FILED
03 Sep 2024
OFFICE OF THE INDUSTRIAL REGISTRAR

THE SEAL OF THE INDUSTRIAL RELATIONS COMMISSION OF NEW SOUTH WALES

EXHIBIT JW-1

IN THE INDUSTRIAL RELATIONS COMMISSION OF NEW SOUTH WALES AT SYDNEY

No: **2024/00211169**

STAGE WAGE CASE 2024

EXHIBIT NOTE

Exhibit JW-1 to the affidavit of Joann Wilkie

Date: 3 September 2024

Filed for:
Industrial Relations Secretary

This is the exhibit referred to as "JW-1" in the affidavit of Joann Wilkie affirmed before me on 3 September 2024.

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NSW Treasury

Productivity Considerations

For the Industrial Relations Commission of New South Wales Review of Wage Fixing Principles

23 August 2024

NSW GOVERNMENT

Acknowledgement of Country

We acknowledge that Aboriginal and Torres Strait Islander peoples are the First Peoples and Traditional Custodians of Australia, and the oldest continuing culture in human history.

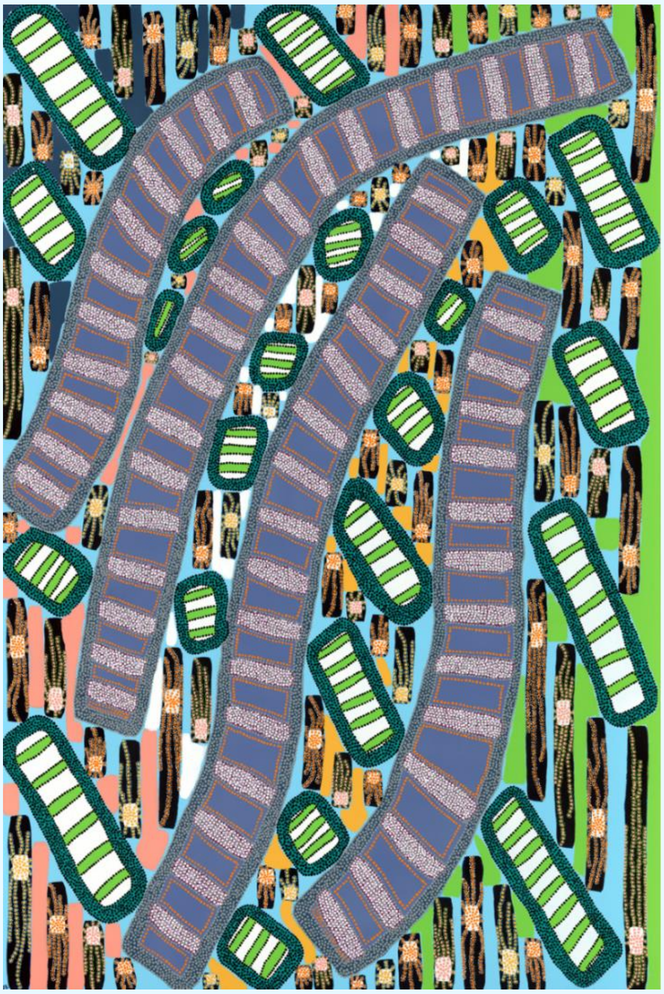
We pay respect to Elders past and present and commit to respecting the lands we walk on, and the communities we walk with.

We celebrate the deep and enduring connection of Aboriginal and Torres Strait Islander peoples to Country and acknowledge their continuing custodianship of the land, seas and sky.

We acknowledge the ongoing stewardship of Aboriginal and Torres Strait Islander peoples, and the important contribution they make to our communities and economies.

We reflect on the continuing impact of government policies and practices, and recognise our responsibility to work together with and for Aboriginal and Torres Strait Islander peoples, families and communities, towards improved economic, social and cultural outcomes.

Artwork:
Regeneration by Josie Rose



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Productivity and efficiency considerations

1. Purpose

1.1. The Industrial Relations Commission of New South Wales (IRC) is conducting a broad review of the form and content of the IRC's wage fixing principles.

1.2. The IRC has invited submissions on "Whether and to what extent sub-principle 8.3 (Productivity and Efficiency Considerations) ought to be amended, or some other mechanism introduced to expand, clarify and/or refine the concept of public sector productivity and efficiency and, in particular, the relevance of and relationship between improvements in the quality of public sector services and employee-related costs."

1.3. This paper outlines matters NSW Treasury considers relevant for defining, assessing and measuring productivity enhancing reforms in the NSW Government industrial relations context, to support the IRC in its review.

2. Defining productivity

Productivity is an economic concept relating to real inputs and outputs

2.1. According to the Reserve Bank of Australia, *"productivity refers to how much output can be produced with a given set of inputs"* (RBA, 2024). It reflects how well an economy, industry or organisation utilises its resources to generate goods and services.

2.2. Productivity improvements are changes that allow more output to be produced with a given set of inputs. For example, a process redesign that allows the same number of surgeons (given inputs/labour hours) to undertake more life-saving surgeries (increased output volumes), is a productivity improvement, assuming there was no offsetting decline in quality of surgery or increase in other inputs.

2.3. Closely related to productivity is efficiency. Being more efficient can be one way to improve productivity.

2.4. Higher productivity is the main source of real per capita income growth in the long term and helps to improve living standards and national wellbeing (Australian Government, 2023).

There are many ways to improve productivity

2.5. Productivity or efficiency improvements in the public sector could arise from:

2.5.1. delivering the same service (quality or quantity) with fewer inputs (i.e. efficiency). For example, processing the same number of licence applications using fewer labour hours through a change in processes (all else being equal)

2.5.2. delivering a better service (quality or quantity) with the same inputs. For example, extending operating hours of a service through changes to rostering, without changing staff hours overall (all else being equal)

2.5.3. achieving a large reduction of inputs, with a slight reduction in service quality/quantity. For example, digitising a service may slightly reduce customer experience but with a large reduction in the staffing hours required for service delivery (all else being equal)

2.5.4. achieving a large improvement in service quality/quantity, with a relatively small increase of inputs. For example, implementing telehealth consultations might require a modest upgrade to IT equipment, but greatly improve services to remote areas (all else being equal).

2.6. The following do not constitute productivity or efficiency improvements:

2.6.1. gaining a small improvement in output with a proportionate or relatively large increase in inputs

2.6.2. achieving a small reduction in inputs with a proportionate or relatively larger reduction in service quality/quantity

2.6.3. gaining a small improvement in quality, with no extra inputs, but with a relatively large reduction in output

2.6.4. slightly boosting output, with no extra inputs, but with a relatively large reduction in quality.

2.7. Common drivers of public sector productivity include:

2.7.1. improving management practices

2.7.2. more effective/efficient working practices or processes

2.7.3. creating a culture of continuous improvement and innovation

2.7.4. adopting technology and/or infrastructure that make processes more efficient overall (for example, effective use of data, technological advances, effective use of ICT, better use of data)

2.7.5. ensuring workers' skills and competencies are fit for purpose (both technical and soft skills)

2.7.6. using markets and/or competition to strengthen incentives (new entry and market creation)

2.7.7. reducing red-tape to encourage efficiency and/or innovation

2.7.8. service redesign and alternative delivery mechanisms (prevention/early intervention)

2.7.9. responding to context specific needs, especially regional or local requirements

2.7.10. establishing governance, accountability, and measuring and incentivising performance

2.7.11. improving resource allocation (reconfiguring services) and budgeting.

2.8. Every decision government makes involves a trade-off between different uses of resources. Some reforms may be productivity enhancing, but not as much as alternative reforms.

Productivity is not a financial concept, but financial variables can impact it

2.9. Productivity relates to real inputs like labour hours, machinery, land, technology, and real outputs like goods and services. Factors like revenue, expenditure, wages, profit, financial costs, capital expenditure (etc.) are financial variables not real variables, and so do not factor directly into productivity.

2.10. Changes to financial variables can, however, impact productivity when they influence real inputs and/or real outputs. But these impacts are often indirect and have to be established in the circumstances. For example, all other things being equal, increasing wage rates does not directly change productivity, whereas increasing labour hours does. A higher wage rate may, however, in practice divert funding from other uses and in doing so indirectly impact real inputs and outputs and hence productivity.

2.11. Productivity reforms may or may not result in fiscal savings, and fiscal savings may or may not improve productivity. The Government takes the fiscal impacts of proposed productivity reforms into account when considering them, as well as its broader fiscal position and objectives.

2.12. The IRC has specifically invited submissions to address the relationship between an improvement in the quality of public sector services and employee-related costs. Some points are relevant in relation to this:

2.12.1. changes in employee-related costs may or may not improve public services

2.12.2. improvements in public services may or may not result in or be caused by changes in employee-related costs

2.12.3. establishing the relationship requires an analysis of the circumstances as the relationship will differ from setting to setting

2.12.4. an improvement in the quality of public sector services does not necessarily indicate that productivity has improved, as this would also require an analysis of whether and how inputs have changed too

2.12.5. employee-related costs is a financial variable and does not directly factor into productivity (whereas real inputs like labour hours do).

3. Considerations when assessing productivity enhancing reforms in exchange for wage increases

A principles-based approach should be used to assess whether a measure constitutes a productivity enhancing reform that may warrant enhanced wages and/or conditions

3.1. Various factors will likely need to be considered when assessing whether a productivity enhancing reform could be exchanged for enhanced wages and/or conditions. One factor on its own will not necessarily rule a reform in or out. The merits of each proposed reform should be assessed on a case-by-case basis

3.2. Some of these factors are already covered by sub-principle 8.3 (Productivity and Efficiency Considerations), including that that the reform delivers substantial benefits, that employees make a significant contribution to the reforms, and that benefits can be measured.

3.3. Productivity enhancing reforms that may be *less likely* to warrant additional enhancements to wages and conditions include those that: (note: this list provides a guide and is not exhaustive)

3.3.1. **are not substantial:** The scale of the reform(s), relative to the size of the workforce, is a consideration. A reform may be substantial, for example, because it delivers substantial cost savings or productivity improvements, or delivers significant improvements in the way work is undertaken. The value of the reform should be considered against the cost of the enhanced wages and/or conditions

3.3.2. **require limited or no contribution from the employee**: Employees should make a significant contribution to productivity gains that are proposed to be exchanged for enhanced wages and/or conditions. Streamlining processes to improve outcomes for citizens may deliver productivity gains but may also result in reduced effort by employees. The role of the employee is an important consideration.

3.3.3. **have already been recognised:** Productivity enhancements should not be double counted, meaning if the reform is recognised already through enhanced wages and/or conditions, it should not be provided as justification for additional changes to wages and/or conditions at a later date

3.3.4. **already provide benefits to employees:** Reforms may deliver non-monetary benefits to the employee, such as enhanced employee-centred flexibility. Non-monetary benefits should be factored in when determining whether enhanced wages and/or conditions are appropriate

3.3.5. **are not measurable**: In every workforce, there should be direct or proxy measures of inputs and outputs, including their quality and quantity. This provides a suite of productivity indicators that together can support measurement of productivity gains.

3.4. Productivity gains should be shared between the employer and the employee. The appropriate split of gains being directed towards enhanced wages and/or conditions (as opposed to returning to the government as savings or to fund new services or infrastructure) should be determined having regard to a number of factors, including the role of the employer/employee in realising the productivity gains.

4. Measuring productivity in a public sector context

Productivity enhancing reforms should be measured using a context-specific approach

4.1. Two common macroeconomic approaches of measuring productivity are Labour Productivity (LP), which considers labour as an input to production, and Multi-Factor Productivity (MFP) which considers multiple inputs (labour, capital, technology, etc). However, published indicators of these measures do not accurately capture public sector productivity, as the calculation of LP and MFP requires a value attributed to the output of the market.[1] Public sector outputs or services are often difficult to value as they may be either free of charge or not priced in a market.

4.2. As a result, in public sector settings, productivity is generally measured through a range of indicators and proxy measures relating to the relevant inputs and outputs of a specific workforce or setting. There is no single measure of productivity across the public sector. The appropriate measure or suite of measures will differ depending on the service delivery or policy context. These measures can be quantitative and/or qualitative.

    4.2.1. For example, in a hospital setting, we can measure inputs like doctors' work time, and medical equipment, and outputs like medical procedures delivered. In a school setting, we can measure inputs like teachers' work time, and educational resources, and outputs like lessons delivered.

4.3. NSW Treasury uses a context-specific approach underpinned by economic principles to measure productivity enhancing reforms in an industrial relations setting. In general, this will involve measuring and assessing claims of public sector productivity:

    4.3.1. by considering changes in inputs relative to outputs (for example, changes in service delivery (quantity or quality) per hour worked, or more efficient resource allocation that enables the same level of service delivery with fewer resources);

    4.3.2. over an appropriate time period (generally over a period of several years, considering productivity gains take time to materialise, and that reforms should deliver sustained gains in productivity rather than a temporary uplift); and

    4.3.3. with regards to the employee's contribution to the productivity reform in question (rather than capturing Government investment in capital, technology, etc), including the role of the employee in realising the productivity gains, and the significance of the change required.

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[1] Australian Bureau of Statistics (2020); Non-market output measures in the Australian National Accounts: a conceptual framework for enhancements, Released 31 August 2020,

https://www.abs.gov.au/statistics/research/non-market-output-measures-australian-national-accounts-conceptual-framework-enhancements-2020#the-measurement-challenge.

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