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Palestine Economic Policy Research Institute (MAS)

**تقييم الامتثال لنظام الحد الأدنى للأجور
في المحافظات الشمالية (الضفة الغربية)**

**Evaluation of Employers' Compliance with the
Minimum Wage Regulations in the West Bank**

بلال الفلاح

Belal Al-Falah

2014

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Founded in Jerusalem in 1994 as an independent, non-profit institution to contribute to the policy-making process by conducting economic and social policy research. MAS is governed by a Board of Trustees consisting of prominent academics, businessmen and distinguished personalities from Palestine and the Arab Countries.

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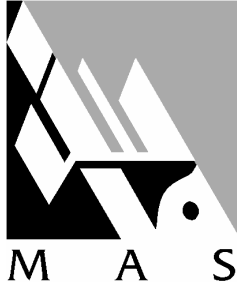
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- ♦ Evaluating economic and social policies and their impact at different levels for correction and review of existing policies.
- ♦ Providing a forum for free, open and democratic public debate among all stakeholders on the socio-economic policy-making process.
- ♦ Disseminating up-to-date socio-economic information and research results.
- ♦ Providing technical support and expert advice to PNA bodies, the private sector, and NGOs to enhance their engagement and participation in policy formulation.
- ♦ Strengthening economic and social policy research capabilities and resources in Palestine.

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Foreword

Fixing the level of a minimum wage for workers is a controversial issue among economists. However, most countries have legislated minimum wages for their workers; Palestine did that as well at the end of 2012 and started applying the legislation as of the beginning of 2013.

Legislating a minimum wage was the culmination of strenuous efforts that went on for a whole year and involved tough negotiations and discussions between the government, private sector employers and workers' representatives. The Palestine Economic Policy Research Institute (MAS) played an active role in these efforts, facilitating the meetings and providing technical support and lectures by specialists on the subject. Despite differences between the parties, in particular on the level of the minimum wage, reaching an accord was in and of itself a positive move towards meeting a stipulation of the Palestinian Labor Law that waited too long to be fulfilled, and towards realizing a higher level of social justice through curtailing poverty, narrowing the wage gap, and curbing the exploitation of workers, especially female ones.

As MAS had been following the efforts exerted by the concerned parties, who worked tirelessly to have the idea of a minimum wage approved and then saw to it that an accord on the minimum wage is reached, it was incumbent on MAS to continue to be involved with the issue and to conduct a careful evaluation, after the lapse of an adequate period of time after its going into force, of the extent to which the minimum wage legislation has been complied with, which is most important. This evaluation resulted in important findings and recommendations that are presented in this publication, which we hope decision-makers will be able to make utmost use of.

On behalf of MAS, I thank the Friedrich-Ebert-Stiftung for providing funding that made this study possible.

Nabeel Kassis, PhD
Director General

Executive Summary

Adopting a national minimum wage is widely considered to be an important tool for enhancing social justice and the well-being of disadvantaged workers. Proponents of minimum wage policy suggest that it helps minimize the wage gap, reduce poverty levels, and prevent exploiting workers, mainly in cases when high unemployment reduces wages below socially acceptable levels. Still, many developing countries struggle with implementing this policy and thus have gained little of its presumed social benefits.

In October 2012, after almost a year of negotiations between representatives of the government, employers, and workers, the Palestinian Council of Ministers ratified regulations that set a national minimum wage for Palestinian workers in the occupied territory. The minimum wage was set at NIS 1,450 per month, NIS 65 per day, and NIS 8.5 per hour. The regulations were slated to go into effect on 1 January 2013, while the interim period (from October until the end of 2012) was to be utilized to settle wage disputes between workers and employers in firms that pay below-minimum wage.

This study aims to explore the demographic, geographic, and economic characteristics of workers in the West Bank who earn below the set minimum. It also aims to assess the extent of employers' compliance with the minimum wage between the beginning of January 2013 and the end of March 2014. This timeframe was selected based on the limits of the available data. With a very weak compliance rate, as the analysis shows, the study aims to isolate the key factors that have led to this outcome. Finally, the study recommends appropriate steps to enhance compliance among employers.

This study uses data from the Palestinian Central Bureau of Statistics (PCBS)'s labor market surveys from 2009 through the first quarter of 2014. It also makes use of primary data from interviews conducted with representatives of the government, employers, employees, and various NGOs, including the International Labour Organization (ILO). It further draws on various reports issued by the Inspection and Monitoring Department of the Ministry of Labor, especially the inspection and labor protection report of 2013 as well as the mid-year inspection report of 2014.

The results indicate that 23% of all waged workers in the West Bank earned below the minimum wage. Still, the percentage rose to 32.3%,

among workers in the private sector. Despite the mandatory nature of the minimum wage and its inclusion of all workers, 4% of public sector workers earned sub-minimum wage salaries.

Predictably, the characteristics of workers earning below the minimum wage are distinct. In particular, their ratio was higher among females, the less educated, and the younger cohorts; they were also concentrated in a few economic sectors. In terms of gender, about 31% of all female workers earned less than the minimum wage, including 51% of all female workers in the private sector. This corresponded to 21% of all male workers and 28% of male workers in the private sector.

In terms of education, the results show that the percentage of workers earning below minimum wage decreased with the level of education, especially for males. Specifically, about 74% of male sub-minimum wage earners did not receive a high school degree, relative to 46% for females. Still, about 26% of female workers with a Bachelor's degree earned below the minimum wage, compared to only 5% of males. In terms of differences across age categories, the results show that more than half of males (57%), who earned below the minimum wage, were younger than 24 years of age. As for females, the highest percentage was in the 25-34 years category.

Distribution across economic sectors is another distinct factor. About 55% of all workers earning below the minimum wage were employed in trade and manufacturing. The results also show that the distribution varies by gender. Specifically, 81% of female workers in the manufacturing sector, mainly in the textile industry, received below the minimum wage, compared to 31% among males, who mostly worked in the food, metal, and furniture industries. As for trade, the percentage rose to 71% for females, compared to 34% for males. The results also show that below minimum wage earners in the private daycare sector were overwhelmingly female (30 out of 32%). Markedly, around 63% of all female workers earning below the minimum wage worked in the textile, trade, and daycare industries.

In terms of firm size (measured in terms of the number of workers), the results show that the percentage of workers earning below the minimum wage generally decreased with firm size. Still, there are variations by gender. About 53% of male workers in this wage category worked in small firms (fewer than 5 workers) as opposed to 28% for females. Nonetheless, in large firms, the share for females (27.5%) was about twice the share for males (14%). As for the geographical distribution, the percentage of workers earning below the minimum wage was the highest in Jenin,

Tubas, Nablus, Qalqilia, Jericho, and Hebron, while it was lower in Ramallah and Salfit.

The results also show that the median wage for sub-minimum wage earners was NIS 1,000 per month and NIS 50 per day. In addition, the median wages among sub-minimum wage male workers was NIS 1,050 per month (NIS 50 per day), while it decreased to NIS 800 per month (NIS 40 per day) for females. Moreover, the median monthly wage was also sensitive to the economic sector. For example, the median wage for sub-minimum wage earners in daycare was NIS 700 per month in daycare, NIS 800 in financial services, and NIS 1,200 in the hotels and restaurants sector. There was also geographic variation with a median wage of NIS 700 per month in Tubas and NIS 800 in Jenin, reaching as high as NIS 1,200 in Jericho.

Using probit analysis, this study attempts to isolate the gender effect on the likelihood of earning below the minimum wage. The results show that when considering all workers, females were 32% more likely to fall into this wage category, while the probability increased to 43% in the private sector. This indicates that employers discriminate against female workers.

As for the extent of compliance with minimum wage, the results show that the percentage of sub-minimum wage workers within the private sector dropped by 3 percentage points (equivalent to 12%) during the studied period. Markedly, this percentage dropped by one point in the public sector (from 5% to 4%, i.e., by 20%). The results also demonstrate that the decrease in non-compliance with the minimum wage took place mostly among males working in trade (9 percentage points) and manufacturing (4 percentage points), mainly in the food and furniture industries. Considering variations across West Bank governorates, a statistically significant decrease in non-compliance took place only in Hebron, Tulkarm, Nablus, and Qalqilia.

This study also sheds light on the nature of the drop in non-compliance and tries to ascertain to what extent this drop was driven by employers' compliance versus changes in the wage trend that is often linked to shocks in the labor market. To explore this aspect, the study traces changes in the share of workers earning below the minimum wage in the two years (2011 and 2012) preceding the implementation of the minimum wage regulations. The results show that the drop in non-compliance during this period (2 percentage points) was close to that in the implementation period (3 percentage points). This suggests that the bulk of

the decrease in the percentage of workers earning below the minimum wage can be attributed to changes in the wage trend. The result is in agreement with what was learnt from tracing changes across industries or governorates that witnessed a percentage decrease for this section of workers.

Exploring the main reasons behind the worryingly weak compliance rate, this study focuses on the relationship between excess labor supply and decreases in wages as well as the extent to which employers are voluntarily motivated to comply with the minimum wage. The study also takes into consideration the role of the government and evaluates the governmental mechanisms which targeted enhancing the compliance rate.

The results show that excess labor supply, measured via the unemployment rate, affects compliance negatively. Utilizing probit analysis, the findings show that increasing unemployment by one percentage point raises a worker's likelihood to earn sub-minimum wage by 0.6%, regardless of gender, age, years of education, size of establishment, or geographical location. When disaggregating data by gender, the results show that the marginal effect of unemployment is higher for females (0.8%) than for males (0.5%).

This study also finds that the weak compliance with the minimum wage is linked to numerous deficiencies in the process that led to determining the minimum wage level, such as the lack of representation of sectors that pay lower wages and the polarization and weak role of worker unions. Other factors include ineffective inspection procedures and scarcity of inspection resources available at the Ministry of Labor, laxity in the implementation of the labor law and in the application of penalties for violation of the minimum wage regulations, and lack of voluntary compliance among employers given the high financial returns of non-compliance.

In conclusion, this study suggests a number of recommendations to the government in order to enhance compliance with the minimum wage regulations. These include re-establishing the minimum wage committees at the district and national levels as mandated by the minimum wage regulations; raising workers' and employers' awareness regarding the importance of implementing the minimum wage; enhancing inspection efforts mainly in sectors with high share of sub-minimum wage earners; conducting serious negotiations with representatives of sectors that are vulnerable to implementing the minimum wage in order to facilitate government subsidies; increasing the cost of non-compliance by significantly raising the fine; strict application of penalties for non-

compliance with the minimum wage; enhancing inspection capacity of workers' unions; improving the inspection administrative standards as well as boosting the capacity of inspectors; and upgrading monitoring procedures regarding workers' wages.