

## **EXECUTIVE SUMMARY OF KEY RECOMMENDATIONS**

### **INTRODUCTION**

The Working Group on Wages has reviewed the wage and benefits systems in Singapore. It recommends changes to promote greater wage and labour market flexibility, and introduce portability in employment benefits. This would enhance business competitiveness and employability of Singapore's workforce in a rapidly changing environment. The Working Group also examined the role of the National Wages Council (NWC) and its continued relevance in a rapidly changing business environment.

### **TOWARDS GREATER WAGE FLEXIBILITY**

2. Over the years, our wage system has undergone major reforms and has become more flexible to meet the needs of companies, employees and the economy. However, in today's rapidly changing and unpredictable business environment, greater wage flexibility is needed to ensure that companies are able to make quick adjustments to their wage cost. This is because wage cost constitutes a key component of business cost. A flexible wage system would allow companies to stay viable and preserve jobs during economic downturns while rewarding workers when companies do well.

3. Since the introduction of the flexible wage system in 1986 as recommended by the NWC Wage Reform Sub-Committee, most companies in Singapore have adopted the flexible wage system with a variable year-end payment linked to company's performance. As at 2001, the percentage of variable component is about 15% of total annual wages. This is below the 20% target as recommended by the sub-committee.

4. While companies have built up the year-end variable component, the recent sharp downturns revealed that our wage system was still not flexible enough to enable companies to make quick adjustments to their wage costs. As a result, the employer's CPF contribution rate had to be cut in 1999.

5. The Working Group noted that the NWC has recommended in 1999 the introduction of a Monthly Variable Component (MVC), to be built up from future wage increases, to form 10% of total wages. This would provide greater flexibility for companies to respond more readily to a volatile business environment. Instead of waiting till year end to adjust the annual variable

component, companies could make quick adjustments to their wage costs through the MVC as and when the need arises. Successful building up of the MVC would also minimise the need to cut the employer's CPF contribution rate whenever our economy faces a severe downturn.

6. The Working Group noted that the progress in implementing the MVC has been slow since its introduction in 1999. In 2001, only 4.8% of firms had adopted the MVC structure. This comprised 34% and 3.4% of firms in the unionised and non-unionised sectors respectively. The low level of implementation was mainly due to the wage freeze or wage cuts in many companies during the 2001 recession.

### **Variability of Wages**

7. The Working Group is of the view that more could be done to enhance the flexibility of the wage system. In this regard, companies should expand the variable component in their wage structure. As the contribution of management staff, particularly the senior management staff, is closely linked to company's performance, their variable component should be higher than that of the rank-and-file employees.

8. **The Working Group therefore recommends that a different ratio of variable component be adopted for different levels of employees.**

- **For rank-and-file employees, to give a measure of income stability, 30% of their annual wages should be made variable.** This would comprise 10% in MVC and 20% in annual variable component. This is consistent with past NWC recommendations.
- **For the middle management, professionals and executives, the variable component should account for about 30-40% of their annual wages.**
- **For senior management, as they are directly accountable for the performance of the company, the percentage of their variable component should be higher than that of the other employees. It should constitute not less than 40% of their annual wages.**

## **Monthly Variable Component (MVC)**

9. Companies should build up the MVC expeditiously.

- **For companies that have not implemented MVC in their wage structure or where the MVC is less than 2% of workers' basic wages, the Working Group recommends that they set aside a portion of basic wages to build the MVC up to 2%. This will kick-start the implementation of the MVC.**
- **For companies that have 2% or more MVC in their wage structure, the Working Group recommends that they discuss with their trade unions/workers whether a further portion of basic wages could be set aside to build up the MVC further. This will expedite the building up of the MVC to the 10% target.**

10. With the MVC wage structure in place, clear guidelines would be needed on when the MVC could be adjusted downwards and subsequently restored. Under the current practice, companies can only cut the MVC when they suffer severe losses. This does not provide sufficient flexibility for the companies to make quick adjustments to their wage cost in a volatile business environment to remain viable and save jobs for workers.

11. **The Working Group recommends that companies, in consultation with their trade unions, could reduce the MVC in a severe economic downturn when the business is adversely affected and/or the jobs of a significant number of workers are at risk. Likewise, employers should restore the MVC when business conditions improve.**

## **TOWARDS A MORE COMPETITIVE WAGE STRUCTURE**

12. Wages and productivity levels are important considerations for businesses in deciding which country to locate their operations. Measured in nominal terms, Singapore's wages are generally higher than that of other Southeast Asian countries and developing economies like China. However, when compensation is adjusted for productivity, the cost differential narrows, especially for the manufacturing sector that is exposed to global competition. Notwithstanding this, China's productivity could catch up with us quickly while its wages could remain relatively low given its large pool of labour. Hence, we need to watch our wage costs vis-à-vis China very carefully.

13. Over the years, a close link has been established between productivity and wage increases. However, the gap has widened since 1996 with real wage increases leading productivity gains. The situation was aggravated by the economic downturn in 1998 and the recession in 2001 which resulted in sharp reductions in output and a cyclical decline in productivity. **To sustain our wage competitiveness, the Working Group recommends that the National Wages Council (NWC), in formulating its annual wage guidelines, maintain the principle that “real built-in wage increases lag behind productivity growth at all levels of the organisation”.**

### **Competitive-Base Wage System**

14. One of our key challenges is to enhance the cost competitiveness and employability of our workers, especially older ones. Under our predominantly seniority-based wage system, workers' wages are closely linked to their length of service and this is manifested in long salary scales. As a result, older workers become less cost competitive and are at greater risk of being retrenched when companies need to downsize.

15. In the 80s, the wage differential for workers doing the same jobs was often 2 to 3 times. In 1986, the NWC Wage Reform Sub-Committee recommended that the average maximum-minimum salary ratio should be reduced to 1.5. Since then, the ratio has gradually been brought down and it is currently 1.7.

16. To help move further away from the seniority-based wage system, the Base-up wage system was recommended in 1997. The system is founded on the principles that the wage structure should reflect the actual value of the jobs and that wage increase should be closely linked to productivity and performance. Such a system would help older workers remain cost competitive and employable.

17. **To accelerate the implementation of the Base-up wage system to replace the seniority-based wage system, the Working Group recommends the following:**

- **Companies and their trade unions work towards narrowing the salary ratio to 1.5 within 2 collective agreements, i.e. 4 to 6 years; and**
- **Companies, in consultation with their trade unions, regularly review and adjust the salary ratio when job skills and job requirements**

**change so that workers would be rewarded based on the value of the jobs and their contributions.**

18. **The Working Group also recommends that the Base-up wage system be renamed the “Competitive-Base Wage System”.** This would better reflect the objective of enhancing the cost competitiveness of our workers.

### **NATIONAL WAGES COUNCIL (NWC) – A TRIPARTITE MECHANISM TO ACHIEVE WAGE COMPETITIVENESS AND EQUITABLE REWARDS**

19. Since its inception in 1972, the NWC has played an important role in formulating and issuing wage guidelines based on relevant economic and productivity indicators. The NWC guidelines ensure that workers are equitably rewarded for their contributions and that wage increases would not undermine our cost competitiveness.

20. The NWC provides an important forum for the 3 social partners – employers, trade unions/workers and Government - to discuss and reach consensus on key wage and wage-related issues for the benefit of workers, companies and the economy. The NWC guidelines have served as an important reference point in wage negotiations. Employers and trade unions have been able to reach agreement on wage adjustments based on NWC guidelines. This has helped foster labour management co-operation and industrial harmony which have been competitive advantages for Singapore.

21. Given its contribution to maintaining orderly wage increases, initiating wage reforms, and fostering industrial harmony and tripartite partnership, the Working Group concluded that the NWC is a valuable institution which has played an important role in Singapore’s economic and social development.

22. The Working Group is of the view that the NWC can continue to play a strategic role in the new economy, and should be preserved and strengthened. Specifically, the NWC :

- **Should continue to focus on issuing wage and wage-related guidelines based on fundamental economic and productivity indicators and tripartite consensus;**
- **Could proactively set up tripartite working groups to look into specific industrial relations and employment-related issues or to study emerging trends; and**

- **Could, with the support of the Ministry of Manpower and other government agencies, provide timely and relevant labour market information as well as international comparisons on wages.** This would enable companies and trade unions to be better informed of such trends and guide them in wage negotiations. Such information could further enhance management's capabilities in developing human resources.

23. The Working Group also examined the desirability of expanding the role of the NWC to include other manpower issues such as strengthening social safety nets and foreign talent. **The Working Group recommends against the expansion of the NWC's role, as this would dilute the effectiveness and affect the timeliness of the NWC recommendations.**

## **INTRODUCING PORTABILITY IN EMPLOYMENT BENEFITS**

24. Companies are restructuring, downsizing and merging in response to today's intensely competitive global environment. The average job tenure of most workers is becoming shorter as business cycles shorten, and companies employ contract workers and outsource non-core activities. Workers are likely to switch jobs several times in their working life. However, current employment benefits are often tied to individual employers and workers cannot carry along unused benefits with them when they change jobs.

25. At the same time, the Working Group recognises that benefits form a significant portion of the business cost to employers. This cost will go up when our workforce ages, especially medical expenses.

26. To better meet the needs of workers and companies in the new economy, there is therefore a need to inject portability into the provision of these benefits, allow for more efficient use of the benefits and to promote greater personal responsibility.

### **Portability in Medical Benefits**

27. Most large companies bear both the outpatient and inpatient costs incurred by their employees. Small companies provide less. At the same time, employers make contributions to the employee's CPF account, part of which

is allocated to the Medisave account<sup>1</sup>. Employees can use their Medisave contributions to pay the premiums for Medishield or other approved medical insurance schemes, as well as for inpatient expenses. About 72% of the resident population is covered by Medishield or other approved medical insurance schemes<sup>2</sup>.

28. Currently, medical costs amount to about 1.4% of the total wage cost, of which inpatient costs constitute about 40%. However, medical costs are likely to rise significantly over time as the experience of developed countries has shown. In particular, with a rapidly ageing workforce, medical costs of older workers are expected to rise sharply and this would undermine the employability of older workers. At the same time, with more frequent job changes, workers would need medical coverage not only during employment but also when they are in between jobs.

29. The Working Group has reviewed the previous study undertaken by the Tripartite Committee on Portable Medical Benefits. **Building on the study, the Working Group proposes an approach to the provision of outpatient and inpatient benefits that seeks to provide choice and flexibility to employers and employees, and allow for free play in the market.** It proposes a range of options that employers and employees can adopt. The adoption of a particular option would depend on the existing medical benefit usage, the needs of the employees and the unique circumstances of the company.

### ***Outpatient Benefits***

30. **The Working Group proposes 3 options<sup>3</sup> for employers and employees/trade unions to consider in restructuring their outpatient benefits.** All the options have 2 common features as follows :

- Provision to allow employees to accumulate unused medical benefits for future use; and
- Co-payment element to promote personal responsibility for medical expenses and thus help contain the rise in medical cost.

Implementation of these options is optional.

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<sup>1</sup> 6-8% depending on the age group. The long term target is to raise the allocation to 7-9%.

<sup>2</sup> Source : Report of the Tripartite Committee on Portable Medical Benefits, May 2002.

<sup>3</sup> The first two options were recommended by the Tripartite Committee for Portable Medical Benefits.

#### Options A: Co-payment with Annual Individual Budget

- Employers and employees co-pay outpatient expenses, say in the ratio of 85%:15%.
- Employers to set aside an annual outpatient budget for each employee from which the employer's portion of the outpatient bill would be drawn.
- Unused portion of the lump sum would be credited into employees' Medisave accounts.
- Once the lump sum is exhausted, employees would be responsible for the entire outpatient bill.

#### Option B: Direct co-payment with additional Medisave contribution as trade off

- Employees co-pay outpatient expenses of say 20-25%.
- As a trade-off, employers could make an additional contribution to employees' Medisave account, say 0.5% to 1% of employee's monthly salary.

#### Option C: Direct co-payment with cash incentives as trade off

- Employees co-pay outpatient expenses of say 20-25%
- As a trade-off, employers could grant employees cash incentives.

### ***Inpatient Benefits***

31. **The Working Group proposes two options on inpatient benefits - the Portable Medical Benefits Scheme (PMBS) and the Transferable Medical Insurance Scheme (TMIS)<sup>4</sup>.** Both options introduce portability to medical benefits (which are elaborated below).

32. The Working Group proposes that **the PMBS or TMIS be implemented through promotional efforts, rather than through legislation.** Employers and trade unions/workers should consider either option for adoption. While mandating the implementation of PMBS or TMIS would help ensure adoption by all companies, it imposes a statutory cost on employers and sets a minimum national standard of medical entitlement. This could introduce rigidity and increase the operating cost for companies, especially smaller ones. **To encourage the adoption of the schemes, the Working Group recommends that Government make adjustments to the existing tax structures on medical benefits.**

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<sup>4</sup> PMBS was recommended by the Tripartite Committee on Portable Medical Benefits while TMI was formulated with the support of MAS, the General Insurance Association and Life Insurance Association.

33. Given the need for workers to be continuously covered throughout their working life and the concern over rising medical costs, **the Working Group recommends that the Government monitor the implementation of these portable schemes over time.** If the coverage remains low, other measures may have to be adopted to facilitate implementation. The Working Group noted that some countries, eg. US, have mandated the provisions of inpatient benefits.

#### Portable Medical Benefits Scheme (PMBS)

34. The main features of the PMBS are as follows :

- In lieu of the existing employer-based inpatient benefits, employers would make additional contribution to employees' Medisave account, subject to a minimum of 1% of monthly salary.
- Employees would be responsible for inpatient expenses from the 1<sup>st</sup> dollar henceforth.
- Employees should use the additional Medisave contributions to purchase approved medical insurance schemes, eg. Medishield, to meet their inpatient needs.

35. The PMBS rides on the existing Medisave/Medishield framework. It provides coverage during employment, in-between employment, and even after retirement, so long as the individual continues to pay the premiums for the medical insurance. It can help enhance the wage competitiveness and employability of older workers as companies would be paying the same rate of additional Medisave contribution for all workers. Furthermore, the co-payment and deductible elements under the approved medical insurance schemes would discourage indiscriminate use of medical benefits, and this would help contain medical cost. Employers would benefit from the PMBS as it provides certainty for them to plan and set aside funds for medical expenses.

36. The Working Group assessed that younger and healthy employees would be more receptive to the PMBS as they generally do not incur high medical expenses and can save the unconsumed amounts for future needs. However, older workers and those with pre-existing medical conditions may find the additional Medisave contribution insufficient to meet their current medical needs, let alone save for future needs. **To encourage acceptance of the schemes by all employees, the Working Group recommends that the Government consider providing a once-off assistance to older workers and workers with pre-existing illnesses by paying, say 1 to 2 years' premiums for the medical insurance.**

37. Workers and unions have expressed concerns about the high deductible and co-payment levels, as well as the low rate of successful claims under the existing Medishield and other approved medical insurance schemes. To address these concerns and facilitate the implementation of the PMBS, the Ministry of Health may need to review and enhance these schemes.

### Transferable Medical Insurance Scheme (TMIS)

38. The main features of the TMIS are as follows :

- It is an employer-sponsored group medical insurance scheme which offers transferability of coverage when an employee moves from one employer to another. It provides inpatient benefits coverage up to prevailing retirement age (currently 62 years old).
- Participating group insurers will treat any employee covered under a TMIS plan as continuously insured, for the purpose of applying the pre-existing medical exclusion<sup>5</sup>, when he joins a new employer.
- It offers an extension of medical coverage of up to 12 months to employees who are retrenched, provided premiums are paid.
- Premiums are expected to be between 5 and 20% more than existing group insurance plans.
- Insurers may provide various insurance plans under TMIS with different levels of benefits and premiums.

39. The TMIS builds on the existing employer-provided group medical insurance scheme, and is therefore relatively easy to implement. It covers employees both during employment and for up to 12 months in-between employment<sup>6</sup>. Under the TMIS, it is possible to build in co-payment and deductibility features which would encourage individual responsibility for medical needs.

40. For TMIS to meet the objective of injecting portability into the medical benefits scheme, it has to be widely accepted and implemented by employers so that employees could continue to be covered under TMIS plans when they change employment. Active promotion by the insurance industry would be necessary. Initial indications from insurance companies are that large companies may be receptive to the scheme. The insurance companies have feedback that the TMIS can be offered to companies with not less than 30

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<sup>5</sup> In a typical group medical insurance plan, an employee with a pre-existing medical condition is excluded from medical coverage in respect of that condition for 12 months each time he joins a new employer. Under the TMIS, this pre-existing condition exclusion occurs once only, ie. with the first employer.

<sup>6</sup> This is adequate as 98% of retrenched local workers are re-employed within 3-6 months. Source : Labour Market Survey, Second Quarter 2002.

employees. For smaller companies, ways can be explored to make it viable for them to participate in the TMIS as well.

### **Portability in Training**

41. While achieving wage flexibility and competitiveness could help workers remain employable, it is equally important to ensure that the workforce is adequately equipped to take on new or higher value-added jobs in a knowledge economy. Life-long learning to encourage workers to constantly upgrade themselves with relevant skills is therefore crucial. **The Working Group recommends the setting up of a portable training account for workers to fund individual-based training.** This would encourage greater individual ownership of training and allow workers greater flexibility to choose their own upgrading courses. **The funding of the portable training account could come from different sources including the Lifelong Learning Fund.**

42. An alternative to the portable training account is to incentivise employers to provide funding to workers for training that is not job-related. At present, employers are allowed to claim 100% tax deduction for training expenses incurred. For individuals, they can claim relief for course fee up to \$2,500 a year if the training course leads to approved academic and professional qualifications or vocational qualifications related to his trade, business, vocation or employment. **To encourage employers to help fund worker training that may not be job-related but can help enhance their employability, the Government could consider granting double taxation deduction to employers in respect of funds provided for such training.**

## **ENHANCING LABOUR MARKET FLEXIBILITY**

### **Allowing Flexibility in Working Hours**

43. The Employment Act which regulates the minimum terms and conditions of employment including working hours has generally been flexible enough and companies have no difficulties in implementing various forms of flexible work arrangements. The Act stipulates that an employee is not required to work more than 8 hours a day or 44 hours a week. All work in excess of these shall be considered as overtime work and the employee must be paid at the rate of not less than 1½ times his hourly basic rate of pay.

44. However, there are industries, such as the aerospace industry, whose business cycles are volatile and where orders fluctuate sharply. Companies

in these industries do not require their employees to report for work on a regular basis when there is no demand for their services but require them to work overtime when they are needed to complete the task.

45. **The Working Group recommends that companies, whose nature of business justifies the implementation of a flexible working hours scheme, be exempted on a case-by-case basis from the provisions of the law governing daily and weekly working hours and the rate of overtime payment.** Companies will then have the flexibility to implement flexible working hours over a monthly, quarterly or longer duration and will only be required to pay overtime after the contractual hours of work computed over a specific duration.

46. As the proposed flexible working hours scheme has an impact on workers, there is a need to gather more information from companies which require such flexibility. **The Working Group recommends that a tripartite taskforce be set up to work out the principles and operational details.** The Taskforce should draw up a set of safeguards against abuses to ensure some stability in workers' income, securing workers'/trade unions' consent and ensuring the safety and health of workers before implementing the flexible working hours scheme. The Taskforce should also study how savings and productivity gains could be shared between companies and workers.

### **Modifying the CPF System**

47. The Working Group has made the following 3 recommendations to enhance labour market flexibility and preserve the employability of older workers through modifying the CPF system.

- Keep the employer's CPF contribution rate for employees in the 50-55 age group at its present level of 16%
- Lower the salary ceiling from \$6,000 to \$5,000
- Raise the wage floor for employee's CPF contribution from \$200 - \$363 to \$500 - \$750

48. The above recommendations, incorporated into the CPF Report<sup>7</sup>, have been accepted by the Government in July 2002.

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<sup>7</sup> "Refocusing the CPF System for Enhanced Security in Retirement and Economic Flexibility", 15 July 2002.

## **CONCLUDING REMARKS**

49. The recommendations made by the Wages Working Group aim to bring about greater flexibility in the wage system to enable companies to make quick adjustments in response to the changing business conditions. To maintain wage-competitiveness and to enhance employability of older workers, the seniority-based wage system should be replaced with one that rewards workers based on the value of the jobs and their performance, and motivates them to give their best.

50. In view of the greater churn in the labour market and the rising cost in providing employment benefits, there is also a need to make changes to the benefits system to introduce greater portability and personal responsibility in the consumption of the employment benefits.

51. Some of the measures recommended would need time to implement. For example, the proposed portable medical benefits which seeks to serve the long-term interest of our ageing and increasingly mobile workforce would require time for companies and trade unions/workers to go through a process of consultation and implementation. Together with the recommendations submitted by the other Working Groups of the Economic Review Sub-Committee, the Working Group hopes that the recommendations could help contribute to Singapore's competitiveness and continued economic growth and ensure that workers have jobs and remain employable.

**E N D**