliate unions would need to decide whether to opt into the PSPA process. The Commission and the Treasury will work on arrangements for what is an unprecedented level and complexity of bargaining.

13. The paper asks that the Prime Minister, Minister of Finance and Minister for the Public Service have power to act to implement the decisions in this paper, in consultation with relevant Ministers, [33]

## **Background**

14. On 27 May 2022 the NZCTU wrote to the Minister for the Public Service proposing negotiations for an agreed pay adjustment that would form the basis of “all collective bargaining agreements across the public service”. The catalyst for this proposal appears to be cost-of-living pressures faced by union members. The Minister, after discussions with the Minister of Finance, responded that he was open to engaging on a “constructive and strategic approach to setting pay rates in the public sector in the context of both significant fiscal pressures and cost of living challenges”.
15. Since the initial exchange of letters there has been extensive consultation between the NZCTU and designated lead chief executives for the Public Service, supported by the Commission, Te Whatu Ora and Ministry of Education. These discussions have now concluded. They have largely been positive and there is a draft record of views that would form the base for further engagement. That said, there is also considerable work to be done to develop an agreed PSPA but that needs to progress within a formally mandated bargaining process.
16. The wider environment is now one of considerably raised expectations with some mounting risk of industrial action. There is some frustration being expressed by NZCTU-affiliated unions at a perceived lack of progress on the PSPA.
17. We brought an Oral Item to Cabinet to inform colleagues of this work on 12 September 2022. We are now asking Cabinet to agree that we take the next steps on a PSPA.

## **The Public Service Pay Adjustment approach**

18. There are efficiency and equity benefits at this time for coordination and alignment in bargaining and employment relations outcomes across the system. For many years government has articulated employment relations expectations around wage growth and a range of other employment and workforce related matters in relation to public sector employment.
19. The PSPA proposal could take us a further step forward in seeking to align bargaining outcomes around a fiscal envelope that will allow negotiated settlements that are fair to employees, affordable for government, and aligned with one another. The extent to which such a complete solution could be achieved as a result of a PSPA bargaining process is ambitious and may not materialise as comprehensively as intended.
20. In advancing the PSPA proposal, we are seeking to provide certainty in volatile and inflationary times. We also want to advance our values of reducing income inequality amongst public sector workers. In doing so, we hope to avoid what might otherwise have become a period of unrest in workplace relations. However, there are risks of this unrest still occurring, as noted in this paper.
21. Although the approach of the PSPA has benefits in-principle, there are risks attached to both the process of reaching an agreement and in its implementation:

- 21.1. The current high inflation environment and heightened union expectations could well mean that the funding available for a PSPA is insufficient.
  - 21.2. Some will perceive the PSPA as a guaranteed minimum increase, not a maximum and it could become a “floor” in current or future bargaining activity.
  - 21.3. The process for negotiating and agreeing a PSPA would be complex with a wide range of moving parts and few precedents to draw upon.
  - 21.4. Although public sector wage inflation is likely to accelerate more than previously assumed with or without a PSPA, a PSPA would likely bring forward and amplify some of the increases and spill over into wages in the private and wider public sectors.
22. [33], [38]
23. The proposals in this paper are designed to mitigate these risks. Cabinet is asked to make decisions regarding the proposed parameters of the PSPA. This paper also informs Cabinet about the processes for aligning negotiations in each sector to facilitate an orderly approach to bargaining.

## **Proposed parameters of the PSPA**

### ***Structure and scale of the proposed adjustment***

24. It is not feasible to unilaterally determine the parameters of a PSPA and there are risks with even trying to do so.
25. Subject to that caveat, there are some key features that we would be looking for public service employers to seek to negotiate.
26. Firstly, we have a strong view that the PSPA should be for a minimum two-year term. This gives a period of certainty without bedding in too much an arrangement that may not fit changing needs as we move on from the current period of turbulence.
27. Secondly, we have been consistently of the view that the PSPA should prioritise the needs of the lowest paid employees: We consider the simplest and most effective way of achieving that is through a flat rate adjustment i.e. all employees within the scope of the PSPA receive the same dollar sum increases. If the pay adjustment were to be a set across-the-board percentage increase then it will tend to reinforce existing inequalities.
28. The finalised size of the adjustment will be a matter for negotiation. [33], [38]

29. [33], [38]

30.

30.1. [33], [38]

30.2.

### ***Scope of the PSPA***

31. CTU-affiliated unions in their discussions with officials have envisaged a broad scope including the core Public Service and the health and education sectors, but all Crown entities, a range of other public service organisations, and even the state-funded sector. However, this scope presents risks in terms of broad and uncertain fiscal risks, as well as variation in the ability to ensure alignment of bargaining outcomes.

32. On the other hand, without some breadth of sector coverage, the PSPA will not achieve coordination, alignment and certainty that we are seeking to achieve.

33. We are seeking Cabinet's approval to set the intended scope of a potential PSPA as covering:

33.1. The core Public Service (public service departments and departmental agencies).

33.2. state and state-integrated schools and kindergarten teachers.

33.3. the state-employed health sector, and

33.4. other Crown agents.

34. Appendix 1 includes the estimated costs for each of these components [33], [38]

35. [33], [38]

36. [33], [38]

### ***Negotiating parameters***

37. Risk is mitigated by having clear parameters for negotiation. Unions will need to opt-in to the PSPA process if they wish to negotiate within it. It is appropriate that Cabinet

sets out its objectives and parameters in relation to the fiscal envelope. Those parameters are:

37.1. [33], [38]

37.2.

37.3.

37.4.

## **Implications of the PSPA**

### ***Financial modelling***

38. [33], [38]

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41.

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[33], [38]

42. We will bring a paper back to Cabinet in early 2023 once the majority of the bargaining is completed, [33]
43. We note that meeting the costs of a PSPA will further constrain what are already tight allowances. We also note that not all Budget 2023 wage cost pressures will be met by the PSPA process as there are likely to be wage pressures in sectors and organisations that are not covered in the scope of the PSPA. There will also be some spill-over to higher wages for public sector employees not covered by the proposed PSPA and the contracted and funded sectors.

### **Implications for inflation and interest rates**

44. [33], [38]

Higher public sector wage inflation would boost household incomes and hence household spending. It could increase competition for labour and spill over into private sector wages. Combined, this could add to existing inflation pressure and prompt an interest rate response from the Reserve Bank. The inflation, and hence interest rate, consequences could be larger if the higher public sector wages were at least partly funded by increased government expenditure rather than funded from existing baselines and operating allowances.

45. Conversely, if all public sector wage inflation is funded from within existing allowances, thus largely exhausting scope for any other initiatives, there would be little impact on inflation and interest rates. It should also be noted that, realistically, the counterfactual to agreeing a PSPA is still likely to involve public sector wage inflation above Budget 2022 forecasts.

### **Legal risks**

46. [36]

- 46.1. [36]

- 46.2.



46.3. [36]

47. [36]

### **Aligning bargaining**

#### **Process following approval to proceed**

48. [36]

49.

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51.

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[36]

54.

### **Consultation**

55. There has not been formal interagency consultation on this paper. It has been prepared by Te Kawa Mataaho Public Service Commission and Treasury with input from Health New Zealand, the Ministry of Education, Crown Law, and Simpson Grierson. The Department of the Prime Minister and Cabinet has been kept informed.

### **Financial Implications**

56. Treasury has produced the financial estimates in this paper drawing on information provided by agencies. However, agencies have not reviewed the results given the sensitive nature of the material. As a result, a higher-than-normal degree of uncertainty exists around these estimates.

57. [33], [38]

[33]

58. [33]

59.

60.

61. [33]

### **Legislative Implications**

62. This paper has no legislative implications.

### **Impact Analysis**

63. No impact analysis is needed.

### **Human Rights**

64. The legal advice we have received is that there is a low risk of the proposal being in breach of the freedom of association right under the New Zealand Bill of Rights Act 1990 or being discrimination in relation to political opinion under the Human Rights Act 1993. We will continue to take legal advice on these matters as the proposal proceeds.

### **Gender and Disability Implications**

65. The government's expectations favour an emphasis on addressing the position of lower paid workers in the public sector.

### **Publicity**

66. This Minister for the Public Service and the Minister of Finance will jointly manage communication and publicity about the PSPA.

### **Proactive Release**

67. The joint Ministers propose to release this paper, subject to any redactions of financial advice, following conclusion of negotiations.

### **Recommendations**

68. The Minister of Finance and the Minister for the Public Service recommend that Cabinet:

1. **note** that following an approach from the NZCTU, in relation to a uniform pay adjustment in the state services (the PSPA) the Minister for Public Service asked the Public Service Commission to address certain issues with the NZCTU
2. **note** that the discussions between the Public Service Commission and the NZCTU have concluded, and that it is now timely to decide whether, and in what form, a PSPA could proceed
3. **note** our view that a PSPA would bring a level of coordination, alignment and certainty to bargaining and employment relations across the system and would provide further opportunity to align bargaining outcomes around a fiscal envelope that will allow for collective agreements that provide fair pay to employees, are affordable for government, and aligned with one another

4. [36]
- 5.
6. **agree** that officials proceed with formal negotiations with the NZCTU and its affiliates for a PSPA on the terms detailed in recommendations below.
7. [33], [38]
8. **agree** that negotiations will cover the Public Service, state and state-integrated schools, kindergarten teachers, the Health sector and other Crown Agents.
9. [33], [38]
- 10.
11. **note** that before any PSPA is agreed, it is subject to agreement and ratification from relevant public sector unions;
12. [33], [38]

[33], [38]

13.

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18.

19. **note** that Ministers will write to the NZCTU informing them of the framework for the PSPA set out in this paper.

20. **agree** that the Minister for the Public Service, the Minister of Finance, and the Prime Minister in consultation with relevant Ministers, have power to act in relation to the recommendations in this paper, [33], [38]

21. **note** that the Minister for the Public Service and the Minister of Finance will address communication and publicity in relation to the PSPA strategy.

Authorised for lodgement

Hon Grant Robertson

Minister of Finance

Hon Chris Hipkins

Minister for the Public Service

[33], [38]

[36]



[36]

[36]

[36]



[36]

[36]

[36]