

Addendum to GN 7 – FWO’s consideration of submissions Transitional arrangements in modern awards

Background

1. The Office of the Fair Work Ombudsman (**FWO**) released a draft of *Guidance Note 7 - Transitional arrangements in modern awards*, for public consultation on 29 April 2010.
2. Modern awards commenced on 1 January 2010. However, model transitional provisions contained in most awards have the effect of deferring changes to certain monetary entitlements until 1 July 2010. Changes in most rates of pay are to be gradually implemented over a four year period, ending on the first full pay period on or after 1 July 2014.
3. The draft Guidance Note sets out FWO’s approach to interpreting the model transitional provisions in modern awards.
4. The principles articulated in the Guidance Note underpin FWO’s advice and information to the public about rates of pay. This includes information and online tools that FWO will publish on its website which will assist in the calculation of rates of pay. This suite of tools includes calculators, step by step guides and award search tools. FWO anticipates that these practical online tools will be the primary source of information for employers and employees about rates of pay during the transitional period.
5. These principles also underpin FWO’s compliance activity in relation to minimum rates of pay.
6. FWO worked with unions and employer groups to develop the principles contained in the draft Guidance Note. The public release of the draft Guidance Note allowed FWO to seek further views prior to finalising the document.
7. FWO received 15 submissions on the draft Guidance Note. A full list of those who provided submissions is at Appendix A. Submissions will be published on the FWO website. A number of changes have been made to the Guidance Note in response to these submissions.
8. FWO has now finalised the Guidance Note. This document explains the background to the process and FWO’s response to key issues arising out of the submissions. It highlights the substantive areas where FWO has made changes in response to submissions as well as explaining why FWO has not adopted suggestions in some cases.

Classification changes

9. Two submissions sought clarification about how the phasing operated in cases where an employee's classification changed.¹
10. The Guidance Note now makes it clear that to calculate rates of pay, an employee's current modern award classification is matched with the corresponding pre-modern award classification, i.e. the one that corresponds to, and is relevant to, the employee's current duties, and not the one that applied to the duties they were carrying out at some earlier point in time.

State referral employers and employees

11. A number of submissions requested the inclusion of more detailed information about arrangements for State referral employers and employees.²
12. FWO has included additional information in the Guidance Note about how the model transitional provisions apply or will apply to employers and employees who entered the national system from 1 January 2010 as a result of State referrals of power in New South Wales, Tasmania, Queensland and South Australia.
13. FWO notes that Fair Work Australia is required to consider varying modern awards to continue the effect of terms of Division 2B State awards before 1 January 2011 and that this may affect these arrangements for those employers and employees. This information has been included in the Guidance Note (at paragraph 6.5).

New employers and employees

14. Two submissions sought more information about arrangements for new employers and employees.³ One of those submissions sought information about how those employers and employees would determine which pre-modern award entitlements would have applied to them.⁴
15. There are a number of factors that need to be considered to determine what pre-modern award(s) would have applied; including the nature of business, the type of legal entity that it is (e.g. constitutional corporation or sole trader) where it is located, and the work that is performed by the employees.
16. The Guidance Note now emphasises that new employers and employees need to determine what instruments would have covered them if they were in business before 1 January 2010 in order to apply the model transitional provisions. Rather than including detailed information in the Guidance Note about how to find and interpret pre-modern awards, FWO invites new employers and employees to visit FWO's website www.fwo.gov.au for more information and

¹ GTA, paragraph 11; ABI, pages 10 - 11

² Office of Industrial Relations NSW, paragraph 2; HMAA, paragraph 4; HIA, paragraph 2.1

³ Office of Industrial Relations NSW, paragraph 1; Business SA, paragraphs 4.1 – 4.7

⁴ Office of Industrial Relations NSW, paragraph 1

/ or contact the Fair Work Infoline for specific advice and assistance about their business or employment.

Take-home pay orders and contractual entitlements

17. Some submissions, particularly from unions, sought additional detail about the operation of take-home pay orders and the interaction between minimum rates of pay in awards and obligations contained within the contract of employment.⁵
18. FWO has made some changes in response to these submissions to ensure that the availability of take home-pay orders, and the potential impact of contractual obligations, are not overlooked. The Guidance Note has also been updated in accordance with changes to the legislative provisions that were made after the draft was published.⁶
19. Take-home pay orders can be sought from Fair Work Australia (**FWA**). FWO will provide employers and employees with general information about take-home pay orders and will refer enquiries about the process of making applications for orders to the more detailed information on FWA's website.

Industry allowances

20. A number of submissions from both employer organisations and unions sought clarification about the circumstances in which an industry allowance and / or other monetary items would be included in base rates of pay for phasing purposes.⁷
21. FWO has adopted a number of these suggestions. In particular, the finalised Guidance Note clarifies that the primary consideration is the substance of the entitlement rather than what it is called.⁸
22. In addition, the Guidance Note has been amended to make it clear that it is not necessary that the entitlement apply to every employee that is covered by the modern award to be included in base rates of pay⁹ - there may, for example, be more than one 'industry' that is covered by the modern award.
23. The Guidance Note now includes a simple example of an industry allowance in a modern award that is part of an employee's base rate of pay (i.e. phased from 1 July).

⁵ Unions NSW, paragraphs 4, 5, 7 and 8; ACTU, paragraphs 5 - 8 and 31 - 33 ; Ai Group, paragraph 11; BIC, page 2

⁶ Office of Industrial Relations NSW, paragraph 3

⁷ GTA, paragraphs 6-10; Ai Group, paragraphs 37 – 39, 40 and 54; ACTU paragraphs 28 – 30; HIA, paragraph 2.3; BIC, page 2; Business SA, paragraphs 2.1 – 2.8

⁸ ACTU, paragraphs 28 – 30; GTA, paragraph 10

⁹ See Ai Group, paragraph 40. FWO notes that the rules in the FW Act about what is included and not included in a base rate of pay are substantially the same as the rules in the WR Act about what was included in a basic periodic rate of pay.

24. FWO has also clarified that although other monetary items may form part of a base rate of pay in some circumstances, this situation is not common.¹⁰ The Guidance Note confirms and emphasises the general rule that allowances in modern awards apply in full from 1 January 2010.¹¹
25. Some submissions suggested that particular examples should be included in the Guidance Note.¹² The finalised Guidance Note highlights this issue and sets out general principles that FWO applies when considering this question. To assist, it includes two examples to illustrate the principles. Whilst it is not practical to include specific information for every industry or situation in the Guidance Note, FWO invites parties to visit FWO's website www.fwo.gov.au for more information and / or contact the Fair Work Infoline for specific advice and assistance if they are unsure about how to treat a particular entitlement.

Overtime

26. FWO considers that overtime is not subject to the phasing arrangements. The draft Guidance Note acknowledged that there is a contrary view, and this was borne out in the submissions.¹³ A number of submissions that commented on this issue acknowledged that there was ambiguity on this point.¹⁴
27. FWO notes that the AMWU has indicated it intends to apply to FWA to obtain clarification about the treatment of overtime under the model transitional provisions.¹⁵
28. FWO considers that proceedings before FWA offers the best opportunity to resolve areas of ambiguity in the model transitional provisions. FWO awaits the outcomes of relevant proceedings and will of course adjust its position to reflect FWA's decisions.

Approach to 'equivalent' loadings and penalty rates

29. The model transitional provisions distinguish between penalty rates and loadings that are 'equivalent' and those that are not. The effect is that where penalty rates and loadings are equivalent they 'phase across' (i.e. the phased entitlement is calculated with reference to both the modern award and pre-modern award entitlements).
30. However, where rates are not equivalent, old entitlements are phased out while new entitlements are phased in, resulting in some cases in 'double phasing' (i.e. a pre-modern award rate being phased out at the same time that a modern award penalty is phasing in). As noted in the submissions, phasing of non-

¹⁰ Ai Group, paragraph 38

¹¹ GTA, paragraphs 6 -10; Ai Group, paragraph 54; Business SA, paragraphs 2 - 7

¹² HIA, paragraph 2.3; BIC, page 2; ACTU, paragraphs 28 – 30

¹³ Baking Associations of Australia Inc., paragraphs 13 -14; ACTU, paragraphs 18 - 21; Ai Group, paragraphs 52 – 53

¹⁴ ACTU, paragraphs 18 - 21; Ai Group, paragraphs 52 – 53

¹⁵ ACTU, paragraph 21; Scott, S. 'Unions go in to bat for overtime pay', *Australian Financial Review*, 25 May 2010, p.9

equivalent penalties and loadings requires additional calculations to be carried out.¹⁶

31. To be considered 'equivalent' the FWO approach requires the penalty or loading to apply for the same purpose, for the same time periods, and in the same way. For example, under this approach an afternoon shift loading in a pre-modern award would not be 'equivalent' to a night shift loading in a modern award, even if they apply to some of the same hours of work. This is because they do not apply for the same purpose (i.e. a night shift loading traditionally compensates an employee for working unsociable hours at night, or after ordinary business hours). Similarly, whilst the old and the new entitlement apply to some of the same hours, they span different time periods.
32. A number of submissions suggested adopting a broader definition of 'equivalent' penalty rates.¹⁷ The two main alternate approaches proposed were:
 - i. where the penalty or loading applies for the same purpose, not requiring the penalty or loading to apply for the same time period;
 - ii. not requiring the penalties to apply in the same way, in regards to the interaction between casual loadings and penalty rates.
33. FWO is aware that it is possible to take a broader approach to defining 'equivalent'. In developing the Guidance Note FWO considered a number of alternative approaches, including those outlined in the submissions.
34. FWO does not consider that approaches that group different penalty and / or loading entitlements together are compatible with the model transitional provisions. This is because the model transitional provisions apply in relation to 'a particular loading or penalty.'¹⁸ That is, they treat each entitlement that is being phased distinctly and separately. This view follows the reasoning of the Australian Industrial Relations Commission (**AIRC**) which explicitly rejected proposals to adopt an overall or aggregate approach to transitional arrangements. As the AIRC noted, these approaches leave significant discretion to employers and employees and would result in uncertain and inconsistent outcomes. This in turn means that entitlements would be difficult to identify and enforce.¹⁹ The FWO view follows the AIRC principle that each circumstance needs to be considered and determined individually.
35. The potential for uncertainty and inconsistency that was identified by the AIRC was borne out when FWO tested alternative methodologies. FWO found that different approaches could not be applied in a straightforward or consistent manner to all scenarios. In some cases, the alternative methodologies allowed too much scope for discretion which resulted in inconsistencies, uncertainty and/or disadvantage to employers and employees.

¹⁶ Baking Associations of Australia Inc., paragraph 11; ABI, page 8; BIC, pages 3 – 4

¹⁷ Ai Group, paragraphs 48 – 51; ABI, pages 7 – 9; BIC, page 3

¹⁸ See clauses A.5 – A.7 of the model transitional provisions.

¹⁹ *Award modernisation decision* [2009] AIRCFB 800 at paragraph 25

36. For example, it was proposed that FWO’s approach to the interaction between casual loadings and penalty rates (which phases these entitlements separately) should be replaced by an alternative approach whereby loadings and penalty rates (as phased) would interact as per the method in the modern award.²⁰ FWO acknowledges that this alternative approach could reduce the complexity of calculations in scenarios where the penalties would otherwise be equivalent. However, FWO is of the view that the proposed approach is not compatible with the model transitional provisions, nor does it produce fair outcomes.

37. This approach produces significantly different dollar outcomes to the method outlined in the Guidance Note. The following table demonstrates the different dollar outcomes between the two approaches. From the first full pay period on or after 1 July 2010, employees would earn \$1.31 less per hour under the proposed approach.

Effective date	Rates using alternative approach	Rates using FWO approach	Difference (per hour)
1 July 2010	\$35.23	\$36.54	-\$1.31
1 July 2011	\$36.50	\$37.26	-\$0.76
1 July 2012	\$37.82	\$38.16	-\$0.34
1 July 2013	\$39.18	\$39.26	-\$0.08
1 July 2014	\$40.60	\$40.57	+\$0.03

38. Employees would also be significantly disadvantaged in situations where the modern award does not provide for a casual loading during the period which attracts a penalty, whereas the pre-modern award did. Similarly, employers would be disadvantaged by having to immediately pay significantly increased costs from 1 July 2010 where:

- a modern award penalty is paid on a casually loaded rate, which is comprised of a base rate plus the casual loading, and the pre-modern award penalty was paid on the base rate of pay only; and
- where no casual loading was paid during the penalty period under the pre-modern award, but is paid under the modern award.

39. FWO’s approach to ‘equivalent’ loadings and penalty rates, while arguably stricter than some other options, is designed to enable employees to confidently apply the model transitional provisions in all circumstance in a manner which produces certain, fair and consistent outcomes.

40. FWO acknowledges that this methodology requires more calculations when applied to cases where loadings and penalty rates apply at the same time. This is exacerbated by the fact that, in some cases, the way in which the loadings and penalty rates interact in the modern award is different from the interaction in the pre-modern award.

²⁰ Ai Group, paragraphs 48 - 51

Absorption / offsetting

41. Clause 2.2 of the model transitional provisions provides that:

The monetary obligations imposed on employers by this award may be absorbed into over-award payments. Nothing in this award requires an employer to maintain or increase any over-award payment

42. The draft Guidance Note set out FWO's view that clause 2.2 applies in conjunction with long-standing Court authority about when employers can offset over-award payments against other award entitlements.

43. These cases include the full Federal Court decision of *Poletti v Ecob* (1989) 91 ALR 381, *ANZ Banking Group Limited v Finance Sector Union of Australia* (2001) 111 IR 227 and the decision of Goldberg J in *Textile, Clothing and Footwear Union of Australia v Givoni Pty Ltd* (2002) 121 IR 250

44. In summary, this means that where an employer and an employee have agreed that over-award payments are to be directed towards satisfying particular or all award entitlements, those over-award payments may absorb the relevant increases. However, where this is not the case, an employer would need to seek the employee's agreement to treat the over-award payments in this way.

45. The ACTU strongly agreed with FWO's approach. It expressed the view that the traditional approach to offsetting continues to apply and that there is nothing in the AIRC's decision to indicate that the well-established authorities in this area should be disregarded.²¹

46. Most submissions from employer organisations, and in particular, the Ai Group, the MBA and ABI, strongly disagreed with FWO's view.²² These submissions expressed the view that clause 2.2 displaced the Court authorities and instead meant that:

- during the transitional period an employer is entitled to absorb any monetary obligation in the relevant modern award into over-award payments;
- there is no requirement for the employer to reach agreement with an employee before absorbing modern award entitlements into over-award payments; and
- there is no requirement for the employer to have entered into an offsetting arrangement with an employee before absorbing modern award entitlements into over-award payments.²³

47. As observed in one submission, this means that clause 2.2 would have the effect of changing the way that contracts of employment operate.²⁴

²¹ ACTU, paragraphs 9 - 17

²² Ai Group, paragraphs 12 - 34; MBA; HIA, paragraph 2.2; and ABI, pages 4 – 6; BIC, page 2

²³ See Ai Group, paragraphs 28 - 29

²⁴ See ABI, page 4

48. In addition to relying on the words of clause 2.2, employer organisations emphasised the context in which clause 2.2 was developed to support their approach.
49. A number of submissions referred to the Award Modernisation Request and provisions of the *Fair Work Act 2009* which state that modern awards were not intended to increase costs for employers.²⁵ In particular, they noted that where the totality of what an employee receives is at least the amount they are entitled to under the relevant modern award, it would be unfair to require the employer to pay any more as a result of the commencement of modern awards.²⁶ They also submitted that it was unworkable to expect employers to reach agreement with employees about such matters, especially in industries which do not typically have written contracts of employment.²⁷
50. Several employer organisations also referred to submissions that were made to the AIRC when it was considering transitional arrangements in modern awards.²⁸ These submissions noted that the case law was discussed during the proceedings that led to inclusion of clause 2.2, and in particular, the case of *Poletti v Ecob*.
51. After careful consideration, FWO remains of the view that the approach adopted in the draft Guidance Note is the appropriate interpretation of clause 2.2.
52. FWO's view is based on the words of clause 2.2, the absence of any express statements by the AIRC to overrule existing precedents about the interaction between awards and contracts of employment, and the fact that the AIRC chose not to adopt clauses put before it that would have explicitly achieved what employers were seeking.
53. Clause 2.2 does not provide that additional monetary entitlements are or must be offset by over-award payments; it provides that they 'may' be. This is consistent with well-established principles about offsetting and is inconsistent with the submissions advanced by the employer groups.
54. There can be no doubt that the AIRC was aware that federal Court decisions set out principles about when offsetting 'may' or 'may not' occur when it developed clause 2.2.²⁹ However, the AIRC did not make any comment about these cases in either clause 2.2 or in its decision that set out its reasons for including clause 2.2.³⁰ Clause 2.2. can clearly be read in conjunction with existing precedent. It is reasonable to assume that if clause 2.2 was intended to operate to the exclusion of existing principles in this area, the AIRC would have said so.
55. FWO notes that parties did suggest to the AIRC in the proceedings that it adopt clauses that would have clearly allowed any over-award payment to absorb

²⁵ HIA, paragraph 2.2; Ai Group, paragraph 16; ABI pages 3 – 5; MBA

²⁶ Ai Group, paragraph 14 – 16; MBA

²⁷ Ai Group, paragraphs 30 – 33; HIA, paragraph 2.2

²⁸ Ai Group, paragraphs 17 - 25; MBA; HIA, paragraph 2.2

²⁹ See transcript referred to in Ai Group, paragraphs 23 and 24; MBA

³⁰ *Award modernisation decision* [2009] AIRCFB 800, paragraph 19

increases in pay in modern awards.³¹ But the final wording of clause 2.2 does not reflect such an express intention.

56. FWO also notes that unlike other transitional provisions, clause 2.2 is not limited to the phasing period or any time period at all - it operates at large. If it were interpreted in the manner suggested, it would have the effect of permanently setting aside the laws on offsetting rather than doing so to deal with this transition.
57. The interpretation of clause 2.2 that is proposed by employer organisations would have significant implications on employee entitlements and the law of contract. In particular, it would alter the effect of an employee's contract of employment and could adversely impact on an employee's entitlements without the consent of that employee.
58. Taking all of these circumstances into account, FWO considers that the better view is that clause 2.2 does not change the law on offsetting, but operates in conjunction with it.
59. FWO acknowledges that there are strong opposing views on this important issue and notes that the parties may wish to seek clarification from FWA or a court as to the interaction between the common law on offsetting and clause 2.2.
60. FWO would of course consider any decision by a court or FWA on this issue and may revise its approach accordingly.

Illustrative examples and further assistance

61. Some submissions sought the inclusion of additional examples or more detailed practical information in the Guidance Note.³² FWO has adopted some of these suggestions, such as including a clearer example of an applicable industry allowance, and an example of an 'equivalent' penalty.
62. In some cases, additional examples requested have not been included in the Guidance Note but have been incorporated into other tools that FWO is developing to assist employers and employees with the transition to modern awards.
63. These tools are available on the Fair Work Online www.fairwork.gov.au and include:
 - a 'How to Guide' which contains step-by-step instructions as to how to calculate rates of pay, with detailed examples;
 - online calculators to assist employers and employees to calculate base rates of pay, penalty rates and loadings; and

³¹ For example, the Ai Group's proposed clause expressly provided that employers were 'entitled to off-set the additional costs associated with such [specified monetary] entitlements and absorb the increases into the overaward payment.' It also included a requirement that employers consult with affected employees and provided that the offsetting provision would cease to operate after 31 December 2014

³² Unions NSW, paragraphs 3, 10; ACTU, paragraphs 28 – 30; GTA, paragraphs 11 – 12; HMAA, paragraph

- online tools to assist employers and employees to find the information that they need about their modern award and pre-modern awards to phase entitlements.

Parties requiring further assistance may also contact the Fair Work Infoline on 13 13 94.

FWO's approach to compliance

64. FWO's first objective is to educate people about the changes to rates of pay that occur from 1 July 2010 and assist them understand how to calculate rates of pay under the transitional arrangements.
65. FWO will provide guidance to employers as to how to work out rates of pay under these arrangements. This will include information presented on its website and provided to callers by the Fair Work Infoline. The FWO website will contain a number of tools, including pay calculators, step by step guidance, and detailed examples and industry specific information.
66. FWO understands that some employers may not be aware of the changes. FWO also anticipates that in some cases, in spite of seeking advice and making reasonable attempts to work through the issues, an employer may make errors. In some cases, underpayment of employees may arise because an employer has genuinely misunderstood how to apply the transitional arrangements in modern awards to their particular situation.
67. FWO works in accordance with a well established and robust [investigative process](#) and [litigation policy](#). These recognise that employers and other duty-holders may make errors about their obligations, in spite of seeking advice or making reasonable attempts to work through the issues. The policies recognise that underpayment of employees may arise because an employer has made an honest mistake, or genuinely misunderstood what needs to be done.
68. Under the FWO investigative process and litigation policy, it is generally the case that if an employer or other duty-holder readily rectifies the mistake (i.e. by making good any underpayments and putting in place systems to ensure they get it right in the future), FWO will take this into account in determining what, if any compliance action may be appropriate. Normally FWO would not initiate litigation against an employer in such circumstances.
69. However, if an employer has deliberately breached the law, or if the employees concerned are vulnerable workers, then, consistent with its Litigation Policy, FWO will treat that matter very seriously, and, as always, litigation may be considered as an appropriate compliance response.

1 June 2010

Appendix A

1. **AUSTRALIAN BUSINESS INDUSTRIAL (ABI)**
2. **AUSTRALIAN COUNCIL OF TRADE UNIONS (ACTU)**
3. **AUSTRALIAN HOTELS ASSOCIATION (AHA)**
4. **AUSTRALIAN INDUSTRY GROUP (Ai Group)**
5. **BAKING ASSOCIATIONS OF AUSTRALIA**
6. **BUS INDUSTRY CONFEDERATION (BIC)**
7. **BUSINESS SA**
8. **GROUP TRAINING AUSTRALIA (GTA)**
9. **HOUSING INDUSTRY ASSOCIATION (HIA)**
10. **HOTEL MOTEL & ACCOMMODATION ASSOCIATION (HMMA)**
11. **KAJEWSKI, CHARLES WILLIAM**
12. **MASTER BUILDERS AUSTRALIA (MBA)**
13. **OFFICE OF INDUSTRIAL RELATIONS - NSW**
14. **RECRUITMENT CONSULTING SERVICES AUSTRALIA LTD (RCSA)**
15. **UNIONS NSW**