



shopworks

STAFF SCHEDULING

May 2016

“Shopworks special report: The National Living Wage – The UK’s Great Experiment”

What’s in this edition?

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Introduction

The UK government introduced its National Living Wage of £7.20 per hour on April 1st 2016, the first set of bigger pay cheques have been paid out and operators are starting to assess the impact.

At Shopworks we help companies in the retail, leisure, hospitality and service sectors mitigate the impact of the higher staff costs and have held many conversations with our customers about the subject in the last few months. We feel we are particularly well placed to publish a special report which discusses the issues, the impact and the potential actions that operators can take.

This special report is intended to help our customers and others within the sectors most affected to take stock two months in and assist them in formulating the next step in their staffing strategy. It relies a lot on what is happening in the UK right now because the UK is testing something that is being watched throughout the world, which if successful, is likely to be copied in other OECD countries. In an FT article in March 2016 entitled "World watches Britain's "living wage" experiment" Richard Dickens, an economics professor at Sussex University said: "Minimum wages have never been so popular. The next question is: how far can you push it?" At Shopworks we believe that the UK is about to find out.

We hope you find it helpful and would welcome your comments and feedback at info@theshopworks.com



Will Workers Really Benefit?

Under the last Labour Government, then Chancellor of the Exchequer, Gordon Brown, introduced In Work Benefits as a way of encouraging people back to work. In terms of its impact on the unemployment rate it appears to have been a resounding success, reducing the UK rate to 5.1% the lowest in the OECD, despite the UK population rising at unprecedented rates. However the current Conservative government, on a mission to reduce the deficit has introduced the New Living Wage. This has allowed the government to phase out in work benefits and pass the entire cost onto employers. In Work Benefits will fall a little faster than the National Living Wage rises. A family of two, with a single earner on the minimum wage, will actually see their income slide from £14,200 a year now to £14,100 a year by 2020. The increase in the National Living Wage will earn them £4,400 more but higher tax and the loss of tax credits will cost them around £4,600. So even if they work the same hours they will be worse off.

The impact? It is too early to say precisely – the higher rates are being phased in gradually – but there is already plenty of evidence emerging that companies that rely on lots of relatively low-skilled staff are pulling out of those areas or else finding ways to run their businesses with fewer people. The UK has poor productivity and no wonder if the government was subsidising workers with In Work Benefits. This paper discusses the early impact of the changes including some hot air from politicians and some initial cost cutting measures by employers. However in the long term we believe that operators will look at a host of efficiency savings, which will increase productivity, increase unemployment in the service sector and reduce the number of hours worked by staff on minimum wage.

It is yet to be seen if the UK economy adjusts to create new higher skilled workers and more, higher skilled jobs or whether employers simply deliver the same service for less as the unemployment rises towards the EU average of 9.6%. The UK plans to increase the national living wage from 50% to 60% of median earnings by 2020, which would take the UK from the middle of the OECD pack to the upper end. The government chose 60% because a handful of countries such as France and Australia already sustain minimum wages at that level. However this may hold a clue to the likely impact of the National Living Wage; France has unemployment of 10.5% double the UK rate probably as a result of being significantly more productive than the UK. OECD statistics for 2014 show the GDP per hour worked was \$50.5 for the UK, but \$62.7 for France; or 25% greater than the UK. French employers will invest in technology before they take on new staff because of the high costs of employment and the difficulty in letting an employee go.



There are some benefits to employers, in London there is a shortage of quality staff in many sectors especially leisure and hospitality, the changes brought about by the Living Wage may ease that pressure. Also In Work benefits created distortions where staff wouldn't work additional hours for fear of losing benefits, a distortion in the labour market that will now disappear.

As the UK embarks on a huge social experiment, the full impact is unclear, however what is certain is that those workers who are already working 38 hours a week on the minimum wage will be no better off and if they lose working hours as well as benefits they are likely to be worse off in 2020. The UK job market is in for some interesting times as it digests these changes.

5.1%

UK Unemployment Rate



10.5%

French Unemployment Rate



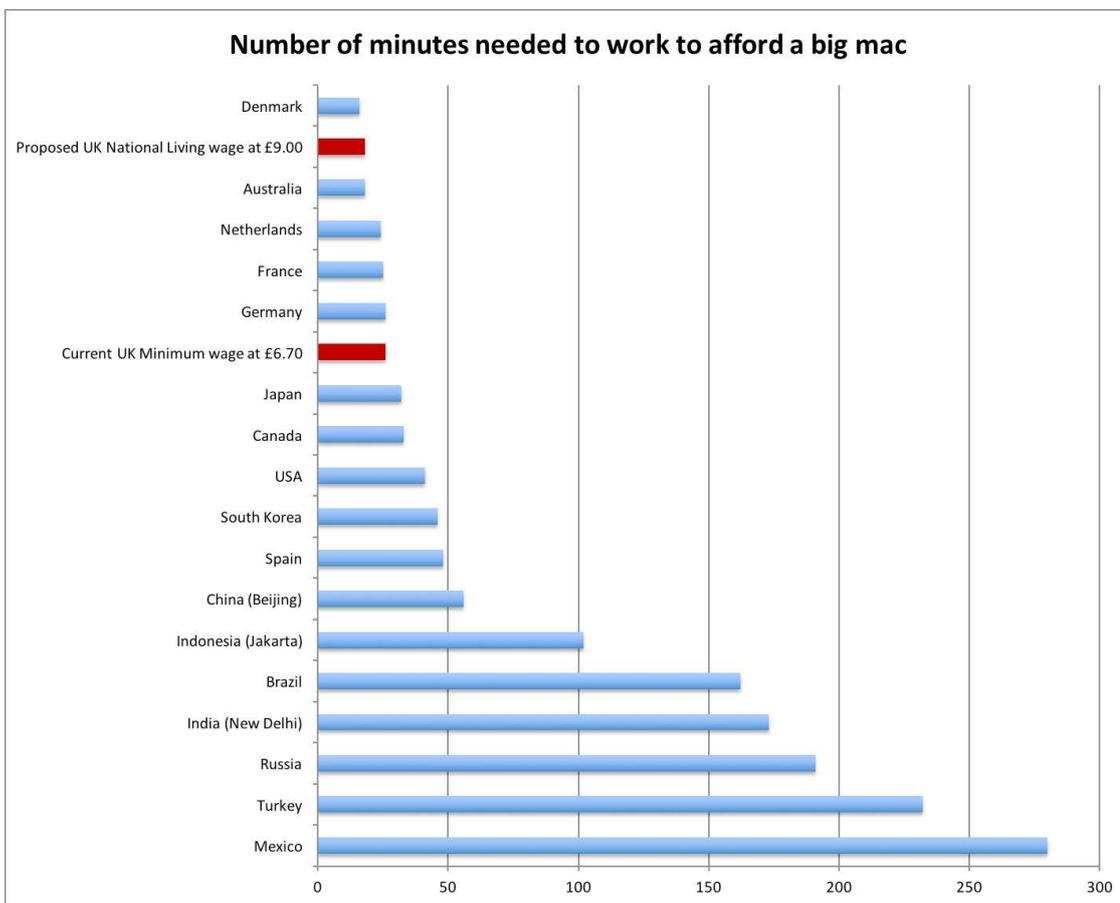
French Workers

25%

More Productive



Big Mac Index



Living Wage Around the World

Minimum wages are now in operation in 26 out of the 34 OECD countries, and 22 EU member states. Germany only joined the list in January 2015 with a minimum wage of €8.50 (£6.57), while some of the EU members without one – that’s Austria, Cyprus, Italy, Sweden, Finland and Denmark – have other mechanisms such as collective agreements and wage floors.

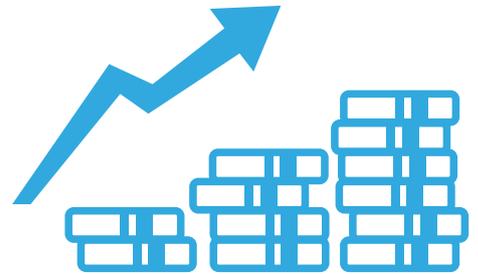
The UK’s minimum wage is similar to the other major EU economies but higher than countries with lower levels of GDP per capita such as Bulgaria, Latvia and Romania. On the traditional minimum wage comparison as a proportion of median monthly earnings, the UK is broadly in line with most EU countries at about 50% but intends to raise it to 60%.

Outside of Europe, New York, Seattle and California have recently pushed through increase in the minimum wage to \$15 an hour, which will make them among the highest in the world.



65%

Of employers say they would raise prices if the minimum wage increased to £10 per hour.



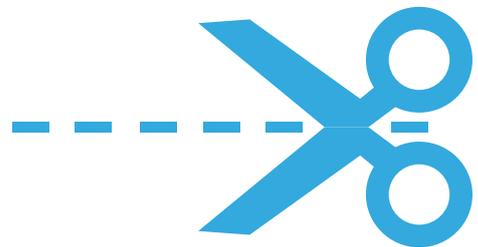
£9

Is the expected minimum wage in 2020



38%

Of employers say they would cut workforce if the minimum wage were to increase to £10 per hour.



What is the National Living Wage?

Basics

There is some confusion about terminology between minimum wage and living wage. The minimum wage applies to workers under 25 – an apprentice gets £3.30 someone under 18 gets £3.85, a worker between 18 and 20 gets £5.30 whilst someone between 21 and 24 gets £6.70. The National Living wage is the governments re brand of the Minimum Wage for people over 25 and is currently £7.20 but will be increasing to £9.00 per hour by 2020. The National Living Wage is essentially a different age threshold band of the Minimum Wage, which will end up 38% higher than the 2015 minimum wage.

The new rate was payable from April 1st 2016. Tips and service charges don't count towards the Minimum Wage or the National Living Wage, whether they are mandatory and paid through the payroll or whether they are given at the discretion of the service user. As we will discuss later, an employer has no legal obligation to hand over tips.

Other New Staff Costs

In addition to the National Living Wage, the UK Government has also passed on other social costs to employers in recent years.

- Auto enrolment of pension obligation means that employers pay 1% until April 2018, 2% until April 2019 and then 3% of salary going forward.
- The apprenticeship levy requires all employers operating in the UK, with a pay bill over £3 million each year, to pay 0.5% of the companies annual pay bill.
- The headline employers National Insurance rate in the UK now stands at 13.8% having steadily risen from 10% in 2003.

What about the Living Wage Foundation?

There are a number of different definitions of living wage in the UK which causes some confusion, so let us clear these up:

Minimum Wage: The UK Governments old name for the National Living Wage, which still lives on for under 25's.

National Living Wage: The UK Governments new name for its legal minimum wage for employees over 25.

Living wage foundation: This not for profit organisation publishes a voluntary hourly rate set independently and updated annually which they say is calculated according to the basic cost of living in the UK. Their current UK Living Wage is £8.25 an hour and £9.40 an hour in London. Employers can choose to pay the Living Wage on a voluntary basis and receive recognition from the Living Wage Foundation in return.



Impact and News

The British Retail Consortium predicted the introduction of the national living wage could cost retailers between £1billion and £3billion a year. Employers are expecting to award average pay rises of just 1.7 per cent this year, according to the latest CIPD Labour Market Outlook, which suggests government- imposed increases in labour costs such as the National Living Wage and the apprenticeship levy are weighing on balance sheets. The survey of more than 1,000 employers – covering the 12 months from March 2016 to March 2017 – found that around a third expected the National Living Wage to raise average salaries by 2 per cent. But 21 per cent said the wage would be a factor in weaker pay awards. In another survey by insolvency trade body R3; 23% of businesses revealed their concerns about the impact of auto-enrolment pensions, surprisingly this exceeded the 18% who were worried most about the introduction of the National Living Wage and the 6% who were concerned by the introduction of an Apprenticeship Levy. Brexit was also a major concern but as Andrew Tate, R3 president said “Brexit might not come to pass, auto-enrolment pensions and the National Living Wage will definitely have to be dealt with by businesses,”

The Investors View: Impact on Valuations

We spoke to Jason Katz, Founding Partner of Kings Park Capital who invest exclusively in companies that operate within and provide services to the leisure sector, which encompass hotels, travel, health & wellbeing, gaming, bars & restaurants and visitor attractions. “ We are finding that investor appetite for and valuation multiples of operators with high staff costs are under pressure, especially where there is perceived to be little scope to pass on these rising costs. When we speak to the operators in our network, staff management and cost control are absolutely at the top of their agenda. Companies that help operators improve their labour productivity and save money are in demand. Cloud based HR software companies, like Shopworks, which specialize in work force management should be very well placed to grow rapidly in this environment.”

Sectors Under Pressure

There is no doubt that some industries are under particular pressure. Research indicates that the National Living Wage has had an immediate and significant impact on employers: one study suggests that just under 60,000 businesses are already in a “dire financial state” and will be “stretched to breaking point”. Companies in the retail, hospitality and leisure sectors are reckoned to be among those most affected as they tend to rely on lower paid labour. There are almost 150,000 hotels, pubs and restaurants in Britain, employing about two million people and that sector is particularly at risk. Two areas in particular have received a lot of coverage about the impact the National Living Wage will have on their



profitability and we discuss those here: Fruit farming: This is highly labour intensive but is an industry which faces strong foreign competition and a supply chain with supermarkets at the top who are themselves engaged in a price war whilst coming to terms with the National Living Wage. According to a recent National Farmers Union report which revealed that the impact of the new minimum pay threshold could cost growers 58% of their profits immediately while over the next four years it could cost fresh food businesses up to 158% of current business profit, making activities such as strawberry growing completely unprofitable for British farmers without extra government support. Care Homes: Another labour intensive business, which struggles to pass on extra costs is the care home sector. In this case cash strapped local governments are the main customer. More than a quarter of care homes in the UK are in danger of going out of business within three years. Research carried out for Radio 4's You and Yours programme by business risk analysts found that about 5,000 homes are at risk of closure. On average, care homes only make £17,647 in profit before tax which is expected to be exceeded by the increase in labour costs by 2020, the research found. John Strowbridge, managing director of Avery Health Care Group, which operates 47 care homes across England, said the new living wage was costing it an additional £2m a year. Mr Strowbridge added: "And if it continues, as it will do with the national living wage into next year and the year after, the number of local authority clients that care homes can admit across the country, will continue to be reduced."

The Optimistic View

It should be noted that many employers are seeking to grasp the minimum wage as an opportunity and are absorbing it with enthusiasm. These companies are keen to invest in their staff and ensure high morale and good retention. The Living Wage Foundation lists many companies that pay above the National Living Wage although not many are in under pressure sectors such as hospitality or care homes. There are exceptions though; Accor hotels pays the National Living Wage to all employees regardless of age and the JD Wetherspoon pub chain is taking a generous approach. Tim Martin, the chairman and founder has vowed not to chip away at benefits: "I'm not going to cut any perks for employees as a result of the national living wage. About 40% of our profits go to staff in the form of bonuses and free shares, and there are no plans for that to change."

There are also plenty of economists who believe that the National Living Wage will confound the skeptics. Alan Manning, a professor at the London School of Economics says "My view of the history of minimum wages is that we've always been surprised about how you seem to be able to push them up without harming job prospects," He also points out that the modeling being done for minimum wage experiments in US cities like Seattle is encouraging. These analyses suggest low-paid workers will spend more money in the local economy, boosting local demand and creating a virtuous circle for employers and employees. receive recognition from the Living Wage Foundation in return.



1.3 million

People in the UK will benefit from the rise



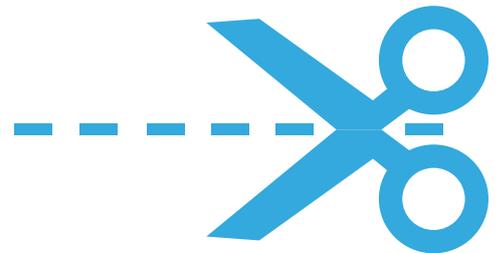
3%

The employers pension contribution by 2019



4 million

Hours per week to be cut by employers



Mitigation

With any increase in costs, businesses will look to make savings elsewhere and these wage related rises are no different. We looked at how companies are mitigating the costs and the reaction so far.

Automate

As we have discussed above, the UK has a productivity issue being 25% less efficient per hour than France and the Government is hoping that the National Living Wage will help improve this. Launched in July 2015 the Productivity Plan is the government's strategy to increase the efficiency of the UK economy. It sets out 15 areas for government action, including taxation, skills, digital infrastructure and research & development. The launch of the plan was when the government formally announced its plans for an Apprenticeship Levy and a National Living Wage which are both key planks of the strategy. The National Living Wage will hopefully drive the UK to become a highly productive high skill economy but it will almost certainly have an impact of low skilled jobs with many being automated. This trend has been evident in France for some time. We are starting to get used to self service check outs at super markets, pay by text parking and pay at the pump petrol as employers seek to replace people with technology and we see no sign that this will do anything but accelerate. In the United States where New York and California have recently increase their minimum wages to \$15 an hour. There is already plenty of evidence emerging that companies that rely on lots of relatively low-skilled staff are finding ways to run their businesses with fewer people. Restaurants are switching to iPad menus instead of waiters where you can order your food on a tablet and the order arrives instantly in the kitchen. One of Shopworks customers in the hospitality sector with 7,000 staff is trialling just such as system and US restaurant operator Wendy's recently said it would automate many of its was 6,500 restaurants because of the increase in the Minimum Wage. In all of Shopworks Casino customers, electronic roulette and black jack tables are becoming more prevalent as employers look to reduce their staff bill.

Change Contract Terms

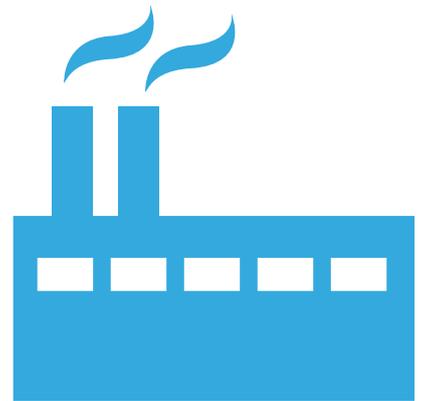
In the UK the most likely way to get some unwanted publicity appears to be to change the existing contract terms of staff. Companies doing this are trying to reduce the amount paid to staff for the same number of hours worked and the most popular changes include removing paid breaks, reducing the rate of pay for overtime and Sunday working and reducing the amount of money being paid in tips.



It is always harder to change terms for existing staff and this is causing some bad PR for those firms doing it, which is why lots of companies are changing the terms of employment for new staff to ensure they are paid the National Living Wage and no more. This strategy is less controversial and is helped by good systems, which are capable of tracking multiple different pay rates. It is most effective in sectors with high staff turnover rates such as Hospitality.

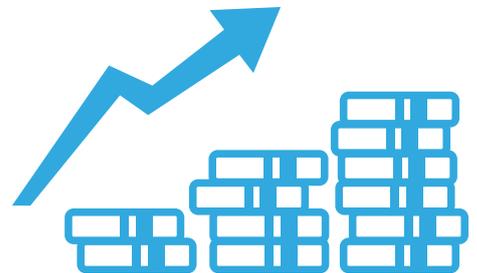
£11 billion

Will be the total cost to industry



April 2016

The minimum wage rose from £6.70 to £7.20



£1BN to £3BN

Extra cost per annum to retailers



Systems to ensure correct payment levels

We know a lot about these systems as Shopworks has been making its cloud based system available to operators since 2009 and is saving companies an average of 7% of their hourly paid staff costs through cutting out over payment and ensuring rosters are checked against budget before they are signed off. These systems cut out "timesheet fraud" by using biometrics and matching the scans against the scheduled roster. They avoid double payment, ghost hours and other overpayment. They are less contentious than some of the other mechanisms as they simply ensure that a company's payroll is 100% accurate and people are paid exactly what they are due. They also provide other benefits such as self-service time off management and demand management to ensure that stores aren't understaffed at peak times.

Some Companies Making Changes

The majority of news coverage about UK operators reacting to the National Living Wage cover businesses looking for ways to mitigate the increase. Shopworks has seen a huge increase in interest in its cloud based work force management system since the National Living Wage was announced and the UK press has been full of examples of companies that have looked to change their terms and conditions. Some of the new coverage includes:

- "Waitrose staff perks go 'to pay for living wage': Supermarket stops paying Sunday and overtime rates for new workers."
- "Belgian coffee shop chain Le Pain Quotidien halted paid breaks for staff just before the introduction of the National Living Wage"
- "Food chain Eat also sought to offset costs by not paying staff for their 30-minute break - saving it £3.60 per employee per shift if they receive the National Living Wage."
- "Italian restaurant chain Zizzi has cut the share of customer tips that goes to its waiters in response to the National Living Wage - and it has also restricted free food for its staff."
- "Morrisons, and Cafe Nero have also responded to the new wage rate by developing new terms and conditions for employees."

These changes all affect existing staff contracts, at Shopworks we are seeing lots of changes to contracts for new employees. We were recently asked to implement a new staff contract for a leisure operator; for all new joiners based on the minimum wage age thresholds. We changed our system so that on the employees 18th, 21st and 25th birthdays they receive an automatic pay rise at midnight on the day of their birthday. This new contract type works alongside the operators existing contract types and will help them manage their cost base as they replace leavers with staff on the new terms.



Political and PR Backlash

It probably doesn't come as a surprise that having passed the responsibility for more social costs onto businesses, politicians have followed this up with a bit of "witch hunt" against operators that are looking to mitigate the costs. Several businesses have been put under pressure as they look to reduce the impact of the National Living Wage. This has materialized as negative press comment, aggressive social media campaigns and also protests against the now familiar target of Top Shop's Oxford St Store.

Chancellor George Osborne has said firms that cut free staff lunches or reduced breaks would be "outed" and see their reputations hit as a result. He said: "It makes me angry. One of the things I'm proudest of doing in this job is introducing the national living wage. Companies are no different from people - we've got responsibilities and should abide by them."

The chancellor also said that those cutting paid breaks, Sunday pay, free food and overtime were "acting against the spirit of the law." In addition to political pressure, the Government is already discussing legislation to cut off potential routes of mitigations, in response to several companies changing the way they distribute tips to hospitality staff.

"Waiting staff should receive their tips in full and it should be clearer to customers that gratuities are optional" Sajid Javid the business secretary has said, a tip had to "go to the people you intended it to go to" and announced proposals to stop or limit employer deductions from tips.

Currently, there is no legal requirement for firms to hand over gratuities to their waiting staff and many operators already retain the service charge and may now be required to distribute their service charge on top of the increase in the National Living wage.



Legal

Penalties for Non-payment of NLW

Penalties can be imposed for not paying the National Living Wage, which are:

- 200 per cent of the amount owed (reduced to 100 per cent) if paid within 14 days
- A maximum fine of £20,000 per employee underpaid
- Those responsible for non-payment banned for being a company director for up to 15 years.

In addition, it is counts as unfair dismissal to sack someone aged 25 or over to avoid paying the National Living Wage or select someone for redundancy.

How many people underpay?

THE number of people paid less than the minimum wage has doubled in the space of just a year and UK workers are owed a total of £68 million. In a recent report published by the National Audit Office (NAO) estimated that 209,000 workers are paid less than the minimum wage. And 58,000 were identified as being owed arrears in the 2015-16 financial year, up from 26,000 in 2014-15.

Investigators found cause for particular concern about the social care sector, where private outsourcing and bit payments for workers mean many do not receive the minimum wage. The NAO had previously estimated that 10.6 per cent of care workers may be paid less.

Legalities of changing contracts

In the UK it is generally against the law to change an employees terms of employment without their agreement, employers doing so risk a breach of contract claim.

An employee could claim that they had no alternative but to resign from their employment due to a pay cut if they claim that it fundamentally undermines the employment relationship. In this case, the employee can claim "constructive dismissal".

A company is allowed to change the key terms of employment without the agreement of the employee where they have a "pressing business need". Although agreement should always be sought and there has to be a period of consultation where the Employees are given the opportunity to have their say.



What can Shopworks Workforce Management System do for my Business?

We provide systems for a number of operators but have been very busy with new customers since the Living Wage was announced because operators are finding this difficult to absorb.

Shopworks use biometric readers to remove all “ghost hours” alongside a cloud based system to monitor spend against budget and ensure there is no overspend. These systems are helping operators reduce the number of hours they pay for. As the Office for budget responsibility forecast “the living wage is expected to reduce hours worked by four million a week”, systems like Shopworks help operators remove those hours.

We have evidence from several retailers and leisure operators that changed from managing staff via spreadsheets to our full blown staff scheduling system and saved up to 12% of their hourly paid staff costs – all by paying for less hours.

As wages rise, making sure that each member of staff is correctly remunerated is vital. Unnecessary expenditure must be eliminated and staff costs are a great place to start.

Tightening up payroll processes can also have a positive impact on employee motivation. If an employee is not paid correctly and on time, their motivation will undoubtedly drop and time will be spent on complaints to payroll.

Introducing employee self-service via smart phones removes payroll complaints, ensures that staff understand where they are meant to be and when, makes leave administration more efficient and frees up management time.



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STAFF SCHEDULING

If you would like a demonstration of the Shopworks system or want to discuss how our system can help you mitigate the impact of the National Living Wage, please contact mike@theshopworks.com