Wage Setting, Labour Markets and the Politics of Industrial Relations:
Accounting for the Public Sector Wage Premium in Ireland

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Abstract

Using individual earnings and labour force data, and evidence derived from in-depth interviews with key industrial relations actors, the authors seek to account for the presence of and large rise in the estimated public sector earnings premium in Ireland from 2003 to 2006. Most labour economists have come to recognise that, while public sector earnings premia can, in large part, be explained by the personal characteristics of employees and the attributes of their jobs, they often struggle to account for any remaining variation. We show that public sector employees are paid more in Ireland, even after controlling for their personal characteristics and the specific features of their employment, and that the average earnings premium rose significantly in recent years. We find that the presence of and the rise in this premium can be accounted for by changes in the composition of the labour market and the politics of the wage bargaining process. We thus offer a comprehensive explanation for the existence of a public sector earnings premium which draws both from econometrics and industrial relations.

JEL Codes: J6, J45, F22.

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This paper addresses the question of how variations in the earnings of public and private sector employees may be explained. The reasons identified in the international literature lay stress on the different attributes of employees in the public sector and the characteristics of their employment. Such characteristics often account for a significant part of the differential, but not it all. Most of the existing research has been undertaken by economists who increasingly recognise that, to explain the existence of any outstanding earnings premia, greater consideration needs to be given to possible explanations within the domains of industrial relations and politics.

In this paper, we hope to make a contribution to the literature by examining the case of public sector pay determination in Ireland. The Irish case is interesting for the very significant institutional innovations which have been introduced in recent years to reform public sector pay settlement under the aegis of national social partnership. We seek to make a contribution in two ways. First, we conducted an econometric analysis of two national data sets to examine the public sector earnings differential. After controlling for differences in employee characteristics and factors associated with the employees’ place of employment, we find a significant overall public sector premium, essentially an unexplained public sector ‘economic rent’. This premium rose considerably between 2003 and 2006, following the payment of the so-called benchmarking awards recommended by the Public Sector Benchmarking Body (PSBB). Second, in an attempt to account for changes in the overall public sector earnings premium, we examine the influence of changes in the composition of the labour market and the institutional context of wage bargaining. It is the first time that such a comprehensive analysis, combining an econometric approach with insights from industrial relations, has been conducted in Ireland to explain the existence of an earnings premium in the public sector. Analyses of this type are also rare in the international literature.

Literature review

The literature on public sector pay in labour economics is extensive and rich. An early attempt to review this literature – the vast bulk of which then had been conducted in the US – by

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1 Any discussion of “the” public sector or “the” private sector cannot overlook the caveat that such a simplification or aggregation is adopted usually for analytical convenience. As indeed has been pointed to by others (e.g. Gregory and Borland, 1999: 3575), there is considerable opportunity for labour market processes and outcomes – including wages and conditions of employment – to vary within both sectors of the economy.
Ehrenberg and Schwarz (1986) found there was considerable evidence for the presence of a public sector earnings premium. A later examination of the literature by Bender (1998), which included a large number of countries, found that the evidence for the presence of a wage premium was mixed. In the UK, the differential was found to be about 10% and, while it was significantly greater for female employees, there was some evidence that it had decreased through the 1990s. In Sweden, Denmark and the Netherlands, the premium was found to be small and, in some instances, negative. The differential in Australia was large and varied between 12% and 23%, and, in large part, was accountable to the higher qualifications of public sector employees. As with Ehrenberg and Schwarz (1986) review of the American evidence, Bender found that women and minority groups working in the public sector enjoyed higher earnings than their counterparts in the private sector. The presence of affirmative action programmes and a reduced level of gender and race discrimination in the public sector were considered to be important influences. A broadly comparable assessment of the presence of a public sector wage premium was presented in a subsequent review of the evidence by Gregory and Borland (1999).

The aforementioned economics literature attributes observed differentials to the personal characteristics of public sector employees (educational qualifications, age) and to specific characteristics of their employment (workplace size, geographical location and union status). Any unexplained component is usually attributed to ‘economic rent’ which is somehow acquired by public sector employees.

In recent research, Bender and Elliott (2002) examined whether the presence of a public sector pay premium might be explained by employees’ productive characteristics or by differences in the types of jobs people perform in the public sector. The former, of course, draws from human capital theory, while the latter is termed “a hybrid approach” which draws from the work of Belman and Heywood (1996) in the US. As well as focusing on differences in the occupational structure of employment in the private and public sectors, the latter also considers differences in the characteristics of the employee’s workplace. Research of this form remains relatively

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2 Gregory and Borland make the important observation, however, that as different studies within the one country often use different econometric techniques, include different explanatory variables and use different sample selection methods, estimates of the public sector earnings premium or discount often vary markedly. As a result, it is often difficult to arrive at definitive statements in respect of the size of the public sector wage premium between countries.
rare principally due to the absence of suitable data. The availability of the Social Change and Economic Life Initiative (S CELI) data set in the UK provided Bender and Elliott with a unique opportunity to examine the theoretical purchase of the so-called hybrid approach in explaining wage differentials.

Using a series of Blinder-Oaxaca decompositions and using the private sector as the reference wage structure and controlling for differences in employees’ human capital and the occupational composition in the two sectors, the earnings differential was found to be 9.6% for males and 24.2% for females. Once account was taken of employees’ job attributes, the earnings gap fell to 7.1% and 12.1% for males and females respectively. When the public sector was used instead as the reference wage structure, and conducting the same two tests as before, the differentials were reduced even more sharply, falling from 5.1% to 0.36% for males, and from 8.3% to 4.3% for females. The job attribute with the most significant level of influence was workplace size. The evidence from this study is indeed impressive in showing how, and to what degree, job attributes account for differences in average earnings between employees in the public and private sectors.

At this juncture, and certainly when the findings of Bender and Elliott’s (2002) research are considered, one might concede that the variables which are usually included in econometric models – employees’ personal characteristics, job attributes and the specific features of their employment – are likely to be sufficient to account for any identified difference in the earnings of public and private sector employees and that there may be little room for a political or industrial relations perspective. Before coming to such a view, however, we wish to look again at the findings from previous analyses, which would give one reason to be more circumspect.

We make the following observations. First, the study by Bender and Elliott is relatively unique in its ability to account – almost entirely – for the existence of a public sector earnings premium on the basis of workers’ characteristics and job attributes. Other research has invariably conceded that there is a significant component which it has not been able to explain (Ehrenberg and Schwarz 1986, Bender 1998, Gregory and Borland 1999; and, in Ireland, Boyle et al. 2004). In an attempt to account for such ‘unexplained’ variation, Bender (1998) – drawing from the work of Gunderson (1979) in Canada, Fogel and Lewin (1974) in the US,
and Gregory (1990) in the UK – highlights features of public sector employment, such as the ‘politics of wage setting’ and ‘vote producing’ activities, which distinguish it from the private sector. Public sector employees are identified as not only being significant in terms of their voting numbers, but, in their work, they are also seen to be able to influence the demand for, and the quality of, public services’ provision. As such, public sectors workers critically mediate the impression the public (i.e. the electorate) derive of a government’s ability to govern. Where public sector employees seek to gain advantage from their strategic position, governments may concede a wage premium to increase their prospects of re-election.

But the calculus informing government actions is unlikely to be fixed, as Gregory and Borland (1999) remind us. ‘Vote-maximisation’ may indeed come to trump ‘efficiency maximisation’ in some circumstances, but not in all contexts. Where voter demands for greater public sector efficiencies, including wage restraint, coincide with the presence of a confident, majority government, politicians may be well placed to prioritise and achieve efficiency gains and may move to bring earnings in the public sector in line with those in the private sector. But whichever situation might be said to prevail, it is expected that the politics of the wage determination process is likely to be an important factor in explaining the presence or absence of a public sector pay premium.3

Second, the structure of labour markets and the employment preferences of employers are also likely to be important influences. Consider the US evidence here. In an attempt to explain long-term changes in relative earnings, Gregory and Borland (1999) focus on levels of educational attainment. As the public sector employs larger numbers of graduates than the private sector, increases in real earnings for this cohort has the effect of increasing the public sector/private sector earning ratios. This would be grist to the mill for those proponents of a human capital approach, but such findings might mask other important changes in the structure of labour markets and the employment strategies of employers. To the extent that public service employment remains a place of secure employment and pay determination is governed by the

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3 It is of note that the wage premium available to public service workers has often been found to decline to zero or even turns negative as one moves down through the various levels of public sector employment, from federal to state to local employments. Such variation might suggest that the premium identified at central government level cannot simply be attributed to the presence of a “public sector” effect. Plainly something else is at work which may be attributable to the location of employment, the ‘politics’ of that employment and, perhaps also, to the level at which collective bargaining is conducted (Freeman 1987; Bender 1998; Ehrenberg and Schwarz 1986: 1248).
maintenance of unified structures and centralised collective bargaining, and private sector employment become more variable and flexible, achieved in part by the introduction of ‘subordinate’ forms of employment, such as temporary and casual work, as union power declines, we may come to witness increased divergences in the earnings of public and private sector workers. Thus, differences in pay levels may not solely be attributed to the occupational composition or skill profile of public sector employees, but they may also be rooted in the different recruitment strategies and labour market structures within which management in the two sectors operate.

Third, differences in earnings might be explained by the manner in which the two sectors respond to changes in macro-economic conditions. There is considerable evidence, for example, that private sector earnings tend to be procyclical, while public sector earnings tend to exhibit less cyclicality. Hence we might expect the ratio of earnings to vary depending on a given country’s economic fortunes and the manner and speed at which earnings in either sector respond to macro-economic circumstances.4

Fourth, short-run fluctuations in wage differentials, on the other hand, might be better accounted for by changes in the industrial relations context, such as the structure of collective bargaining, the power of trade unions and the determination of governments to impose their will on the pay determination process. An interesting account of such influences in the UK is provided by Gregory (1990).

From the foregoing review, the following factors might be identified a priori as providing a possible basis for explaining the presence of a public sector wage premium in Ireland:

1. Employee characteristics (education, experience, etc.). Such a modus of explanation has its roots in human capital theory (Mincer 1974, Chiswick 2003).
2. Job attributes (size of workplace, nature of work, etc).
3. The structure of the labour market and employer recruitment preferences. There are two sides to this factor: the labour supply and changes therein and the ability and preferences of employers to hire new employees on inferior or subordinate contractual terms. We would

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4 An important corollary of any such time-series variation in public/private sector earnings ratios, as Gregory and Borland (1999) emphasise, is that caution is required in making any large inferences in respect of wage premia from data which are cross-sectional or which cover only a limited number of time periods.
expect the preferences of employers and their freedom of manoeuvre to vary between the two sectors. To the extent that there is a ready supply of relatively cheap labour and a willingness amongst private sector employers to alter their recruitment practices, we would expect to see a growth in low earnings employment and a commensurate increase in the gap of private and public sector earnings.

4. Union power and the political context of collective bargaining. This perspective involves a consideration of the capacity of public sector unions to pursue wage increases and, in turn, the extent to which government is willing, or feels compelled, to concede to union demands. How a government responds is likely to vary depending on: the political sensitivities surrounding the delivery of quality public services; the importance attached to seeking efficiencies and the reform of public service provision through the maintenance of stable industrial relations; and finally, the extent to which the adoption of a confrontational posture in dealings with public service employees and unions might be countenanced.

5. Macro-economic circumstances. Different market circumstances are likely to impose different pressures on government in the regulation of pay.

The Context of Pay Determination in Irish Public Services Before 2000

*Internal and external relativities.* The Irish system of public sector pay determination sought to justify wage increases primarily on the basis of external relativities; internal relativities were permitted but only in the context of occupations which lacked a direct comparator in the private sector. A complex system of conciliation and arbitration developed as a means for adjudicating on wage claims. Over recent decades, however, the principles informing the determination of pay in the public sector were turned on their head: the secondary principle of internal relativities came to override the primary criterion of fixing wages on the basis of fair comparison with rates in the private sector. So-called ‘marker grades’ – principally executive and higher executive officers – set the initial wage norm, while linked grades and related occupations sought to use such settlements as a target norm or, as increasingly became the case, a floor upon which they endeavoured to secure even larger increases. There thus developed a complex system of inter-linked wage relativities where wage

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5 The one significant exception was the Crafts Analogue Review which, every four years or so, set the pay of craft employees (and related general operatives) by drawing on comparisons with employees in an agreed group of comparable private sector and semi-state companies.
increases were sought on the back of cross-occupational relativities, leapfrogging claims and industrial muscle.⁶

Over many decades successive governments attempted to initiate reform. Ad hoc efforts were variously and at different times cast as wage freezes, embargoes on “special” pay claims, the prohibition of second-tier bargaining (during periods of centralised pay bargaining), as well as appeals to the consideration of the State’s “ability to pay”. Very often, governments’ attempts to hold fast were abandoned in the face of union resistance and militancy. There thus continued a practice through recent decades, up to and including the 1990s, of muddling through with little, if any, attempt to reform public service pay determination in a fundamental manner.

_The adoption of social partnership._ The return to a centralised and co-ordinated approach to wage bargaining under social partnership in the late 1980s might have augured well for the reform of public service pay settlement. It certainly had a very significant effect on the moderation of wage increases and in the maintenance of industrial peace in the private sector.⁷ Successive national wage agreements in the early and mid 1990s laid down basic wage increases. Additional wage claims were permitted under the guise of productivity and flexibility deals, but these were to be set within tight parameters. Industrial action in the pursuit of claims in excess of those set out in the agreements was prohibited. Early optimism that these efforts might establish a more orderly process of wage determination was soon dashed, however. Initial attempts by the government to cap wage increases and to be resolute in refusing to grant special wage awards gave way to the by then familiar posture of alternating between refusing, postponing and, in the face of union resistance, conceding to special wage claims. As the economic boom of the late 1990s took off and as private sector wages increased, the perception amongst public service employees that their salaries were inferior to those of the private sector took hold and made for difficult and tense relations between the Government and public sector unions. The climate of industrial relations was further exacerbated by claims of increased staff work loads, declining staff morale, recruitment and retention problems in a

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⁶ A review of strike levels from 1960 to 1995 illustrates how the public sector came to account for a greater share of overall strike activity in the 1980s and 1990s (Brannick et al. 1997). By the early to mid 1990s, public sector workers were three times as likely to strike as their counterparts in the private sector.

⁷ See the Appendix below for a brief account of the system of pay fixing which developed under social partnership in Ireland in the late 1980s.
tightening labour market and an inability to reward staff for the acquisition of new skills and responsibilities.

A series of difficult and protracted industrial disputes in the late 1990s marked a significant turning point. Foremost amongst these was the nurses’ pay dispute which, in its various phases, lasted from 1995 to 1999, culminating in a nine day strike. Staff nurses secured increases worth 26%, ward sisters attained an increase of 37.4% and directors of nursing were awarded a 46.6% increase. During the nurses’ dispute, the Gardaí (the Irish police force) put in a claim for a 15% increase and, on rebuttal, marched on parliament. This was later followed by a bout of so-called ‘blue-flu’ where officers, abiding by their obligation not to go on strike, reported sick instead. These disputes gave rise to widespread concern amongst the public. The situation was further exacerbated when many large groups of public servants, mainly in white collar positions, claimed that they had been disadvantaged by having settled their pay claims early and for having abided by the terms agreed in national agreements. Unease amongst such groups eventually led to pressure which forced the Government into the unusual position of conceding additional top up increases to make up for any shortfall. It was observed: “Public sector pay policy had all but collapsed. A pay policy originally worth 3% had delivered 20% for many and the Government’s credibility on the issue of public sector pay had been undermined” (Hastings et al. 2007: 131-2). The then Minister for Finance and now EU Commissioner, Charlie McCreevy, remarked, “it was mad because you could not finish anything”. It was “doctors, followed by nurses, following firemen and county council employees... The circle would never end.”

A debate with renewed urgency took hold in the late 1990s and early 2000s. In pressing for reform, employer groups argued that public sector workers needed to give greater consideration to the public finances’ ability to meet pay claims and that cognizance also needed to be taken of the favourable employment conditions (employment security and pension provisions) enjoyed by public servants. Senior union representatives, too, accepted that a continuation of the existing pay determination system was untenable. As well as accepting that it was an unwieldy and, at times, chaotic edifice, they had also come to recognise that its central pivots – the ‘marking’ of certain grades’ wage increases, the pursuit of leapfrogging

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8 Quoted in Hastings et al. 2007: 134.
claims and trials by industrial muscle – had strained and embittered relations between unions. Marker grades’ unions grew increasingly resentful of the enforced role placed upon them. In turn, they often felt compelled to seek to restrain other (late settler) unions’ ambitions. Such complexities and tensions led to the withdrawal of the teachers’ union, the ASTI, from the Irish Congress of Trade Unions (ICTU) in the late 1990s. There developed thus a fear that the disorder attending the system of wage determination was creating deep divisions within and between public sector unions, and with unions in the private sector, which risked undermining the cohesion of the ICTU and, more broadly, unions’ role within social partnership.

The promise of benchmarking. Discussions between the Government and the ICTU Public Service Unions Committee eventually led to the germination of the concept of “benchmarking” whereby wage increases in the public service would be based on comparing public service jobs, grades and salaries with private sector occupational analogues. The Government was widely seen to exhibit a new resolve in achieving reform: “Benchmarking was the product of a political conviction: come hell or high water the old system of relativities had to end and the end had to be permanent” (senior union representative). In 2000, under the fifth social partnership agreement, Programme for Prosperity and Fairness (PPF) (2000-02), a pay review body called the Public Service Benchmarking Body (PSBB) was established. Mr Ahern, the Prime Minister, was at pains to point out that, while change would come through negotiation, any new system would not permit ‘separate or free standing’ pay mechanisms for different parts of the public service (Hastings et al. 2007). Cross-sectoral relativities were declared an invalid basis for comparison.10

9 In this respect, Ireland was to stand apart from other countries (e.g. the UK, Sweden and Australia) where the reform of public sector pay determination was synonymous with the decentralisation of pay bargaining and the individualisation of pay (see Elliott and Bender 1997; OECD 1994). In Ireland, performance related pay (PRP) has only become a feature of a very small number of senior civil servants’ compensation plans. Otherwise, the idea that PRP might provide an effective means for enhancing public sector performance has failed to receive widespread endorsement. In agreeing to work with the PSBB, public sector unions were assured that PRP would not be introduced.

10 A separate review body covering the pay of higher public servants, as well as members of the judiciary, members of parliament and government ministers, has traditionally (since 1969) advised the government on remuneration levels appropriate to employees in these categories. The so-called Review Body on Higher Remuneration (sic) in the Public Sector reported every four years or so, and as happened, reported shortly after the PSBB was established. It recommended pay increases of between 7 and 33% with an average increase of 12%. In anticipation that its recommendations might come to be used by unions to garner support for similar increases for other public service groups from this review” (quoted in IRN, 6, 2001). When the Buckley Report was published it was explicit in its view that the salaries of high ranking public servants were substantially lower than those of comparable occupations in the private sector. In making such an
The work of the PSBB followed a number of stages. First, written submissions were taken from unions and employers which were then exchanged and were followed by written observations on each party’s initial submission. Leading management consultancy firms were hired to research job profiles and wage rates. A specific job evaluation scheme was designed for this purpose. A series of job ‘factors’ or components were identified, defined and allocated specified weightings and operationalized in a job evaluation questionnaire. Questionnaires were then administered to a representative sample of almost 4,000 employees in the public sector and, of those, 347 underwent a comprehensive one-to-one in-depth interview with the PSBB’s consultants. With the help of the Central Statistics Office (CSO), the PSBB identified an appropriate sample of private sector companies in respect of sector, size and geographical location. In all, 202 firms were chosen for study covering over 46,000 employees and some 3,500 jobs were evaluated. Information was also collected in respect of pay, benefits and conditions of employment attached to each identified job.  

An analysis of CSO data on average wage rates in the public and private sectors was also prepared by the PSBB. It found that over the period 1988 to 2000, public servants were on average better paid than private sector employees. (We conduct a similar analysis in Figure 1 using data from 1998 to 2006). The analysis was deemed to be of limited value, however, as it was unable to control for the independent influence of such factors as workplace size, educational attainment, gender and age. Given these limitations, its findings that average earnings in the public sector exceeded those in the private sector by an average of 13% passed little muster with the unions and were roundly dismissed. These data were not published in the PSBB’s final report.

--- Figure 1 Here ---

It was widely perceived to have been a considerable achievement for the PSBB to have brought all public sector occupational groups under the remit of the one pay determination system.

unambiguous statement, the Buckley Report was to stand in stark contrast to the forthcoming PSBB report’s reluctance in making such explicit statements. See discussion below.

11 Further details on the PSBB study’s methodology can be found in Chapter 3 of the Body’s final report see: http://www.finance.gov.ie/documents/publications/other/Bench.pdf.

12 Such data only became available some time after the PSBB finalised its report in June 2002 when the CSO conducted the first NES survey in 2003. We use data from this first survey together with data from the March 2006 survey in our analysis below.
without regard to traditional relativities. Nevertheless, expectations amongst supporters of the process that the report would recommend substantial increases took firm hold. “The perception at the time was that there was a huge lag behind the private sector: this was an entrenched view” (senior union representative).

The 2002 recommendations of the public sector benchmarking body. The PSBB’s report, in the main, received a positive but guarded reception from union leaders. The size of the recommended pay awards was seen to vindicate their prior claim that public service workers were significantly underpaid in comparison to their counterparts in the private sector. While there was some arguments over some groups of workers losing out in comparison to others – notably nurses, gardaí, prison officers and fire-fighters – reflecting how deeply embedded such relativities had become in the industrial relations mindset, these were relatively minor objections which failed to generate significant support. The average pay award was 8.9%. Senior nurse managers received increases of between 12 and 16%; medical technicians obtained 25%; teachers 13%; while gardaí, university lectures and technical grades in engineering received lower awards of between 3 to 6%. The awards were widely seen to be generous when placed alongside the cumulative pay increases of between 18% and 21.5% together with the tax concessions agreed under the national wage agreement, the PPF.

Other elements of the PSSB’s report were to prove more controversial, however. Remarkably, the PSBB did not publish or make otherwise available to outside observers, or indeed to unions, employers or government, any data or evidence with respect to pay levels in the public and private sectors. The PSBB’s data was also exempted from the provisions of the Freedom of Information Act. Perhaps even more confounding was the reticence of the reports’ authors to

13 There were, however, two legal challenges to the report. One was taken by the university teachers’ union, IFUT. It succeeded in gaining leave to seek a judicial review to quash the report’s recommendations in regard to its own members and to require the PSBB to reveal the reasons for its recommendations. Another union, the CPSU lodged a complaint under the Employment Equality Act, 1998, arguing that the report’s recommendations discriminated against women in that it awarded larger increases to staff in senior positions who are predominantly male, compared to lower staff grades which are occupied predominantly by females. IFUT subsequently withdrew its challenge. The CPSU case was dismissed by the Equality Tribunal and later by the Labour Court. If either or both of these cases had been successful, there was the prospect that not only would the PSBB have been forced to reveal how it arrived at its recommendations, but also that it might have encouraged other disaffected groups to challenge the report and its recommendations.

14 The first 25% of the award was paid up front without any conditions as had been agreed between the parties in advance, but the remaining 75% was conditional on verifiable programmes of work practice changes and modernisation in the delivery of public services.
state explicitly that public sector wage rates lagged behind those of the private sector. It is rather implied or assumed that the recommended wage increases were warranted and deserving.\textsuperscript{15} This lack of openness and transparency was to become the focus for much criticism amongst independent observers and critics of the benchmarking process. (See discussion below). The PSBB was dissolved immediately after publishing its report.

\textit{A review of recent Irish econometric research on public sector pay.} Before turning to the current study’s analysis, we examine significant Irish econometric research on the presence of public sector wage premium. Until recently, the most recent and important paper was that by Boyle\textit{ et al.} (2004). Using data collected by the Economic and Social Research Institute (ESRI) under the auspices of the European Community Household Panel, the authors found that Irish public sector workers’ average gross monthly earnings in 2001 were 46\% more than their counterparts in the private sector. When differences in employee attributes and job characteristics were controlled for, the wage premium was estimated to be 13\%. This is a relatively large premium by international standards (Lucifora and Meurs 2006; Disney and Gosling 2003).\textsuperscript{16} In common with most other international research, the premium was found to be significantly greater for employees near the bottom of the wage distribution than for those near the top, and was significantly greater for women than men in the mid 1990s although not at the end of the 1990s.

Boyle\textit{ et al.} (2004) also found that there was little change in the size of the wage premium between 1994 and 2001.\textsuperscript{17} This is significant as this was a period of significant economic expansion in Ireland: real GDP doubled, GNP increased at an annual average rate of almost 8\% in real terms, total employment grew by a cumulative 45\%; and the labour market tightened considerably (unemployment fell from 15.7\% in 1993 to 3.6\% in 2001). See Table 1. As Boyle\textit{ et al.} emphasise, it might be expected that, under such circumstances, wages in the private

\textsuperscript{15} See, in particular, para. 2.11 of the report.

\textsuperscript{16} Boyle et al.’s measure of earnings does not include other elements of employee compensation such as pension provision and benefits-in-kind. If such other elements were to be included, they might be expected to increase the size of the wage premium even further, save perhaps for employees at the top echelons of the wage distribution.

\textsuperscript{17} In principle, the ECHP provides an ideal means for estimating changes in wage rates over time: it is a panel data set, it tracks the same individuals over the given time period and, importantly, allows for the control of unobserved individual effects. In practice, however, this is hard to do as the sample size is quite small. For example, the number of individuals moving from one sector to another is small. Further, attrition bias (the loss of individuals over time from the sample) may be important. Boyle et al. analyse the earnings of 3,246 individuals in 1994 and only 1,494 of the same individuals remain in the sample in 2001.
sector would rise quickly as competition for a declining pool of labour intensified thereby reducing the public sector wage premium. This would not seem to have occurred. Of course, the Irish labour market is extremely open.

--- Table 1 Here ---

In seeking to explain why the public sector wage premium is so large in Ireland and why it has remained so in recent years, Boyle et al. (2004) ponder whether the answer might lie with the “wage bargaining framework”. Their paper concludes: “an obvious hypothesis suggests itself. It is that Ireland’s social partnership model, and in particular the enormous value that politicians and policy-makers attached to it, conferred on Irish public sector trade unions greater bargaining power than they would otherwise have had… public sector unions were thus enabled to …more successfully pursue pay claims that matched the increases taking place across the private sector during the Celtic Tiger period” (Boyle et al. 2004: 22).¹⁸

**Data and Empirical Analysis**

We use the March 2003 and 2006 National Employment Survey (NES) anonymised micro datasets to estimate the ceteris paribus public sector earnings premium or discount. The NES is a major new workplace survey conducted by the Irish Central Statistics Office (CSO). The survey covers both the public and private sectors using the same methodology. The purpose of the NES is to provide detailed information on workplace employment issues, including earnings, and factors influencing earnings such as sector of activity, occupation, educational attainment, age group, length of service and nationality.

The 2003 NES was collected two months before the first benchmarking payments were made. It does, however, include the wage increases awarded to higher public servants under the

¹⁸ There are two other studies which deserve mention. O’Connell and Russell (2006) look at the public sector wage premium in respect of third level graduates. Once a variety of personal and occupational characteristics are controlled for a wage premium of 20% is identified. Hourly wages are used as the basis of comparison. When the monthly earnings of graduates working full-time are examined, the premium falls to 14% and falls further to 9% after controlling for compositional influences. When bonus payments are taken account of, which are more common in the private sector, the premium falls to 7%. Casey (2004) uses macroeconomic earnings data for full-time employees to construct aggregate and sectoral hourly earnings indicators for the period 1998 Q1 to 2003 Q3. He finds that the public sector (excluding health) had the largest premium over the national average – over 30%. However, over the same period, earnings grew disproportionately faster (about 1.5% per annum) in the private sector, which led to a reduction in the public sector earnings premium. Casey’s results are for hourly earnings only and do not control for important differences in the sample composition by sector.
Buckley Report (see fn. 10 above). The 2006 NES does capture the effect of the benchmarking awards (3-27%) along with wage increases recommended under the social partnership wage agreement, Sustaining Progress (7%), including almost half of the increase agreed under the Mid-Term Review (5.5 - 6%); and for senior civil servants, the increases recommended under their Review Body’s reports, No. 40 (7.5%) and No. 41 (senior positions in the Health Service Executive, 4%).

Econometric Models
We estimate a number of econometric models using the March 2003 and March 2006 NES datasets. All results are reported in Tables 2a and 2b.

Basic earnings regression equation. When examining the public sector earnings differential, one is interested in the “ceteris paribus” effect of being employed in the public sector, controlling for relevant factors such as age, sex and educational level. The simplest method involves running an ordinary least squares (OLS) regression of the natural log of earnings \( \ln w_i \) where the subscript \( i \) stands for individual \( i \) on a set of \( K \) relevant explanatory variables (denoted by \( x_{ij} \) where \( j \) ranges from 1 to \( K \)) and a dummy variable (denoted by \( d_i \)) for working in the public sector.\(^{19}\) This is a standard, augmented Mincer (1974) type or hedonic earnings equation.\(^{20}\)

The explanatory variables typically include individual characteristics of the workers and their job and firm characteristics. We used the following explanatory variables when modelling weekly earnings: age and age squared (to capture non-linear effects); sex; experience; highest level of education; occupation (Standard Occupation Classification; SOC’s 1-9); full-time/part-time; permanent/temporary; log hours and log 38+ hours (to capture overtime effects). Generally, adding such additional explanatory variables reduces the size of the estimated public sector premium or discount.

\(^{19}\) A dummy variable is a 0 or 1 coded variable which indicates the presence or absence of some characteristic such as being male or working in the public sector.

\(^{20}\) Mincer type or hedonic earnings equations are described in almost all labour economics textbooks (e.g. Borjas 2004 and Ehrenberg and Smith 2003) and most econometrics textbooks (e.g. Wooldridge 2003). They are very widely used.
The basic earnings equation may be represented by the following equation:

(1) \[ \ln w_i = \alpha + \sum_j \beta_j x_{ij} + \gamma d_i + u_i \]

where \( u_i \) is a (possibly heteroscedastic) random error term, which captures a range of omitted, unmeasured factors and measurement error in earnings (assuming a correctly specified model). In this equation, \( \alpha \) is just the constant or intercept term. The \( \beta \)'s and \( \gamma \) coefficients measure the “return” or contribution to log earnings of the various explanatory variables (experience, sex, educational level etc.) and working in the public sector. We estimate a gamma coefficient of +0.08 which suggests that public sector workers earn approximately 8% more than private sector workers, other things being equal. Unfortunately, this basic earnings equation is generally too simple. It assumes that the \( \beta \)'s or returns to the various personal characteristics are the same in the public and private sectors. The international literature suggests that this is not the case.

The weakness of the public sector dummy variable approach is that it models the effect of sector as an “intercept” shift, where returns to productivity related characteristics and job attributes are restricted to be equal across sectors. It thus fails to address the issue of how much of the difference in average earnings between sectors is due to observable differences in worker characteristics and job attributes between sectors and to differences in the returns to worker characteristics and job attributes in the two sectors. The former would help to tell us whether any difference in earnings is due to workers in one sector possessing different skills to those of the other sector, or simply that employees work at different jobs in either sector. The latter, on the other hand, helps us address the critical question of whether an employee working at the same job with the same characteristics is paid more or less in the public sector or in the private sector. This is the reason why we consider more general models of earnings and Blinder-Oaxaca decompositions (Blinder 1973, Oaxaca 1973).

A more general model of earnings in the two sectors. The more general model consists of two earnings equations, one for the public sector (denoted by the superscript \( \text{pub} \)) and one for the private sector (superscript \( \text{pri} \)):

\[ \ln w_i^{\text{pub}} = \alpha^{\text{pub}} + \sum_j \beta_j^{\text{pub}} x_{ij} + \gamma^{\text{pub}} d_i + u_i^{\text{pub}} \]
\[ \ln w_i^{\text{pri}} = \alpha^{\text{pri}} + \sum_j \beta_j^{\text{pri}} x_{ij} + \gamma^{\text{pri}} d_i + u_i^{\text{pri}} \]
This model nests the previous model as a special case. Of course, it is important to check the specification of the model thoroughly so that it provides a good fit to the data. In common with the practice in the international literature, we estimated separate equations for males and females, as well as for various occupation groups. In addition, we estimated least absolute deviation (LAD)/median regressions, which are robust to outliers, and obtained similar results.

*The Blinder-Oaxaca decomposition of earnings differentials.* Estimates of the public and private sector earnings equations in (2) may be used to decompose the difference in log average earnings in the two sectors into two components - (i) the part due to differences in the average characteristics of the workforce and jobs in the public and private sectors and (ii) the remainder due to differences in the returns to the various characteristics in the two sectors (Blinder 1973, Oaxaca 1973). The public sector premium or discount consists of the latter component.

Assuming we treat the public sector as the reference group, the equation for the Blinder-Oaxaca decomposition is:

\[
\ln w^{\text{pub}} - \ln w^{\text{pri}} = \sum_j \beta_j^{\text{pub}} \left( \bar{x}_j^{\text{pub}} - \bar{x}_j^{\text{pri}} \right) + \left( \bar{\alpha}^{\text{pub}} - \bar{\alpha}^{\text{pri}} \right) + \sum_j \left( \beta_j^{\text{pub}} - \beta_j^{\text{pri}} \right) \bar{x}_j^{\text{pri}}
\]

In this equation, the bars denote averages and the estimated coefficients are denoted by a hat. \(^{21}\) The term on the right hand side of the first line of this equation is the difference in log of average earnings which is explained by the difference in the composition (i.e. personal, job and firm characteristics) of the public and private workforces. The term on the second line is the net public sector premium or discount which is discussed in the literature. \(^{22}\)

*Propensity score matching.* It is important that we compare “like with like” individuals (in terms of the observed explanatory variables) in the public and private sectors when decomposing the earnings differential. Technically, we want the two groups to have a

\(^{21}\) There are no residual terms in the standard Blinder-Oaxaca decomposition since the average of the OLS residuals are always zero.

\(^{22}\) The Blinder-Oaxaca decomposition is not unique. If the private sector is treated as the reference group, the first component in the Blinder-Oaxaca decomposition is \(\sum_j \beta_j^{\text{pri}} \left( \bar{x}_j^{\text{pub}} - \bar{x}_j^{\text{pri}} \right)\) as opposed to \(\sum_j \beta_j^{\text{pub}} \left( \bar{x}_j^{\text{pub}} - \bar{x}_j^{\text{pri}} \right)\).

“common support”. This is achieved by matching individuals on the basis of their propensity score (i.e. the estimated probability of being employed in the public sector) and discard sub-samples with little common support. For example, see Morgan and Harding (2006). We used the propensity score matching procedures in Becker and Ichino (2002). It turns out that the propensity score results are very similar to the OLS dummy variable and Blinder-Oaxaca results, which is in line with the a priori arguments made by Angrist and Pischke (2009).

Selection and other issues. There is a large, rather involved literature dealing with issues of treatment effects and selection bias (as well as other issues such as endogeneity) in wage equations - see Lee (2005) and Wooldridge (2003, Chapter 18) for example. Selectivity bias may occur when the choice of sector of employment is non-random. Although some researchers present estimated public-private sector earnings equations that take account of selection bias, it is not obvious that one is interested in ex-ante public-private sector earnings differential i.e. the differential netting out selection effects. One is generally interested in the ex-post earnings differential, i.e. the differential including any selection effects.

Econometrics results. Various estimates of the public sector premium in gross weekly earnings in 2003 and 2006 are set out in Tables 2(a) and 2(b), using unweighted and weighted (grossed up) NES data respectively. We present weighted and unweighted results since there is some disagreement in the literature regarding the desirability and/or best method of weighting regression results (e.g. Deaton 1997, Gelaman 2009). The OLS regression results with a public sector dummy, Blinder-Oaxaca decomposition results and propensity score results are pretty consistent, which is reassuring. Separate results are also presented for males and females and all employees and “core” employees i.e. full-time, permanent employees aged 25 to 59.

23 The sample sizes and adjusted R²’s for the basic OLS dummy variable models for males and females combined are (i) 46.4 thousand and 0.71 in 2003 and (ii) 48.5 thousand and 0.70 in 2006. The explanatory variables are highly significant and have the correct sign and order of magnitude. Earnings are positively correlated with age, education attainment, experience, hours of work and hours of overtime. Permanent employees (other things being equal) are paid more than non permanent, similarly for full-time employees (vis-à-vis non full-time).

24 The OLS dummy variable results are similar to those in Kelly et al. (2009), who use a very similar model to that used by Murphy and Ernst & Young (2007).
The 2003 NES results, which exclude most benchmarking pay awards, suggest that the overall public sector premium in log weekly earnings was about 11%. The estimates range from 8% to 15%, depending on the econometric technique and whether or not the sample is grossed up. The average premia for males and females are in the range of 5% to 9% for males and 11% to 15% for females. Note that there is considerable variation in the estimated premia by occupation group and by earnings decile, which we ignore here.

--- Tables 2(a) and 2(b) Here ---

The 2006 (post Benchmarking) results are striking. The overall public sector premium in log weekly earnings had jumped to over 20%, the estimates ranging from 18% to 25%, with similar premia for both males and females. An analysis of the data by occupation group (SOC) results in a very large public sector premium of over 50% in SOC 6: Personal and Protective Services, which includes the police force and prison officers, *inter alia*. However, when SOC 6 is omitted from the analysis, the public sector premium for males and females combined still grew substantially from between 6% to 7% in 2003 to between 12% and 17% in 2006.

--- Table 3 Here ---

**The Labour Market and the Influence of Migration**

The focus of this section is to examine the possible influence of labour supply on earnings in the private and public sectors. A remarkable feature of Ireland’s demographic structure has been the extraordinary pace at which it has moved from being characterised by net outward migration to one of significant inward migration. Between 1986 and 1991 net outward migration was estimated at an annual average of 27,000 people. The period 1996 to 2002 recorded an average annual inward growth of 26,000. The magnitude of immigration flows increased further in the most recent intercensal period, 2002 to 2006, to produce an annual average net migration figure of 46,000 (CSO, 2006).

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25 Strictly speaking, the results are for the public service (i.e. the public sector excluding semi-state bodies) and the estimated percentage premium in earnings, as opposed to log earnings, is 100 times $e^{0.11} - 1$.

26 Note that there is considerable variation in the estimated public sector premium / discount by occupation group and by earnings decile, which we ignore here.
Ireland was only one of three countries (the UK and Sweden being the others) of the original EU-15 countries to grant workers from the 10 new accession member states (NMS) free access to its labour market and to take up residence upon accession to the EU in May 2004. Of the three countries, Ireland attracted the largest number of NMS migrants relative to its size (Barrell et al. 2007). In 2002, it was estimated that there were less than 20,000 nationals from the NMS employed in Ireland. Within four years, this figure had reached 126,000, an increase of almost 650% (Quinn et al. 2008). Between 2004 and 2007, over 320,000 PPS numbers were issued to EU10 migrants, of which 60% were allocated to Polish workers (Fás 2007). In 2007, foreign workers represented close to 14% of the Irish workforce, which is believed to rank as one of the highest percentages of foreign workers in a country’s labour force in Western Europe (Fás 2007). By any standards, this is an extraordinary transformation in a country’s demographic structure and workforce profile.

Workers from the NMS are largely concentrated in four sectors: manufacturing, construction, wholesale/retail trade and hotels and catering. Large numbers of immigrants from outside the EU also work in the hotel and catering industry and many – mostly Asian workers – work in health and social work. By contrast, public administration and defence account for the lowest proportion of non-Irish national employees at 2.6% (CSO 2008).

The questions in the present context are: what has been the effect of this large influx of migrants on the labour market and wage patterns? Has the employment of large numbers of foreign workers moderated wage pressures in the private sector such that employees’ pay levels have come to lag behind those of comparable public sector employees? To date there has been little research which has addressed this question directly. There is one study by Barrett (2009) which, by drawing on previous research findings (from 1966 to 2002) and by taking account of the recent influx of migrants from the NMS, seeks to “infer” or simulate the impact of immigration on wage rates. In their simulation of the likely effects, they find that wages fall (on average) by 7.8%.28

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27 PPS (social security) numbers are issued by the Department of Social and Family Affairs and are required to take up employment. The number of immigrants receiving such permits is significantly greater than the number recorded by the CSO. The discrepancy is explained by the short-term duration of stay by many migrants (see Barrett 2009).

28 There are other studies which have examined the presence of a wage gap between migrants and native Irish workers. Using data from the 2005 EU Survey of Income and Living Conditions, Barrett and McCarthy (2007)
In the international economics literature, however, the balance of the economic research appears to suggest that the share of immigrants in the workforce has little or no impact on the pay rates of the existing workforce (e.g. Friedberg and Hunt 1995, Card 2005, Dustmann et al. 2005 and Manacorda et al. 2006). But it is an area of research where there remains ongoing controversy as exemplified, for example, by research into the impact of the Mariel boatlift of Cubans into the Miami labour market. Card (1990) reports small wage effects whilst Borjas (2003) reports large negative wage effects at the national level, once out-migration of the existing workforce is taken account of. However, Card and diNardo (2000) cast doubt on the Borjas results.

In a recent contribution, Nickell and Salaheen (2008) note that most economic research has concentrated on looking for wage effects by skill level, where skill levels are defined in terms of education. Unfortunately, it is quite difficult to compare educational qualifications across countries. Moreover, it is well known that many immigrants with high qualifications work in low skill occupations. In the light of these two factors, Nickell and Saleheen (2008) model the impact of immigration on occupation wages by region using Labour Force Survey and Annual Survey of Hours and earnings (ASHE) / New Earnings Survey (NES) data for Britain for the period 1992 to 2006. They find that, once the occupational breakdown is incorporated into a regional analysis of immigration in Britain, the share of immigrants in the workforce has a significant, small, negative impact on average wages. Closer examination reveals that the biggest impact is in the semi/unskilled services sector. This finding accords well with intuition and anecdote, but does not seem to have been recorded previously in the empirical literature.29

We now turn to consider some evidence for Ireland. Table 4 shows the share of recent (past three years), non-Irish immigrants in employment in 2003 and 2006 alongside the growth in

found a substantial wage gap (32%) between native workers and recently arrived EU10 immigrants. A more sophisticated analysis using the NES 2006 by Barrett et al. (2008) found an 18% and 14% wage gap between Irish workers and workers from the NMS and from non-EU/non-English speaking countries respectively. The concentration of immigrant employees in sectors and occupations which are characterised by lower than average earnings was found to account for a large proportion of this variation, but net of these effects, there was still a significant wage disadvantage: 10% for NMS employees and 5% for employees from non-EU/non-English speaking countries. Subsequent statistical tests revealed that, while there was no wage gap at the lowest level of educational attainment, the earnings disadvantage generally rose with educational attainment. A statistically significant wage gap was found also to exist between Irish and NMS workers across all deciles in the earnings distribution ranging from 4% and 5% at the 10th and 20th deciles respectively to 13% and 16% in the 80th and 90th deciles.

employment and weekly earnings.\textsuperscript{30} The share of recent immigrants rose from 4.2% to 6.6%. However, this rise was not uniform across industries or occupations. In some occupations and industries, including Public Administration and Defence, the share of recent immigrants fell. In other cases, the share more than doubled e.g. the Construction industry, SOC 5: Craft and Related Occupations, SOC 8: Plant and Machinery Operatives and SOC 9: Other Occupations. Table 4 shows that wage rates did not increase as quickly in those parts of the private sector where migrants were employed in significant numbers.

--- Tables 4a and 4b Here ---

The Nickell and Salaheen (2008) results suggest that the large rise in the share of immigrants in various occupations in Ireland may have driven up the estimated public sector premium to some extent. The basic regression results in Table 5 for earnings by occupation suggest that a rise in the share of migrants is associated with reduced earnings, which is consistent with the Nickell and Salaheen (2008) findings. Of course, these results are only suggestive since earnings and employment are simultaneously determined. A more structural model is required to address the criticism that we are just looking at correlations in the data and are not identifying causal effects.\textsuperscript{31}

--- Tables 5 and 6 Here ---

Some very preliminary results along these lines are presented in Table 6. There are a number of data issues with the anonymised Quarterly National Household Survey data provided by the CSO and, pending the release of revised datasets, we cannot directly apply the Nickell and

\textsuperscript{30} The employment data are from the 2003 Q2 and 2006 Q2 QNHS anonymised micro datasets. The QNHS is a labour force survey and uses ILO definitions of employment, unemployment and inactivity. The earnings data are from the published March 2003 and March 2006 National Employment Survey (NES).

\textsuperscript{31} In Nickell and Salaheen (2008), other things being equal, labour demand in a particular occupation and region depends negatively on the real wage and (possibly) the share of immigrants, assuming migrant workers are less productive than other workers. Labour supply and share of immigrants depend positively on the current real wage and last period’s share of immigrants, and negatively on last period’s unemployment rate, ceteris paribus. Solving the model, the real wage in a particular occupation and region depends positively on last period’s unemployment rate and negatively on last period’s share of immigrants share in this occupation and region, ceteris paribus. The lagged unemployment rate effect is positive mainly because high unemployment last period reduces the supply of labour to that occupation and region. The lagged unemployment rate (share of migrants) effect is positive (negative) mainly because a high unemployment rate (share of migrants) last period reduces (increases) labour supply this period, which drives up (down) real wages, ceteris paribus.
Salaheen (2008) model to Ireland.\textsuperscript{32} However, the fixed effects regression results in Table 6 suggest that wages in a particular occupation are sensitive to the lagged employment rate and the lagged share of immigrants, with correctly signed effects. Unfortunately, both effects are statistically insignificant, since we do not currently have access to the correct data. The point estimate of the lagged migrant share effect suggests that a 5 percentage point rise in the share of migrants in a given sector may have reduced earnings by up to one and a quarter percent. Given the limitations of our analysis, this finding must be treated with caution. However, the evidence does suggest that, where migrant workers gained employment in large numbers in the private sector, they acted as a brake on wage growth, which resulted in a higher public sector average premium.

\textbf{The Politics of Industrial Relations}

On the basis of the econometric evidence presented here, the majority of public sector workers in Ireland were paid more than comparable private sector workers in the early and mid 2000s. In part, this can be accounted for by differences in employees’ attributes and the characteristics of their workplaces, and by changes in the composition of the labour market, whereby a large influx of migrant workers was associated with a smaller growth in wages in certain specific private sector industries and occupations. The remaining analytical task is to examine whether and how the industrial relations and political processes associated with public sector pay determination might have influenced public sector wage settlement.

At the outset, a prima facie case might be made that public sector ‘union power’ was the reason why the benchmarking awards were so generous. The argument is that, since public sector unions are powerful actors in Irish industrial relations as measured by their high density levels\textsuperscript{33} and as derived from the key role they played in initiating and sustaining social partnership (see Baccaro and Simoni 2007), they were in a position to win generous wage increases for their members. That is, in exchange for their continued support for social partnership and for agreeing to the restoration of order to the conduct of public sector pay determination through the benchmarking process, public sector unions set a price which resulted in the payment of a significant wage premium. Such a view received considerable

\textsuperscript{32} Inter alia, we do not have complete data on unemployment rates by occupation and recent non-Irish born migrants by occupation for the period 2003 to 2007.

\textsuperscript{33} Union density is estimated to be 68.8\% in the public sector and 28.2\% in the private sector (Geary 2007).
support from critics of the benchmarking process both in the media and in academia (McManus 2003, O’Leary 2002, Ruane and Lyons 2002). These criticisms might be read to suggest that the some or all of the work of the PSBB was a charade used as a cover to mask behind-the-scenes deal-making and brokering between government and public sector unions.

Critics focused on a number of the features of the benchmarking process. First, there was the composition of the seven member Board. Apart from the Chairman and one member, all the other members of the Board were closely associated with the early development and operation of social partnership.34 One leading business columnist commented that: “The benchmarking body was above all else a creature of social partnership, the faustian pact… (T)he people who forged it became very powerful and influential figures…One can’t help feeling that something similar went on in the benchmarking process…choreographed to arrive at an outcome that has already been determined by the big players” (McManus 2002).

Second, there were criticisms of the report’s findings in regard to its terms of reference. In making its recommendations, the PSBB was enjoined first, to have regard to the need to ensure equity between employees in the public service and the private sector; second, to have regard for the need for public sector managers to recruit, retain and motivate staff; third, to ensure the ongoing modernisation, efficiency and flexibility of the public service; and finally, to underpin the country’s competitiveness and continued prosperity. These principles might seem reasonable to most observers and have provided the bases for determining pay in public services internationally, but the problem, as perceived by critics, was twofold. In the first instance, it was unclear which was the primary criterion informing the PSBB’s findings and, in turn, whether the PSBB had sufficiently considered the macro-economic implications of their recommendations. In a veiled but sublime critique of the PSBB report, John Fitzgerald (2002) speculates as to the principle rationale(s) informing the Board’s findings. He considers two possible scenarios: first, that the awards were made to restore “parity” in employee earnings in the public and private sector; and second, that they were made to set a “market rate” (i.e. to match supply and demand where there were particular skill shortages). The consequences are

34 These included: Billy Attley (a former general secretary of Ireland’s largest union, SIPTU); Phil Flynn (former general secretary of the largest public sector union, IMPACT); John Dunne (former director of the principal employers’ association, IBEC); and Paddy Mullarkey (former secretary of the Department of Finance). Jim O’Leary, an economist, resigned from the PSBB in April 2002.
seen to be very different in either scenario. In the former case, increases in public sector pay would have had little effect in improving output or service quality; they would have led to increases in taxes, raised incomes in the private sector, which would have interacted with consumer prices and led to a loss in competitiveness. By contrast, in the latter scenario, any such negative economic effects would have been minimised if wage increases were targeted at resourcing and retaining staff with scarce skills. The improved service offered by such staff would have represented a significant gain. While Fitzgerald is unable to determine, on the basis of the information available in the report, as to which rationale was primary, he suspects that the “parity case” predominated in informing its recommendations.

Third, critics were aghast that the report was not required to present any empirical evidence to validate its recommendations. The defence marshalled by the PSBB, namely that they had undertaken to protect the identity of the private sector pay comparators who had participated in their study, carried little weight with commentators and scholars.35 Since, no other reliable, disaggregated data on public and private sector earnings were available at the time, independent observers could not verify the probity of the PSBB’s analysis or and the worthiness of its recommendations, the critics remained doubtful that public sector earnings had fallen behind those of the private sector.36

Fourth, and echoing John Fitzgerald’s criticism, other critics pointed to weaknesses in the report’s findings regarding public sector employee recruitment and retention problems. The PSBB report presented evidence which suggested that, while parts of the public service did

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35 Another defence given to Eithne Fitzgerald (2002: 5), an economist and former Labour Party Minister of State, when she enquired of a senior official as to why the PSBB’s findings were excluded from designation under the Freedom of Information Act, was: “It would be undesirable in an industrial relations and pay determination context that any party should seek to look behind the published reports, reasonings and findings of the bodies”. In interviews conducted by the present authors with key informants this rationale was indeed seen to be critical. One senior union official remarked, it was “recognised that the more information you fed members, the more they would want to be the body (i.e. the PSBB)”; while another said, “I know that in practice any opportunity to pick over the bones by people dissatisfied with the outcome would have caused the whole thing to unravel”. In essence, a key reason for keeping the report confidential—although unstated publicly at the time—was to avoid legal challenge, either by judicial review or under equality legislation. See fn. 13 above.

36 Using CSO aggregate data, however, O’Leary (2002) was able to show that, between 1997 and 2002, average public sector earnings grew more or less at the same rate as employee earnings in other sectors except for construction. At the level of broad occupational groupings, too, earnings growth for administrative civil servants was not found to be out of line with comparable employee groups in the private sector. While this does not discount the possibility that public sector employees were inequitably treated prior to 1997, or that particular groups of public servants might be have been poorly paid relative to comparable private sector groups, it does raise some questions with respect to the veracity of the PSBB’s findings and methods on which they were based.
indeed encounter problems of recruitment and retention, these could not be attributed to the payment of relatively low wages. The PSBB was disarmingly candid in concluding that it was “evident … that a number of the recruitment and retention problems… point more to deficiencies in personnel analysis and strategic planning. Simply increasing pay levels cannot resolve such problems” (PSBB 2002: 56). That this criterion did not provide the PSBB with firm grounds on which to recommend pay rises was given added weight by an independent report on vacancies in the public service published some months after the PSBB finalised its report. The Expert Group on Future Skill Needs found that vacancy rates for the public sector (4%) were not significantly out of line with those of the private sector (3%) (Hughes et al. 2003). 37 And while there were high vacancy rates and difficult-to-fill positions in particular sub-sectors of the public sector (health and education), and amongst particular occupations (engineers, technicians, associate professionals), these were not necessarily the occupational groups who gained the most generous pay awards under the benchmarking process. Apart perhaps from teachers and nurses who received 13% and between 8 and 9.2% increases respectively, the others groups received relatively modest pay awards (technicians, 2.7 to 5.1% and engineers, 4.3 to 10.5%). Thus, the critics claimed that the findings and arguments of the PSBB, when placed alongside the evidence from the EGFSN study, belied the recommendation to pay increases to public sector workers on the basis of labour shortages and employee retention difficulties.

Another criticism rested with the recommendation that 75% of the pay awards be conditional “upon agreement on relevant modernisation and change”. Particular changes were not specified. The report simply stated that such matters were to be determined by management and staff at a local level. Such provision for a productivity agreement was criticised for not only being too vague, but also that the social partners had already accepted under the terms of the existing national wage agreement that “change is a requirement of a modern high-performing public service and is not, in itself, a basis for claims for improvements in pay” (PPF, 36). Change was thus seen to have been paid for already.

Finally, in the face of the emerging economic difficulties and fiscal problems which confronted the government in 2002, the opponents of benchmarking and others critics argued that the

37 In contrast to the PSBB, the EGFSN was free to publish its data, which was collected from 1,068 private sector firms and 413 public sector entities.
PSBB’s pay awards could not be afforded and should be withheld. When the PSBB was established in 2000, the Irish economy was at its peak. It was a period of phenomenal growth in productivity and employment. Unemployment had fallen close to 4% (see Table 1). However, by 2002 both the international and Irish economies had cooled considerably. Inflation in Ireland had risen to be the highest in the Euro zone. A substantial fall in government revenues was predicted, while government day-to-day spending was running close to 30% ahead of target. The fear was that rising prices would lead to higher wages across the economy and that the country would be pulled into an inflationary spiral. With a projected end-of-year government deficit of between €1 and €2 billion, many argued that the estimated gross benchmarking cost of €1.5 billion was unaffordable and should not be paid.

The six criticisms advanced by the critics of the benchmarking process raise important questions in respect of the transparency of the PSBB’s findings, as well as the considerations and methods on which they were based. Simply put, their argument is that the case for awarding pay increases to public sector employees had not been demonstrated and nor the pay awards were not affordable. Their charge that the benchmarking process was an exercise in *realpolitik* - that to gain the support of unions for the reform of public sector pay and to ensure their continued participation in social partnership, the government agreed to pay generous wage increases - must now be examined.

At the outset, we find it difficult to accept the critics’ case, at least as advanced in its extreme form, that the PSBB somehow plotted with union leaders and government to fabricate the report’s evidence. Notwithstanding the reservations in respect of the appropriateness of the research methodologies which it employed and its refusal to share its evidence, it is most likely that the PSBB’s research found real and well-founded differences in pay levels and that it then acted in good faith to correct for these differences. Certainly, in our interviews, we found no evidence to support the critics’ case. Rather any such suggestion was roundly dismissed. One very senior union officer objected, saying that to believe that this could have occurred “requires (one) to accept that a judge (i.e. the chair of the PSBB) and his hordes of consultants all conspired to fabricate the evidence.”
The question remains, however: might the politics of industrial relations have acted in ways – perhaps as anticipated in our literature review - to influence the setting of pay in the public sector? In answering this question we need also to bear in mind the issue of why the government agreed to pay the recommended awards in relatively difficult economic circumstances. We identify the following influences.

First, there was the imperative to restore order to the system of pay determination in the public sector. This was the principal motivation for both the government and the unions when they initiated the benchmarking process. One senior civil servant explained it thus: “the late 1990s was a hairy time in Irish industrial relations. There was a lot of industrial strife in the public sector, particularly with the gardaí and nurses. The primary logic (for benchmarking) was to find a rational basis for pay determination and to restore order”, and while he insisted that, “it could not be peace at any price, there was an urgency to pay the awards quickly.”

There were a number of considerations at play here for the government. There was recognition that public sector unions were powerful actors, that they were capable of bringing a lot of pressure to bear on the government and that the delivery of sensitive public services was in their members’ hands. A senior civil servant close to the process acknowledged candidly that the PSBB was an “IR body”. Putting it pithily, he said: “Look at its composition. You would have to be naïve to think otherwise”. He continued, while the reform of pay settlement had to be seen to be impartial - as determined on the basis of external comparisons with the private sector and co-ordinated in a centralised manner - there was a recognition that, “We had to find a solution to an industrial relations problem, and while one has to be fair, one could not be unfair”. This remark was intended to convey the view that the reform process did permit certain room for manoeuvre and there was the possibility of the payment of relatively generous pay awards. The then Assistant General Secretary of the ICTU was later to observe that “public service unions and the government see the (benchmarking) process as delivering significant change and rationalisation within the public services which justifies the payments being made. Whatever the merits of (the critics’) arguments the arrangement seems, for the moment at least, to have provided a solution, albeit at a price, to the perennial problem of public service relativities” (Wall 2004: 175, our emphasis).
Second, there is the influence of what we term ‘the weight of invested political capital’ in the benchmarking and social partnership process. It bears emphasis that many of the union leaders, who had committed themselves to the benchmarking process as a mechanism for restoring order to public service pay determination, had done so in the face of criticism from other more radical union members. They saw themselves as taking a large gamble which risked endangering their reputations and leadership if benchmarking failed to recommend significant pay increases. In turn, there was an incentive for the Government to work with these more moderate and co-operative union leaders who saw value in working with government officials in seeking to restore order to public service pay determination. This reciprocal incentive was well illustrated in an editorial in *The Irish Times* (2002). In making a case for what it saw as teacher unions’ “right to demand a significant increase in pay”, it argued, “A disappointing outcome for teachers would have the most serious implications. It would punish the INTO and the TUI – who invested heavily in the process – and vindicate the ASTI who did not. It would also undermine public confidence in the entire partnership process. Benchmarking must deliver.” A senior civil servant put it, albeit somewhat more obliquely, to us: “The INTO and the TUI had stayed on the reservation, albeit for not unworldly motives, but they had remained on side”.

On the government side, too, senior politicians had also come to invest a great deal of time and energy and of their reputations in the social partnership process. Arguably, Prime Minister Ahern had, more than any other political leader of his generation, identified himself politically with social partnership, and had come to stake much of his political reputation on its successes (Roche 2008). For Ahern, it was thus important that a solution to public sector pay determination would be rooted in the partnership process and that partnership in turn would be seen to deliver a successful outcome. For his colleague and Minister for Finance, Charlie McCreevy, the motivation to find a solution within social partnership may have been less pressing, given his right of centre economic views and general lukewarm view of commitments entered into under social partnership, but in steadfastly seeking the reform of public sector pay determination he was pragmatic in enjoining his officials to work with trade union representatives to find a viable solution.

38 INTO, Irish National Teachers’ Organisation; TUI, Teachers’ Union of Ireland; ASTI, Associated Secondary Teachers of Ireland.
Third, although it may not have been wholly foreseen, there was another political motivation, or at least benefit, for the government in co-operating with unions in the benchmarking process and in paying the recommended awards. As events unfolded following the publication of the report, it was the unions who were cast as the scapegoats: on the one hand, media commentators ‘blamed’ them, in large part, for extracting excessive wage increases from government; while, on the other hand, union members – at least in some unions – ‘blamed’ their leaders for conceding to government pressure to accept what they perceived as modest wage increases. In the face of such charges, one senior union officer said to us in exasperation, “we had to remind ourselves, we didn’t invent this (benchmarking)”; while another union leader bemoaned, “with members it’s just thankless. (We faced charges like…) You recommend it, you defend it. We never hear anything from management and we never hear any politician defending it”. By having to defend the PSBB’s recommendations, the unions provided the government with a convenient ‘blame-avoidance’ partner. By such means, the government was able to shift, or at least share some of, the ‘blame’ with unions for the costs associated with the benchmarking process.

Finally, we consider the possible influence of electoral politics on the payment of the benchmarking awards. The publication of the PSBB report was immediately preceded by a general election campaign. A priori, one might have assumed that, while the deteriorating fiscal climate might have inclined the government to take assertive action over the management of the public finances, including reining in public sector workers’ expectations of wage increases, any such move would have been tempered by a fear of confronting strong public service unions when a general election loomed. In our interviews with key informants we found that views differed as to the influence of the election. Union representatives believed it exercised some influence over the actions of the government, while senior civil servants felt it had little or no influence. From our reading of the press reports at the time and post-election academic commentary it is clear that benchmarking was not a central concern of the electorate (see Gallagher et al. 2003). Notwithstanding this, however, it is notable that the politics of industrial relations loomed large at the time of the election campaign. There were two notable features: on the union side, there were threats of industrial action and refusals to enter talks on a new national wage agreement if the government refused to pay the forthcoming benchmarking increases; and on the government side, there was a marked reluctance to explain
explicitly – in response to opposition parties’ questions and criticisms from critics of benchmarking – how the benchmarking payments might be afforded and justified.

Our reading, to put it prosaically, is that the government was caught between a rock and a hard place: it felt compelled to meet the raised ambitions and expectations of public sector employees, introduce a new and more orderly system of pay determination, maintain industrial peace, retain the social partners’ commitment to social partnership, win a general election, while at the same time gain greater control over the public finances. In these circumstances, the political priority was accorded to the establishment of order over the machinery of public sector pay determination while avoiding confrontation with strong unions.

**Summary and Conclusion**

In this paper, we have established that public sector employees were paid more than private sector employees in Ireland in the early and mid 2000s. A significant public sector earnings premium was found to exist, particularly in the latter period. In an attempt to explain this earnings premium we looked to the economics and industrial relations literature. With respect to the former we expected that explanations which relied on human capital theory and on differences in the types of jobs people perform in the public sector would be helpful in accounting for at least some of the identified differences in employees’ earnings, but, that on their own, these factors would be unlikely to account for the entire differential. This was found to be the case. Our econometric analysis of the 2003 and 2006 NES data showed that, after controlling for personal and job characteristics, the estimated average public sector earnings premium was between 6 to 7% in 2003 and rose to between 12 and 17% in 2006.

The task then was to see how such a significant and increased premium might be explained. We anticipated that two other influences might be important. The first related to changes in the composition of the labour market arising from a large influx of migrant workers. We found that between 2003 and 2006 the number of non-Irish born immigrant employees as well as their share of employment rose significantly, especially in the bottom two occupational groups (SOC’s 8 and 9) and in Craft and Related (Soc 5). When we looked at the growth in average earnings between 2003 and 2006 by main industry and major occupational group, we found that the growth in earnings was negatively correlated with share of recent migrants employed
in a given industry or occupation. This evidence suggests that the share of immigrants in the workforce had a significant, albeit small, negative impact on average wages, mainly in the semi/unskilled services sector. We argue that, as immigrant workers were largely concentrated in the private sector, their employment had the effect of acting as a drag on wage increases in that sector, thereby contributing to the maintenance of, and an increase in, a public sector earnings premium.

Second, there was the potential influence of the politics of the wage determination process. We considered whether it was union power which forced the government to concede generous wage increases. We find that there is something to this explanation, but that on its own it is not sufficient. In understanding the ‘power’ of public sector unions, it bears emphasis that unions were non-unitary actors. Although the predominant view amongst union leaders was that benchmarking was the preferred route for reforming and determining public sector pay, there were significant sections within individual unions that held contrary views. The presence of inter- and intra-union divisions not only created considerable risks for the champions of benchmarking within unions, but it also had an impact on the strategies of government. Thus in explaining why the government came to act as it did and in turn why public sector workers came to enjoy a pay premium over their counterparts in the private sector, we argue that it is not enough simply to point to the ‘power’ of public sector unions, at least as conceived in terms of their organizational attributes (density and cohesion). While this is undoubtedly important, the power which was derived from the interdependence of unions and government was an equally or more important factor. The government needed the co-operation of the unions to maintain industrial peace, to restore order to public sector pay determination, to secure the future of social partnership, as well as to garner support for their re-election. On the basis of these considerations, the government had to estimate the ‘limits’ of union support for benchmarking; that is, what recommendation both in respect of wage increases and the terms of their implementation might be acceptable to the greater majority of unions and union members. Arguably, it was the presence of competing factions between and within unions which increased the power resources of those union representatives who had come to champion benchmarking.39

39 We borrow here from Avdagic et al.’s (2005) conceptualisation of power as used in their study of the emergence and evolution of social pacts in Europe.
Thus we argue that ‘the weight of invested political capital’ was an important factor in accounting for the payment of the benchmarking awards. That is, the proponents and supporters of the social partnership process – under whose aegis the reform of public sector pay determination and benchmarking was established – had a lot to lose, if the recommended pay awards were not perceived to be fair and/or generous and were not agreed to by government. Here again union leaders and senior political leaders had a shared interest. The former, as indicated, had to face down significant criticism and opposition from within their ranks to the introduction of benchmarking. Rejection of the proposed pay awards would have posed a very significant risk to their reputations and status. Similarly, as social partnership had been central to Prime Minister Ahern’s modus of governance and political reputation, he too was anxious to ensure that benchmarking – and by implication social partnership – would be seen to deliver a successful outcome.

In sum, an important reason in accounting for the presence of a public sector earnings premium in the early and mid 2000s was that the awards made under benchmarking were granted by government because they had a stake in doing so. The legitimacy and public standing of government and the institutions of social partnership which it had crafted were, in its eyes, in some significant danger if the benchmarking awards were not made. The government acted in a way that was seen to be politically advantageous, rather than perhaps immediately desirable in the economic climate. By such means, the politics of industrial relations came to play a significant part in explaining the determination of public sector pay in Ireland and in accounting for the payment of the benchmarking pay awards.

In conclusion, the following remarks may be made with respect to the respective merits of the different theoretical frameworks employed for explaining the existence of a public sector earnings premium in Ireland. While standard econometric explanations, which rely on human capital theory and on differences in the types of jobs people perform in the public sector, do help to account for the presence of a public sector earnings premium in Ireland, they are not sufficient. Theoretical perspectives which give emphasis to changes in the composition of the labour market and the recruitment preferences of employers are found to be helpful. But to add to our understanding we were required to examine the interface between politics and industrial relations. In drawing both from econometrics and industrial relations, we believe this paper
offers a more comprehensive explanation for the existence of and growth in the public sector earnings premium in Ireland in the mid 2000’s than has been evident in the literature to date.

APPENDIX.
Pay Settlement under Social Partnership, 1987-2006

Since 1987, the principal mechanism for determining employees’ pay has been collective negotiations involving employer groups, unions and government under the ambit of national social partnership. To date, there have been seven such agreements and all, bar one, have involved 3-year phased agreements on permissible pay rises. Each agreement has consisted of two parallel pay accords, one for the private sector and another for the public sector. In general, the pay increases in the latter have been awarded without issue. Although union density in the private sector is considerably lower than in the public sector and there are some large non-union employers, the terms of the agreements have generally been adopted as the “wage norm” throughout the economy. A significant cohort of non-union employers, in particular US MNCs, has been willing to pay wage increases above the norm to safeguard their non-union status (Collings et al 2008; Gunnigle et al. 2007; Ch. 5). Yet other employers, although few in overall numbers, have used special ‘inability to pay’ provisions to plead they cannot afford to pay the recommended wage increases, in part or in whole.

The agreements have generally endeavoured to prevent the emergence of a second tier of bargaining and, only on two occasions, has the inclusion of a so-called local bargaining clause – within tight parameters of 2-3 % – been approved. In the early to mid 1990s, local bargaining in the public sector was permitted but again within predefined parameters. However, as documented above, pay bargaining became highly disorganised with pay ceilings being regularly exceeded on foot of disputes in essential services and the payment of “special” pay awards. In the private sector, it was not until the early 2000s at the peak of the economic boom that wage drift of a significant form began to emerge. With this coalescence of pay pressure and drift in both sectors of the economy, the government sought to move decisively to re-centralise an already highly centralised system of pay determination by introducing benchmarking in the public sector and by installing elaborate enforcement mechanisms in the
private sector. By such means, the government sought to continually reduce the scope for wage negotiations at the sector, enterprise and workplace levels and thereby set Ireland apart from other European countries where social pacts prevail but where “organised decentralisation” in pay bargaining has been the predominant pattern (Hassel 2006, Roche 2007).

Since the early 2000s, the government’s efforts to restrain wage drift in the private sector have been successful. The majority of unionised companies have generally been able to afford to meet the terms of the wage agreements – certainly up until 2008 – and the strictures attending the enforcement mechanisms would seem to have been successful in deterring unions from pursuing above the norm pay claims.

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