



**Palestine Economic Policy Research Institute (MAS)**

**Background Paper**

**Roundtable (2)**

**Assessment of the Private Sector's Compliance with the  
Minimum Wage Decree:**

**Activation of Implementation Mechanisms and Causes for Low  
Compliance**

March 2017

The minimum wage policy is one of many social policies that countries adopt to sustain social justice in securing a minimum income that provides for basic needs of the people. Although there is almost an unanimous agreement on its importance and impacts on socio-economic aspects of life, it still stimulates theoretical-academic debate, especially regarding its economic impact. Despite this debate, minimum wage is provided by law in 90% of the world's countries as an instrument for achieving social justice, yet its application varies widely across countries, particularly in developing countries. Researchers attribute the low compliance with the law to several factors, most importantly: governments' low capacity in enforcing the law, legal constraints confining the role of labor institutions in monitoring compliance, and high costs of implementing the minimum wage on employers compared with its non-application.

Four years following its application in the Palestinian territory, compliance with this decree is still very low. Moreover, the number of private sector workers who receive wages below the minimum wage, increased after the ratification of the decree, from 124.5 thousand in 2012 to 126.4 thousand in Q2 2016, surprisingly the opposite of what is to be expected from applying this law.

This background paper examines the underlying causes of the weak implementation of the decree in the West Bank,<sup>1</sup> especially in the context of the deteriorating economic situation of Palestinians today, where poverty and unemployment rates remain high without any significant improvement on the ground. The paper discusses in brief the different theoretical approaches of minimum wage policies in the global context, and then briefly addresses legislation and implementation in the international context and the mechanisms that are applied in different countries. Then, the paper addresses the enforcement of minimum wage in Palestine, and attempts to identify the causes of low compliance with the law, from the viewpoints of relevant parties, based on interviews with the Ministry of Labor, representatives of trade unions, employers, in addition to the comprehensive assessment prepared by MAS on the this topical issue (Falah, 2014).

## **1. Legislation and Implementation of the Minimum Wage: Conflicting Results**

Economists hold different positions on the impact of the application of minimum wage policies, on employment, prices and inflation, and alleviation of poverty. Studies that use the supply and demand model, which takes into account competition factors, suggest that raising the minimum wage above the level of market equilibrium would cause the number of jobs available in the market to shrink, as this compels employer to reduce the number of workers in order to compensate the high costs caused by higher wages. Some argue that increasing labor productivity or reducing profits can compensate for this increase in costs. On the other hand, the Keynesian school believes that raising the minimum wage of the poorest workers will improve their consumption demand and thus raise the level of aggregate demand, which will be reflected in an increase in employment.

This discrepancy in theoretical approaches results in conflicting results of empirical research. Falah (2014) study shows that the results of empirical research on the impacts of the minimum wage varied across countries, due to different nature and depending on the

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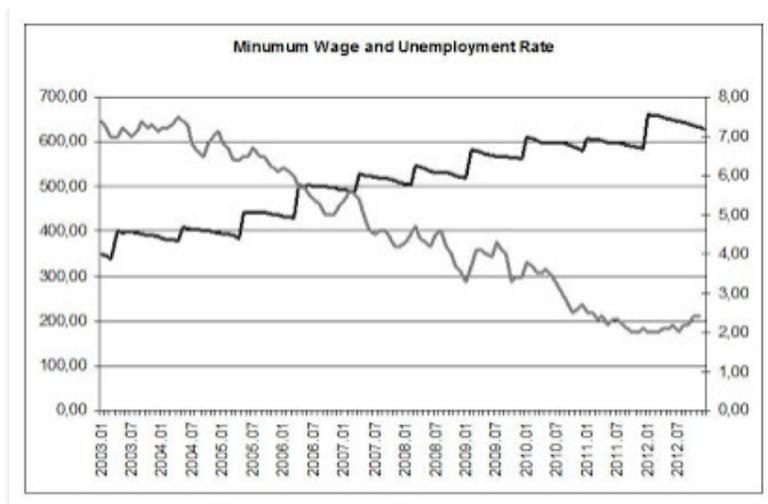
<sup>1</sup> The data of this paper includes the West Bank only, and excludes Gaza Strip because of difficulties of accessing Gaza Strip

efficiency of state institutions and the nature of the labor market. For example, in Colombia, an increase in the minimum wage by 15% led to a 5% reduction in employment. Other studies suggest that it had adverse effects on employment level in France, Canada and Britain. The Fang & Lin (2013) study found that minimum wage in China had adverse effects on employment, especially among women, the youth, and low-skilled workers. A study by the Congressional Budget Office on the impact increasing minimum wage have on labor and household income, states that raising the minimum wage to US\$ 10.10 per hour, would result in significant gains in wages of about 16.5 million low-wage workers. Nevertheless it would result in losing 500,000 jobs in the labor market. Whereas the Falah study (2014), based on Lemos (2009), indicates that although the majority of the United States research asserts that minimum wages do have a negative impact on employment levels, this impact is limited.

On the other hand, other studies indicate that the increase in the minimum wage in a large developing country like Brazil has not recorded any negative impact on employment. Furthermore, another study demonstrates that there is an adverse relation between minimum wage and unemployment in the Brazilian city of São Paulo. The figure below shows that the increase in the minimum wage level during the period 2003-2012 by about twice led to a significant drop in unemployment rate.

Regarding the minimum wage's impact on prices and inflation, Falah (2014) states that some research shows that the implementation of a minimum wage policy may lead to raising prices owing to increased labor costs. However, this effect is linked to several factors, most importantly: level of compliance to the law, the percent of workers whose wages will be increased, and the increase in the average wage associated with the implementation of the law. Another empirical study (Lemos, 2004) suggests that increasing the minimum wage in the United States by about 10% leads to an increase in food prices by 4% only and overall prices by only 0.4%.

Figure 1: Relation between Minimum Wage and Unemployment Rate in Brazil, 2003-2012



The left axis (black line) represents the minimum wage level while the right axis (grey line) represents unemployment rate in Sao Paulo.

Source: <http://nakedkeynesianism.blogspot.com/2013/02/minimum-wage-and-unemployment-brazilian.html>

Several studies have discussed the impact of the minimum wage on alleviating poverty, which depends on the minimum wage level adopted and the fact that it affects workers who benefit from the law only, i.e. affecting the overall poverty level in the country is contingent on the impact this policy has on total employment, which in turn is linked to flexible employment demand.<sup>2</sup> The Numark & Wascher (1997) study, based on “the Current Population Survey (CPS)”, concludes that the increase in the minimum wage increases the probability that poor households will escape poverty, as well as the probability that (previously non-poor) households will fall into poverty, and that the number of the latter is more than the number of the former, yet this difference is not statistically significant.

According to Benassi (2011), 90% of the world's countries apply a minimum wage by law. The same study shows that the implementation of this policy varies widely, in terms of approach, effectiveness, or compliance. It also states that developing countries have the lowest levels of compliance. Abdeen (2014) reports, based on an ILO report, that the number of poor workers all over the world countries is still very high. Nearly half of wage workers, who amounted to some 209 million workers in 22 developing countries according to 2013 statistics, are paid less than US\$ 22 per day (i.e. below the international poverty line). Moreover, 7% of all workers in the United States and 8% of workers in Europe are under the poverty line.

According to Benassi (2011) there are a set of measures and mechanisms that countries adopt to ensure effective application of the law:

- Persuasion strategies are used to build public support for the application of minimum wage and encourage employers to comply voluntarily.
- Capacity-building, including educational courses and training seminars, to familiarize employers and their employees with the minimum wage policy and mechanisms.
- An effective monitoring system that allows detection of non-compliance with the law, including enhanced inspections, especially in sectors where compliance is low, which also enables workers and their representatives to easily and safely file complaints.
- Enabling workers to file complaints not only through individual action, but also through collective action to avoid employers' retaliatory acts against individuals.
- Penalties must be a real deterrent to non-compliance, meaning that non-compliance penalties should be higher than compliance costs.

## **2. Minimum Wages in Palestine - Performance since 2012**

The possibility of enforcing a minimum wage has been widely debated in the Palestinian arena. There have been conflicting opinions about the economic and social impacts of such a policy. Some contend that the Palestinian economy is still fragile and incapable of adopting such a policy, and is still unprepared, in terms of administrative structure or productivity, or handling the costs and consequences of its enforcement. The enforcement

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<sup>2</sup> Less flexibility means that less number of workers will lose their jobs.

of this policy will negatively affect the economy and will not lead to positive results at the level of poverty alleviation and reducing wage gaps among workers (MAS, Economic Monitor no. 45, Q1 2016). Other economists consider that regardless of its economic weight, the minimum wage is a social necessity that cannot be postponed in light of the difficult situation the Palestinians are living, especially the poor. This is of special importance especially if considering strengthening the people's resilience and supporting their existence, .since the working poor's wages should not be determined by market forces alone (<http://www.wattan.tv/news/128363.html>).

Late in Oct 2012, the Palestinian Government decided to put an end to the ongoing controversy by ratifying the minimum wage decree. This move came following a year of negotiations between the members of the National Wage Committee, which comprised representatives of the public sector, trade unions, and the private sector. The promulgated Decree stipulated that workers are entitled to a minimum wage of NIS 1,450 per month, NIS 65 per day, and NIS 8.5 per hour in all the Palestinian territories and for all sectors. In addition a number of issues were agreed upon, which should be considered as part of the Decree, the most important of which are: the government should secure the means for supporting the sectors that will be affected by the application of the minimum wage; to take into consideration the annual increase in the CPI, as issued by the Palestinian Central Bureau of Statistics (PCBS), as an annual allowance paid to all workers in the Palestinian Territories; to activate the central and sub-committees at the governorates levels to supervise the implementation of the decree's articles and the full application of the minimum wage; to put in place the appropriate regulatory mechanisms, while referring to legal provisions in the Labor law in case of violation; the impact of the minimum wage should be assessed annually by the Wages Committee.

In conclusion, the process of setting the value of the minimum wage was not based on clear economic criteria nor full assessment studies of the expected effects. It came about basically as a political settlement, which also took into account national considerations, especially with regard to imposing a unified level of minimum wage across the country for all sectors (MAS, Economic Monitor no. 45, Q1 2016).

During Q2 2016, the number of the private sector's workers who were paid less than the minimum wage in the West Bank and the Gaza Strip reached more than 126,000 workers, i.e. about 19% of total private sector workers in that quarter.<sup>3</sup> The majority of these workers are employed by the trade, restaurants and hotels sector, followed by the services sector, and then the mining, quarrying and manufacturing sector. The Ministry of Labor indicates that workers in kindergartens and clothing and textiles sectors are usually paid below the minimum wage. Figure (2) shows the number of wage workers who receive less than the minimum wage in the West Bank and Gaza Strip by economic activity during the Q2 2012, 2013 and 2016.

The data indicate that there is a change in the top sectors that employ workers who are paid below the minimum wage in Q2 2016 compared with the Q2 2012. As indicated

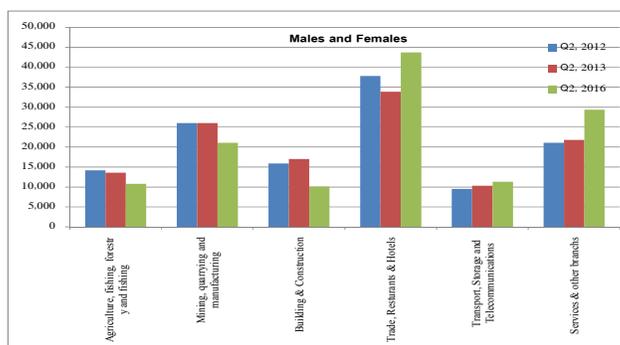
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<sup>3</sup> This data is based on the figures issued by PCBS. However, another study published by MAS titled "Evaluation of the Efficiency of the Palestinian Labor Market", indicates that the percent of those paid less than the minimum wage during 2015 were 29% in the West Bank. The discrepancy in figures might be ascribed to the calculation method used by the PCBS to calculate the number of the private sector workers and the total number of workers who are paid less than the minimum wage.

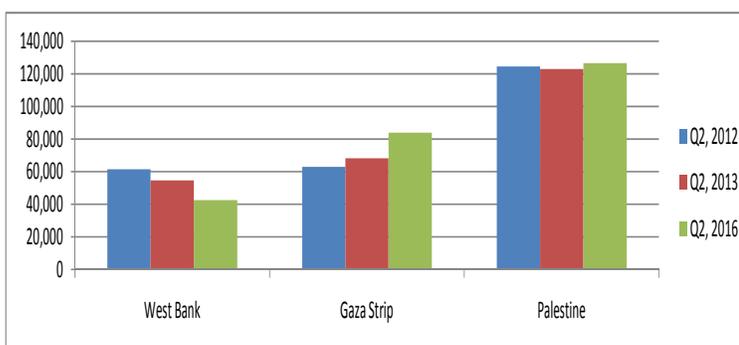
previously most of these workers are concentrated in trade, restaurants and hotels sector, then in the services sector, followed by the mining, quarrying and manufacturing sector. While during Q2 2012 they concentrated in the trade, restaurants and hotels sector, followed by the mining and manufacturing sector, and then the services sector.

The data also indicate that the number of workers who are paid below the minimum wage in Gaza Strip is much higher (absolutely and proportionately) than those in West Bank. In Q2 2016, their number in Gaza Strip was 84 thousand, compared with 42.5 thousand in the West Bank. Figure (3) shows the number of the private sector workers who are paid below the minimum wage in both the West Bank and Gaza Strip.

**Figure 2: The number of wage workers employed in the private sector who receive less than NIS 1,450 (minimum wage) in the West Bank and Gaza Strip by economic activity, during Q2 of 2012, 2013, 2016**



**Figure 3: Number of wage workers in the private sector who receive less than NIS 1,450 monthly (minimum wage) in Palestine by region**



Source: Palestinian Central Bureau of Statistics (PCBS), 2016. Labor Force database, 2010-2016. Ramallah, Palestine.

According to Falah (2014), the median monthly wage for workers who are paid below the minimum wage in the West Bank is NIS 1,000, and the average daily wage is NIS 50. These wages vary according to gender. The male median monthly wage is NIS 1,050

compared with NIS 800 for females, whereas the male median daily wage is NIS 50 and NIS 40 for females. As well these medians vary by economic activity, dropping to NIS 700 in the private education sector and NIS 800 in finance and insurance sector. On the other hand, it rises to NIS 1,200 in restaurants and hotels sector. By governorates, the median wage drops to NIS 800 in Jenin and NIS 700 in Tubas, while it rises to NIS 1,200 in Jericho<sup>4</sup>.

According to Falah (2014), 4% of public sector workers are still paid below the minimum wage level. Although there has been no data available following Q2 2014 on this subject, recording such a percentage in the public, even though very low, following the adoption of the Decree is a clear violation of the law. According to the same study, 51% of females working in the private sector in the West Bank were paid below the minimum wage compared with 28% for males. The study also shows that this percentage rises among workers with less years of education, reaching 74% for males with less than secondary education compared with 46% for females. However, it is notable that the percentage of female workers with a Bachelor's degree and above constitutes 26% of the total number of wage workers who are paid below the minimum wage compared with 4% for males only.

### **3. The Application of the Minimum Wage: Why the Procrastination?**

The following section reviews the reasons behind the low level of employers' compliance with the minimum wage decree, as explained by key involved parties.

#### **A. The Position of the Ministry of Labor (MoL)**

The MoL relies on the inspection and supervision mechanism, run by the General Administration of Inspection and Workers Protection (GAIWP), which is responsible for overseeing the enforcement of the minimum wage law. GAIWP regulates wage violations either through routine unprepared inspection field-visits to establishments. Such visits aim to monitor the implementation of the Labor Law regulations issued there under, including the application of the minimum wage. Or the GAIWP responds to workers complaints about the employer's non-compliance to pay the minimum wage. MoL also carries out campaigns to inspect violations of the minimum wage law. These campaigns target the majority of the economic sectors which have high percent of workers whose wages are below the minimum wage.

One of the main reasons for non-compliance with the decree, according to the MoL officers, is that the application of the minimum wage will lead to the closure of some of economic enterprises (which they described as "poor"). An example of such enterprises is kindergartens and textile and garment factories. According to the MoL, the quandary is that the minimum wage was set at one level for all sectors and did not take into account that some sectors will not be able to adhere to this law. On the other hand, the cabinet ratified a decision that the government should secure the means for supporting the sectors that will be affected by the application of the minimum wage, yet it did not take any action on the ground to support these sectors. Following the adoption of the decree the government had already started negotiating with representatives of these sectors (kindergarten and the garment and textile industry)

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<sup>4</sup> This data covers Q1 2014.

(Falah, 2014). One of the government's proposed solutions was providing kindergartens with a financial support of one million dollars. Nevertheless, negotiations failed as a result of the dispute over who deserves this support. The government thought it should be targeted to the most affected kindergartens after settling their legal matters. However representatives of this sector insisted that this financial support should be distributed equally. The government has also proposed a set of measures to ease the increase in the wage bill to the representatives of the garment and textile industry, such as tax cuts or a reduction in electricity prices by as much as 40%. However, these negotiations had reached a dead end.

Added to which is the limited educational role played by trade unions in Palestine, which falls below expectations, and the multiplicity of trade unions representing workers. The latter issue constrains the unions from playing their part by putting the needed pressure on employers to comply with the law. This also encourages unions' members to violate the law, especially lawyers and physicians, who do not pay the minimum wage to their employees, and even to encourage others to violate the law.

Other reasons mentioned are that some employers do not comply with the minimum wage decree and resort to circumvention. For example, by transferring salaries that equal or exceed the minimum wage to the employees' bank accounts and later requesting the workers to return the difference; or by forcing employees to conceal their real wages during inspection visits, which they are forced to do out of fear of employers reprisals actions against them. The possibility of resorting to these scams increases because the Labor Law does not stipulate in any of its articles or provisions that the MoL can force the employer to rehire the worker if it was proven that he/she was fired from work on the basis of filing a complaint.

As well, the shortage in MoL human resources and vehicles needed to carry out inspection visits thwarts coverage of all sectors and establishments which result in higher noncompliance rates. Currently the MoL employs 45 inspectors who are responsible for monitoring the full implementation of the law all over the West Bank. The PA Cabinet has recently allocated NIS 6 million to be spent over a three years span on hiring 15 inspectors each year and to finance purchasing 5 inspection vehicles. In another context, inspectors of the ministry face many difficulties during inspection operations, including exposure to threats and even assault, and inability to access area "C" or areas adjacent to the Wall. Also the Ministry's inspections cover only 4,000 establishments annually out of the 60,000 establishments that should be adhering to the minimum wage decree.

Another cause of low compliance is that penalties for noncompliance are not a real deterrent (i.e. a penalty between JOD 50-100) and that the employer should pay the difference in wages retroactively, provided that the penalty is multiplied by the number of workers to whom the employer did not pay the minimum wage. In this regard, respondents pointed out that there were a number of establishments that did not adhere to the law, even though the ministry took action against them. The impact of this non-deterrent penalty is increasingly limited if we consider the Ministry's inability to detect violations. This is also related to the costs of implementation compared with noncompliance costs, which are also related to the Ministry's ability to detect violations.

In light of previous experience, there is a serious need to reconsider the minimum wage decree. In this respect, respondents indicated that, while in practice, the Ministry spotted gaps in the decree, which would pave the way for drafting amendments to the decree that seems to be necessary

## **B. The Position of Trade Unions**

According to one of the trade union member institutions (Independent Trade Unions Federation), the main reason for low compliance with the minimum wage decree is the absence of the PA's political will to implement this decree as part of a broader social protection policy. This is evident in the absence of specialized labour courts where workers can exercise the right to litigation; and in the failure to allocate the necessary financial and human resources to the competent ministry to implement the decree, which is evident in the inadequate number of inspectors and inspection vehicles. Furthermore, the absence of a law that protects trade unions' rights and freedoms which is accompanied with a high rate of unemployment and willingness of many unemployed persons to work for wages subminimum wage, undermines the power of under-minimum wage workers to protest and file complaints against employers.

Additionally, the structure of trade unions, which is based on quotas and appointment of representatives according to their political factional affiliation, deprives workers of the right to freely elect their representative. Also the structure of the federation, which comprises multiple trade unions of major sectors, does not entail the implementation of a minimum wage as one of their top priorities, which reflects on the seriousness of these unions' struggle for its implementation. On the other hand, there is a division among union members about different labor issues, including the minimum wage. However, according to the Independent Trade Unions Federation, the multiplicity of unions representing workers does not in itself have a positive or negative impact on the implementation of the Decree, while also noting that the wages of the workers' representatives of workers are well above the minimum wage level.

As with other trade unions in Palestine, the Independent Trade Unions Federation has a limited and weak role. Yet the Federation is working on different levels to enhance the role of trade unions, which could directly and indirectly transform trade unions into a pressure group on employers to increase their compliance with the decree. One of the major steps the Federation took was presenting a proposal for a draft law for regulating the work of trade unions. Moreover, the Federation tried to assemble the members of the National Wage Committee several times to discuss this issue. Also the Federation took some measures to defend and support individual workers who were subject to retaliation as a result of filing complaints against their employers, and held meetings with stakeholders in order to enhance the workers' confidence in the union work and in their ability to make a change through collective action.

The above does not negate the fact that specific small enterprises in some economic sectors do not have the actual potential to implement the decree. This indicates the importance of implementing the provisions of the Decree issued by the Cabinet which stipulate that the government should secure the means for supporting the affected sectors in order to enable them from applying the minimum limits stipulated by the Labor Law, including the minimum wage.

It is clear that implementing the minimum wage is the responsibility of all segments of society, and is related to the type of society we want to live in. From the trade union point of view, there are a number of steps that can lead to higher compliance with the minimum wage. In particular, if the government makes a commitment to pay the difference between the actual salaries and the stipulated level of the minimum wage to workers; to expedite recruitment of the needed number of inspectors and the establishment of specialized labor courts; and the adoption of a law for the protection of trade unions rights and freedoms.

### **C. The Position of Employers**

According to Falah (2014), employers focus on the impact of labor surplus, as high-skill jobs have a negative impact on the level of wages, which impels workers to work in low-wage jobs because of scarcity of alternative opportunities. This impact is more obvious among females, younger workers, or the less educated. A one percentage point rise in the unemployment rate increases the probability that workers receive a wage below the minimum wage by 0.6% regardless of gender, age and years of schooling.

In addition, employers in different economic sectors were not represented directly in the National Wages Committee, which has affected their voluntary compliance with the decree. The multiplicity of trade unions also played part in the low implementation of the decree, especially that there was inconformity between the three unions about their representation of workers. The absence of a unified body representing workers resulted in disagreement between these unions during the negotiation process, weakening their negotiating position and their role as (supposedly) one party in the so-called tripartite national dialogue (government, workers, and employers).

Employers also believe that setting the minimum wage level based on the basic needs necessary for life, is not consistent with the framework and structure of production, considering the structural distortions of the Palestinian economy. As well, the level that were adopted did not take into consideration the different economic structures and levels of income and prices in the various regions. These fundamental differences emphasize the need for adopting different approaches in the two regions of Palestine (West Bank and Gaza Strip), since implementing one level of minimum wage for both regions has adverse effects on comparative working conditions and the standards of living. This also demonstrates that the Decree does not take into consideration the economic structures and standards of living which should play a crucial role in determining the minimum wage level. The final statement of MAS Economic Conference of 2016, and the National Team formed based on a Presidential decree to follow up the Conference's recommendations, included a recommendation that emphasized the need for both the private sector and trade unions to work together to join efforts to accomplish their responsibilities in this regard.

## **4. Conclusions**

We conclude with a number of reasons that explain the low compliance with the minimum wage decree. Despite their conflicting opinions, the different involved parties agree on some of these causes, which include: the infective surveillance and inspection mechanism adopted by the MoL; the limited role of trade unions in Palestine; inability of specific economic sectors (especially kindergartens, and the garment and textile sector) to

implement the minimum wages level; the high rates of unemployment; the government did not commit to support the affected sectors; and the absence of voluntary compliance by the private sector with the decree.

Further procrastinating the implementation of the minimum wage would entail costly social and economic consequences. Therefore the government is urged to expedite its implementation by adopting a number of measures that address the causes of low compliance emphasized above:

- Promoting decent work culture among workers and educating them about their rights, including the right to a minimum wage.
- Penalties (costs) on non-compliance should be higher than the compliance costs on employers (i.e. paying the difference between the actual wage and the stipulated minimum wage).
- Commencing the dialogue between the three involved parties, that aims to discuss social and economic consequences of non-implementation.
- Revising specific provisions in the Labor Law, most importantly, the provision stating the penalty of the law violators.
- Legislating a new law on trade union rights and freedoms, which guarantees protection of workers rights to protest and form unions within their own institutions.
- Trade unions and federations should have the right to access workers' information related to their income.
- Supporting sectors that do not have the financial capacity to adhere to the minimum wage Decree.
- Follow-up all details related to the Decree, including linking it to the cost of living, and activating the role of the National Wages Committee.

### **Questions for Discussion**

Are there fundamental gaps in the core of the decree that explain the low compliance with it? Thus, is there a need to revise the decree?

Is the Palestinian economy still unprepared, in terms of administrative structure or productivity or is it ready to handle the costs and consequences of the enforcement of a minimum wage?

What are the most effective ways to increase the compliance with the law and what are the roles of the three production partners?

What are the social, political and economic consequences of not implementing the minimum wage?

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