Low Pay Commission
8th Floor, Fleetbank House
2-6 Salisbury Square
London
EC4Y 8JX

June 2021

Dear Mr Massey,

Re: FSB response to the Low Pay Commission's Consultation on the National Minimum Wage Rates (including the National Living Wage) to apply from April 2022.

The Federation of Small Businesses (FSB) is pleased to respond to the above-named consultation. FSB is the United Kingdom's (UK) leading business organisation. Established over 40 years ago to help our members succeed in business, we are a non-profit making and non-party political organisation that's led by our members, for our members.

FSB has always supported the National Minimum Wage (NMW) and continues to do so provided the level set does not harm employment or business conditions. We believe that the Low Pay Commission (LPC) plays a critical role in setting the wage floor by taking an independent view that reflects wider economic and labour market changes. The majority of small employers recognise the wage floor ought to reflect improvements in the growth of the UK economy and real term increases in average wages, we therefore support gradual increases to the NMW.

Small businesses are committed to increasing pay for their workers, but face a number of non-wage fixed costs, and some of these are likely to grow in the future. If Government wants to end low pay they also need to support small business employers in managing non-wage wage costs. We recommend HMT Treasury should cut Employer's National Insurance Contributions (NICs). This would help support the return of workers from furlough but give confidence to businesses. Government could also make changes to other non-wage policies, such as introducing a non-Covid SSP rebate for small firms, extending apprenticeship incentives beyond September 2021 and extending the Kickstart scheme beyond 2021.

To inform their deliberations, Commissioners will be interested in the impact of the National Living Wage (NLW) on small businesses to date. Our submission presents new evidence from a recent FSB survey of 901 respondents held in May 2021, and thus assesses the impact of the 2.2 per cent NLW increase from £8.72 to £8.91 in April 2021 and the change in age eligibility from 25 to 21.

- Only 6 per cent of small businesses were paying all of their staff less than £8.91 prior to the increase in the NLW in April 2021.
- 62 per cent report that all of their staff were being paid more than £8.91 per hour prior to April 2021.
- 9 per cent report that the increase in the NLW in April 2021 has increased their wage bill "by a large extent".
- 40 per cent report that the increase in the NLW in April 2021 has increased their wage bill "to some extent".
- Of those businesses whose wage bills have been affected, 68 per cent reduced profitability or absorbed the costs.
- 39 per cent of respondents raised their prices in response to the 2021 increase.

- 20 per cent cancelled or scaled down plans for investing in/expanding the business.
- 14 per cent chose to recruit fewer workers.

Yours sincerely,

Saira Hussain
Chair, Employment and Pensions Policy
Federation of Small Businesses

FSB submission to the Low Pay Commission's consultation on the National Minimum Wage Rates

June 2021

Coronavirus Job Retention Scheme
FSB's response to the LPC last year occurred during a time when a significant number of FSB members workers were on furlough. The Coronavirus Job Retention Scheme (CJRS) and other Covid policy interventions made it difficult to evaluate the impact of NLW increase last year. Our recent data shows that a number of small businesses still rely on the job retention scheme in dealing with the continued impact of the pandemic, especially small businesses in the accommodation and food services sector.

39 per cent of small business employers reported having staff on full and/or flexible furlough in May 2021. 17 per cent had staff on full furlough and 31 per cent had staff on flexible furlough in May. 61 per cent reported to having no staff on furlough in May 2021. There were regional variations in the number of small business employers reporting staff on full and/or flexible furlough with small businesses in the North West, South West and East Anglia reporting the highest numbers (48%, 42% and 41% respectively).

Our data shows the introduction of flexible furlough in July 2020, (a policy which FSB called for in 2020) remains invaluable to small firms. In terms of sectors, the manufacturing sector reported the highest number of staff on flexible furlough (40%). Small businesses in the accommodation and food services sector reported to having half of their staff on full and/or flexible furlough although this data is below the level we would generally rely on for statistical significance.

Impact of the National Living Wage and National Minimum Wage rise in April 2021
In May 2021, FSB surveyed our members regarding the impact of the NLW. A total of 901 small business employers responded to the survey. Respondent businesses represented a broad range of sectors, and came from all regions and nations of the UK. The survey was sent to FSB employer members only (i.e. excluding non-employing, one person businesses).

Q1. Prior to the recent increase in the National Living Wage to £8.91 an hour in April 2021, what were the pay levels in your business?

All interviews (901 responses)	Total
All of my employees were paid £8.91 or more per hour	**62%**
Some of my employees were paid £8.91 or more per hour	**30%**
All of my employees were paid less than £8.91 per hour	**6%**

Our evidence suggests that there were few small businesses which were paying all employees below £8.91 prior to the increase in April 2021, with only 6 per cent of businesses saying this was the case. 62 per cent of businesses were already paying all employees at or above £8.91. Small businesses in London & the South East (71%) were more likely to pay all of their staff more than £8.91 prior to April 2021 in comparison to the East Midlands, West Midlands and Yorkshire & the Humber and the North East (54%, 55% and 56% respectively).

This data highlights the number of FSB small and micro businesses that pay above the NLW, some of which include real living wage employers, see:
'We are an accredited Living Wage employer, and we pay the real living wage, we follow the voluntary guidance produced by the Living Wage Foundation'.

FSB member, tourism business, Cornwall

Q2. Has the increase in the National Living Wage to £8.91 this April increased your organisation's wage bill?

All interviews (901 responses)	Total
Yes, to a large extent	**9%**
Yes, to some extent	**40%**
No	**51%**

51 per cent of all small businesses say that they had not needed to increase their overall wage bill.
However, 40 per cent of small business employers reported that the increase of the NLW has had some impact on their wage bill. 67 per cent of small employers in the retail sector and 57 per cent of those in manufacturing reported an increase in their wage bill, as a result of this year's NLW increase.

Q3. You've said that the National Living Wage has increased your organisation's wage bill. How is your organisation managing these additional wage costs? (Select up to three)

All with increased wage bill after NLW (441 responses)	Total
Improved efficiency/raised productivity	**14%**
Taken lower profits/absorbed costs	**68%**
Reduced the amount of overtime/bonuses	**13%**
Reduced other aspects of the reward package (such as paid breaks or premium pay rates)	**7%**
Raised prices	**39%**
Reduced number of employees through redundancies	**5%**
Recruited fewer workers	**14%**
Reduced hours worked by staff	**19%**
Reduced the rate of basic pay growth for the rest of the workforce	**12%**
Hired more workers aged 22 and under (excluding apprentices)	**4%**
Recruited more apprentices	**4%**
Cancelled/scaled down plans for investing in/expanding the business	**20%**
Cut back on training expenditure	**10%**
Increased share of workforce on non-guaranteed hours contracts, e.g. zero hour contracts	**3%**
Reduced pension contributions to a minimum two per cent for employers	**3%**
Invested in machinery / automated certain processes	**5%**
Other	**4%**

The number of small businesses reporting that they have taken lower profits/absorbed costs, as a consequence of the increase in their wage bills this April stands at 68 per cent. The next most common reaction from small businesses following an increase to their wage bill was to raise prices (39%). One in 10 say they have cut back on training expenditure which is a concern in light of the great need to train workers.

In July 2020, the Government announced incentives for firms taking on a new apprentice. Extra funding for employers to hire apprentices was also announced in the Spring Budget in March 2021. These incentives will remain in place until September 2021. It is our view that this support should continue for a significant period beyond September to boost the number of apprentices and support small businesses.

Interestingly, more small businesses say they have recruited apprentices this year in comparison to previous years.

Q4. How is your organisation improving efficiency/productivity?

All who have increased productivity / efficiency (60 responses)	Total
Job / work redesign. e.g. flexible working	**36%**
Additional investment in technology	**39%**
Additional investment in training	**24%**
Changes to the reward strategy/employee benefits package	**24%**
We expect morale to be lifted and productivity to improve as a result of the NLW increase	**20%**
Greater emphasis on in-work progression and career ladders	**24%**
Changes to employee engagement	**17%**
External business support	**9%**
Other	**6%**
Don’t know/Not sure	**6%**

14 per cent of small business employers report that they have taken steps to increase productivity because the NLW has increased their wage bills. Of those who have taken steps to improve productivity, nearly two in five say they plan to make additional investments in technology. Job/work redesign, e.g. flexible working continues to be a common method for small business employers as a means to improve their efficiency/productivity. Other FSB research shows that small businesses in the hospitality sector (24%) are more likely to offer flexible working arrangements to their staff (excluding the ability to work from home) after the pandemic in comparison to all small businesses (13%). [1]

Nearly one in four stated that as a result of the increase to their wage bill they have made greater emphasis on in-work progression and career ladders to improve efficiency/productivity, an increase of 8 per cent from 2019. Small businesses are better able to tailor their training and development work in a way that better identifies an employee’s needs and, in the process, will be able to build better personal relationships and design more inclusive work packages. This is especially the case in low paid sectors in which progression is not often seen as the norm, but where small business employers are actively trying to change perceptions.

> *“The hospitality sector is often seen as a bridge between jobs or a job while studying. Very few people see it as a full-time career. As a business we are trying to change this perception; we are a living wage employer, we provide training and offer career progression. We need to promote hospitality as a potential career, if we are able to pull UK nationals from other low-skilled sectors into hospitality and so reduce hospitality’s reliance on EU migrants.”*

FSB member, entertainment sector, Glasgow

Q5. What effect has the increase in the National Living Wage (NLW) had on the salary levels of staff who were already earning above the NLW (e.g. managers/supervisors/other staff on higher wages)?

[1] FSB, A Menu for Recovery, June 201 https://www.fsb.org.uk/resource-report/menu-for-recovery.html

Some or all staff already earning above NLW (901 responses)	Total
The difference in pay between those earning the NLW and their managers/supervisors/other staff on higher wages has ***stayed the same***	**55%**
The difference in pay between those earning the NLW and their managers/supervisors/other staff on higher wages has ***decreased***	**17%**
The difference in pay between those earning the NLW and their managers/supervisors/other staff on higher wages has ***increased***	**18%**
Not decided yet – pay review yet to be held	**11%**

Q6. You said that the recent increase to National Living Wage (NLW) has changed the salary differential of some of your staff. What impact has this had on your workforce?

Impact of changed salary differentials on staff in small businesses (231 responses)	Total
Created dissatisfaction among non-NLW staff	**25%**
Increased overall morale of the workforce	**12%**
NLW staff less interested in progression	**9%**
Improved your business' ability to recruit and retain staff	**7%**
Reduced productivity of non-NLW staff	**4%**
Led to staff departures	**4%**
It had no impact	**55%**

55 per cent of employers say that the difference in pay between their staff on higher wages and those earning the NLW stayed the same. 18 per cent of all small business employers reported an increase in differentials, this rose to 26 per cent for employers in retail (excluding wholesale) and accommodation and food services.

"Last year due to the pandemic we didn't make any pay increases other than the statutory, so for almost a year we've had our general assistants, assistant cooks and drivers on the same level of pay. This hasn't been great, but the staff have been really understanding. This year we felt we've had to make proper increases and maintain differentials. From April, our lowest wage is just above the NLW, but we have a differential of 20p between our assistant cooks and cooks. If the NLW increased to £9.42 next year our business may not be viable, as we can't increase our prices to justify the wage increases.

FSB member - Social enterprise, food services, South West

NLW extension to younger workers

The ability of employers to train young people provides young people with the opportunity to improve their employability and transferable skills. FSB's latest research shows that 42 per cent of small businesses employ at least one person aged 16-22.

FSB's research in 2019 found that small businesses that employ 21–24-year-olds were more likely to pay their staff the NLW or above, with 60 per cent of respondents saying they paid their 21–24-year-old workers the NLW or above in 2019. As our previous evidence suggested small businesses are more likely (68%) to consider paying the NLW to staff aged over 21. We advocated for the abandonment of 21-24 age band over a gradual period, with an initial move to 23, after which the LPC should assess the impact on the labour market and on employment levels for young people before a move to 21 is made. This will enable small businesses, especially those businesses with a higher proportion of young workers, such as hospitality, to adjust to the change.

This year our research sought to assess the impact of the recent age eligibility change on small business employers. Our research found that prior to the change in April 2021, 65 per cent of small business employers said they were not using the 21-24 NMW rate to pay their 23- and 24-year-old workers and 35 per cent were using it. 42 per cent of small business employers in retail (excluding wholesale) and accommodation and food said they paid their 23- and 24-year-olds the 21-24 NMW (2020-21).

Q7. In April 2021, the National Living Wage (NLW) age threshold was lowered from 25 to 23. How has your business responded to this change in age eligibility for the NLW?

Business response to change age eligibility for NLW (901 responses)	Total
Improved efficiency/raised productivity	**3%**
Taken lower profits/absorbed costs	**18%**
Reduced the amount of overtime/bonuses	**4%**
Reduced other aspects of the reward package (such as paid breaks or premium pay rates)	**2%**
Raised prices	**10%**
Reduced number of employees through redundancies	**1%**
Recruited fewer workers	**5%**
Reduced hours worked by staff	**5%**
Reduced the rate of basic pay growth for the rest of the workforce	**4%**
Hired more workers aged 22 and under (excluding apprentices)	**2%**
Recruited more apprentices	**1%**
Cancelled/scaled down plans for investing in/expanding the business	**6%**
Cut back on training expenditure	**5%**
Increased share of workforce on non-guaranteed hours contracts, e.g. zero hour contracts	**2%**
Reduce pension contributions to a minimum three per cent for employers	**2%**
Invested in machinery / automated certain processes	**1%**
Other	**2%**
None of the above/it hasn’t had any effect	**68%**

68 per cent of small business employers say the change in age eligibility has not affected their business. Where the change did have an impact the most common impact was on profits/absorbing costs (18%) and an increase in prices (10%). 26 per cent of small businesses in retail say they have taken lower profits with 10 per cent in retail saying they have recruited fewer workers. Our evidence suggests this may be due to the higher number of young people employed in the sector, as just over half (52%) of FSB small businesses in retail employ at least one person aged under 23. Although this data is below the level we would generally rely on for statistical significance, 54 per cent of small business employers in the accommodation and food services sector say the change in age eligibility hasn’t had an effect.

Q8. The Government is considering a further reduction in the NLW age qualification to 21 by 2024. How would your business respond to the lowering of the NLW to 21?

Business response to change the NLW age eligibility to 21 by 2024 (901 responses)	Total
Improve efficiency/raised productivity	**6%**
Take lower profits/absorbed costs	**17%**
Reduce the amount of overtime/bonuses	**7%**
Reduce other aspects of the reward package (such as paid breaks or premium pay rates)	**6%**
Raise prices	**18%**
Reduce number of employees through redundancies	**5%**
Recruit fewer workers	**13%**
Reduce hours worked by staff	**10%**
Reduce the rate of basic pay growth for the rest of the workforce	**9%**
Hire more workers aged 20 and under (excluding apprentices)	**3%**
Recruit more apprentices	**4%**
Cancel/scaled down plans for investing in/expanding the business	**11%**
Cut back on training expenditure	**6%**
Increase share of workforce on non-guaranteed hours contracts, e.g. zero hour contracts	**4%**
Reduce pension contributions to a minimum three per cent for employers	**3%**
Invest in machinery / automated certain processes	**3%**
Other	**2%**
None of the above/it wouldn't have any effect	**59%**

FSB research highlights some differences in sectors which employ a higher number of people aged 21 and 22. 36 per cent of small businesses in retail (excluding wholesale) and accommodation and food services employ workers aged 21-22 in comparison to 28 per cent for all small businesses. Interestingly, 18 per cent of small businesses in retail (excluding wholesale) and accommodation and food services say they would reduce other aspects of their reward package (such as paid breaks or premium pay rates) in comparison to 10 per cent of small businesses, if the NLW age dropped to 21 by 2024.

Given that young people have been disproportionately affected by the pandemic in terms of furlough and jobs loses, a significant increase to the NLW and expansion to younger workers could further reduce employment opportunities for young people as the economy recovers. Although the NLW increase would be beneficial to those in work, it may act as a barrier to those out of it. Based on our evidence we believe the Government should seek to lower the NLW to 21, but to ensure sectors which employ a higher number of young people have sufficient time to recover from the pandemic before the change occurs, the Government should seek to make this change in April 2024. We also support the extension of the Kickstart scheme beyond 2021.

NLW in April 2022

In March 2021, the LPC's central projection for the NLW in April 2022 was £9.42, with a likely range of 7 pence above or below this figure, a potential 5.7 per increase. In May 2021, FSB sought to gauge how small businesses would respond if the NLW increased to £9.42 next year. As in previous years the most common response to a potential 5.7 per cent increase was to increase prices (31%). The second most common response was to take lower profits/absorb costs (27%).

Q9. How would your business respond if the National Living Wage were to increase to £9.42 in April 2022?

Business response to a proposed increase of £9.42 in April 2022 (901 responses)	Total
Improve efficiency/raised productivity	**9%**
Take lower profits/absorbed costs	**27%**
Reduce the amount of overtime/bonuses	**12%**
Reduce other aspects of the reward package (such as paid breaks or premium pay rates)	**7%**
Raise prices	**31%**
Reduce number of employees through redundancies	**8%**
Recruit fewer workers	**15%**
Reduce hours worked by staff	**15%**
Reduce the rate of basic pay growth for the rest of the workforce	**12%**
Hire more workers aged 22 and under (excluding apprentices)	**4%**
Recruit more apprentices	**3%**
Cancel/scaled down plans for investing in/expanding the business	**15%**
Cut back on training expenditure	**9%**
Increase share of workforce on non-guaranteed hours contracts, e.g. zero hour contracts	**5%**
Reduce pension contributions to a minimum three per cent for employers	**5%**
Invest in machinery / automated certain processes	**3%**
Other	**4%**
None of the above/it wouldn't have any effect	**39%**

Economic outlook

In the short term, COVID-19 still presents a significant issue to businesses that needs to be considered when setting the NLW for April 2022.

The most recent data shows that 1.5 million businesses took out a Bounce Back Loan (BBL) and 100,000 firms took out a Coronavirus Business Interruption Loan Scheme (CBILS) that need to be repaid. [2]Although these loans had relatively generous terms, it is still an additional monthly cost that small businesses now need to deal with on top of re-establishing business operations and adapting to the quite different markets they find themselves in. This recovery phase is expected to last until after Q2 2022[3], and so the Government may wish to consider when it intends to reach their target of reaching two-thirds of median earnings to ensure it is in line with economic predictions with the recovery.

The Office for Budget Responsibility's (OBR) forecast published on 16 March 2020 suggested that the NLW target will increase unemployment by 50,000 individuals (equivalent to increasing the rate from 4.0% to 4.1%). However, this analysis was done before the impact of the pandemic. [4] The OBR's economic and fiscal outlook published in March 2021, stated that the unemployment rate will not return to its pre pandemic level before approximately 2025. Not only that, but unemployment is also expected to spike towards the end of 2021 when the job retention scheme ends, reaching 6.5 per cent

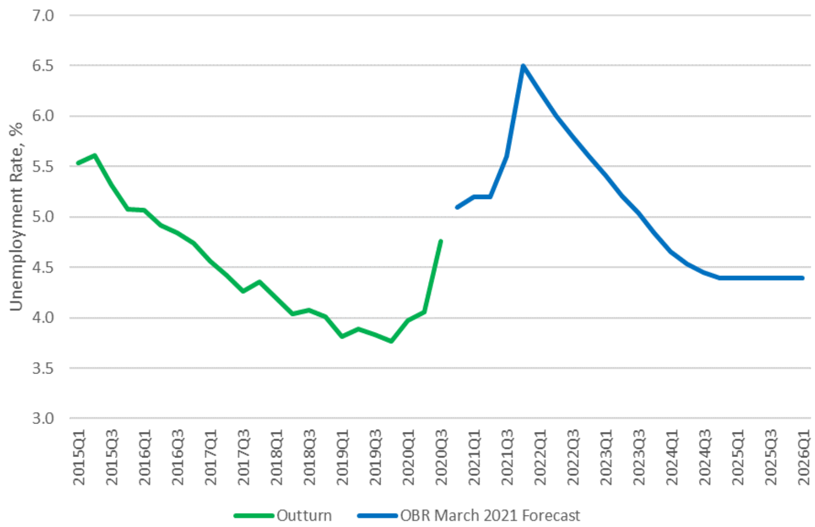
[2] HM Treasury, HM Treasury coronavirus (COVID-19) business loan scheme statistics, ttps://www.gov.uk/government/collections/hm-treasury-coronavirus-covid-19-business-loan-scheme-statistics

[3] OECD Economic Outlook, No Ordinary Recovery, May 2021, see https://www.oecd.org/economic-outlook/

[4] OBR, The National Living Wage, March 2020, see https://obr.uk/box/the-national-living-wage/

before beginning to fall – this is illustrated below in Figure 1 below. [5] Importantly, these forecasts are based upon the assumption that the June 21 benchmark is not delayed, and the job retention scheme is not extended beyond September. Should either be extended or delayed the impact will thus also be pushed further into the future and the unemployment spike would occur closer to 2024.

Figure 1. OBR unemployment rate and March 2021 forecast



Source: OBR
March 2021 Economic and Fiscal Outlook: Charts & Tables

Brexit
The true scale of impact of Brexit is still unknown. It is difficult to truly disentangle the effects of the end of the transition period and the COVID-19 crisis on the economy. As such, the impact Brexit is going to have on the labour market is also largely unknown but is expected to have some negative effects. In the long term, the OBR predict productivity is expected to be 4 per cent lower than the counterfactual of staying in the EU thus harming economic development.[6]

Inflation
The most common response from small businesses to planned increases is to increase prices, 31 per cent say they would do so, if the NLW increased to £9.42 next year. Recent ONS data highlights this in May the ONS reported that 18 per cent of micro and 24 per cent of small businesses noted that prices had increased by more than normal for that time of year[7]. At the time of writing inflation in the UK exceeded the Bank of England's two per cent target in May following the re-opening of parts of the economy. As explained above, business costs are going to increase as they begin repaying debts taken on during the crisis, adding to these costs in the short term will just add to their

[5] OBR, Economic and fiscal outlook – March 2021, https://obr.uk/efo/economic-and-fiscal-outlook-march-2021/
[6] OBR, Brexit analysis, https://obr.uk/forecasts-in-depth/the-economy-forecast/brexit-analysis/#assumptions
[7] ONS, Business insights and impact on the UK economy: 6 May 2021, https://www.ons.gov.uk/businessindustryandtrade/business/businessservices/bulletins/businessinsightsandimpactontheukeconomy/6may2021

burdens and be disproportionately hard on smaller businesses who tend to have lesser cash reserves and less ability to ramp up production over a short period.[8]

Cumulative cost of employment
Non-wage employment related costs have been on an upwards trend since 2011, mainly driven by the introduction of pensions auto-enrolment. These costs are likely to grow if proposed future Government policies on Statutory Sick Pay (SSP) and auto-enrolment are to be implemented in the coming years.

"Last year before coronavirus we made a conscious decision to reduce staff by 10-20%. This was based on a number of factors, such as pensions, Employer NICs and payroll costs, but the big increase to the NLW was the last straw, we had to cut costs. When you factor in business rates, potential tax rises – somethings got to give. Employment Allowance is good and a cut to NICs would also help."

FSB member, retail business, Scarborough

Recommendations
FSB has published a number of pieces of research since March 2020 which highlights the impact of the pandemic on small businesses. The Government's goal for the NLW to reach two-thirds of median earnings by 2024 was set before the pandemic. The pandemic has brought sustained uncertainty for small businesses, at the time of writing the Government has announced that the 21 June roadmap date is to be rescheduled by four weeks. After 15 months of restrictions the pandemic continues to have a significant impact on society and the economy.

FSB has favoured gradual rises to the NLW in previous years to reflect improvements in the economy. Considering the above, we feel that a 5.7 per cent increase next year, as projected by the LPC could lead to job losses, hamper the recovery and destabilise the small business economy at a particularly fragile time therefore an increase like last year of 2.2 per cent would reflect the challenging economic environment and higher rates of youth unemployment.

FSB recommends Government takes a cautious approach in working towards its 2024 goal. It is our view that Government should extend its goal target by one year. This will provide businesses with long-term predictability, giving employers sufficient time to recover from the pandemic, adapt to changes in the labour market and deal with the impact of other major policy changes.

Significant increases to the NLW during a time when employment flows are uncertain, and productivity is expected to remain sluggish will largely impact businesses that rely on workers paid in and around the NLW. Not only will businesses be facing uncertainty around staffing as a result of Brexit, a significant increase to NLW with no non-wage financial support from Government over the next few years could exacerbate the issue.

It is vital that the LPC continues to play an independent role in setting the wage floor and should be free to deviate from a political trajectory, if economic and labour market conditions warrant it to do so. If minimum wage policies are implemented at the wrong level and pace, it will not only damage the recovery and growth of small businesses but lead to higher rates of unemployment.

Small businesses are committed to increasing pay for their workers, but face a number of non-wage fixed costs, some of these are likely to grow in the future. If Government

[8] FSB, A Fighting Chance December 2020, https://www.fsb.org.uk/resources-page/a-fighting-chance-december-2020-pdf.html

wants to end low pay they need to support small business employers in managing non-wage wage costs. Our research found that 24 per cent of small firms plan to recruit staff either on a short-term contracts or non-guaranteed hour contracts over the next 12 months (members were asked in May 2021). Of those members that said they would recruit on a short-term basis, 28 per cent said a reduction in Employer NICs would encourage them to recruit someone on a permanent contract and 16 per cent said an increase in the Employment Allowance would have a similar affect.

Furthermore, FSB small business employers stated a reduction in the Employer NICs bill would help them in retaining their staff (24%), job retention bonus (19%) and an increase in the Employment Allowance (12%). Therefore, we recommend HMT Treasury should cut Employer's National Insurance Contributions. This would help support the return of workers from furlough, but also give confidence to businesses unsure of future consumer demand. Employer's NICs disincentivises both retention and recruitment and cutting them would play an important role in enabling both.

In addition, the Government should seek to support small businesses by uprating the Employment Allowance. The Employment Allowance provides small businesses with a £3,000 discount on employer National Insurance Contributions bills, acting as an incentive for small firms to create jobs, increase pay and encourage business investment. It is our view that the Employment Allowance will continue to be a vital source of support for small businesses, especially for those in sectors with tight profit margins.

FSB supports the Government's pre pandemic plans to reform to SSP to promote and adopt good practice to aid the return of employees back to the workplace and to extend eligibility for SSP to those earning below the Lower Earnings Limit (LEL). This change would increase the cost of employment for small businesses, many of which have been supported by the SSP Covid rebate during the pandemic. On this basis FSB recommends Government provides a full rebate to small firms after four weeks of absence. This could be modelled in the same way as the SMP Small Employers Relief (thus excludes higher earners) to support SMEs deal with costs of long-term sickness absence.

Compliance and enforcement

For small employers, many of whom have no or limited HR or legal support, understanding and adhering to employment law can be challenging. FSB has always supported fair and proportionate enforcement of labour market regulation to create a level playing field and rightly protect the rights of employees. Egregious or deliberate breaches of law should be met with tough enforcement, but the enforcement system, including HMRC enforcement of the NMW and NLW, is in need of reform. A more effective compliance and enforcement system would support workers, and ensure a level playing field for employers.

The current HMRC naming and shaming scheme is ineffective in encouraging enforcement, and yet is detrimental to employers included in the list for a small error. While the recent increase of the threshold from £100 to £500 was a step in the right direction, removing the smallest errors from this practice, this still inflicts reputational damage on small businesses who have made legitimate errors. The length of the lists also dilutes the value. Small businesses have highlighted that HMRC have a more adversarial approach to enforcement than other bodies, being quick to sanction and name and shame, even in instances of genuine error. They should seek to operate more along the lines of the Pensions Regulator, which names and shames only the most egregious non-compliance. This both makes the list more effective and does not reputationally damage small employers who have unintentionally failed to meet their obligations.

HMRC make no distinction between genuine errors and purposeful breaches of the law surrounding the NMW. Many employers unwillingly fall foul of their duties due to the complexity of them and lack of guidance, meaning they are identified as non-compliant by HMRC. Alongside the main legislation around the minimum wage rates, it is often the additional features such as uniforms and the accommodation offset application that cause the most confusion. This system remains complicated, and the price for making an error is huge – through fines and reputational damage through naming and shaming.

To encourage compliance, Government, and enforcement bodies, including HMRC and the single enforcement body once it is established, should create a culture of openness, where small businesses feel able to approach enforcement bodies for help without fear of prosecution. Clear and digestible guidance can play a role in this. The Government committed to reviewing the public facing NMW guidance in their response the UK Labour Market Enforcement Strategy 2019/20, as well as publishing thematic guides on topics where breaches are common. These guides and updated broader guidance would be welcome.

As the Government looks forward to the creation of a single enforcement body, the focus should be on providing greater clarity for employers through education and advice, as well as on compliance and deterrence. Effective signposting and impartial quality advice being available to employers can help to address the uncertainties faced by small business employers, especially around changes to legal obligations. Improving the regulatory experience for small businesses would improve compliance, and benefit small businesses in terms of cost, time, and wellbeing.

As part of the single enforcement body, the Government has committed to developing a compliance notice system for less serious breaches, where employers are given a fixed period to take corrective action before further action was taken. We welcome this approach, and this should be implemented as early as possible. Combined with improved guidance and support from the enforcement body, this should support small businesses making genuine errors to correct their mistake and understand the legislation going forward.

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