

Research Paper

The role of employment agencies in pay setting

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TABLE OF CONTENTS

FOREWORD	3
ACKNOWLEDGEMENTS	4
EXECUTIVE SUMMARY	5
1. INTRODUCTION	7
2. THE STRUCTURE OF THE TEMPORARY EMPLOYMENT AGENCY INDUSTRY IN THE UK	10
2.1 The evolution of the temporary employment agency industry	10
2.2 Typologies of the temporary employment agency industry in the UK	10
2.2.1 <i>Geographical span</i>	11
2.2.2 <i>Contractual relations between agencies and client firms</i>	12
2.2.3 <i>The sectoral and occupational focus of agencies</i>	14
3. A BRIEF LITERATURE REVIEW ON THE ROLE OF AGENCIES IN PAY SETTING	17
3.1 Introduction	17
3.2 The role of agencies in setting margins	17
3.3 Agency working and pay differentials	18
3.4 Who sets pay: the agency, the worker or the client firm?.....	19
4. METHODOLOGY AND RESEARCH DESIGN	21
5. RESULTS	26
5.1 Introduction	26
5.2 Client/agency relations	26
5.3 The role of agencies in pay setting	27
5.3.1 <i>The role of agencies in setting hourly pay rates</i>	27
5.3.2 <i>The role of agencies in setting margins</i>	34
5.4 The role of agencies in setting non-wage benefits	35
5.5 Temp to perm fees.....	38
5.6 Perceptions on the likely impact of the Agency Working Directive.....	38
5.7 The impact of the economic recession on the practices of employment agencies ...	39
5.8 Conclusion	40
CONCLUSIONS	41
REFERENCES	44
APPENDIX 1: INTERVIEW SCHEDULE FOR ACAS RESEARCH INTO THE ROLE OF AGENCIES IN PAY SETTING	47

FOREWORD

The Agency Workers Regulations 2010, due to come into force in October 2011, provide agency workers with the opportunity to receive similar pay and basic conditions as permanent employees in client companies where they are placed, provided they have certain minimum service levels. This raises the question of how pay is determined for agency workers and the relationship between the temporary work agency, the client company wishing to be supplied with workers from the agency, and the workers themselves. Research conducted in the last decade pointed to the complexity of these triangular relationships and the dynamic and often changing employment context where it is even sometimes in doubt who is the employer. Individual agency workers, managers of temporary work agencies and those in client companies can all be expected to want advice from time to time on the impact of the Regulations and how claims for 'equal treatment' can best be handled. The Acas Helpline is often the first port of call for such queries and staff need evidence based analysis to help answer such calls.

In 2009 Acas commissioned Chris Forde and Gary Slater to conduct a small pilot study to provide evidence and some understanding of how temporary work agencies set pay levels and, where they do not set pay, the extent to which they influence pay. This report provides a detailed account of the variety of practices and different type of contracts entered into by agencies and the indirect role of setting profit margins in influencing pay. The researchers also gathered evidence on the preparedness of the industry for the enactment of the Regulations later this year. Not all agencies are prepared for the equal treatment provisions. This implies a difficult period of adjustment. The authors sensibly urge more research as this was only a pilot study. Acas is only able to provide seed corn funding and this report shows how valuable that can be.

John Purcell, Warwick Business School

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EXECUTIVE SUMMARY

- This report examines the role played by temporary employment agencies in pay setting for agency workers.
- There are important gaps in our understanding in relation to the role played by employment agencies in pay setting issues. At a very basic level, very little research has been conducted to address the question of whether agencies do play a role in pay setting.
- The findings in this study are the outcome of a small pilot study of agencies and employers to investigate the role of agencies in pay setting. The research was funded by Acas. It research involved 25 in depth interviews, conducted between September 2009 and March 2010 within case studies of six agencies and two companies.
- Drawing on previous literature, the report sets out a number of typologies which are useful in developing an understanding of the dynamics of the temporary employment agency sector in the UK.
- These typologies reflect different key dynamics of the sector: the geographical reach of agencies, in terms of whether agencies are global, national, or regional/local in nature; the nature of contractual arrangements between agencies and client firms; and the occupational and sectoral composition of agency employment in the UK.
- There is limited direct evidence from other studies into the role of agencies in pay setting. The limited evidence available from previous studies suggests that agencies do appear to play a role in setting margins. However, in terms of hourly pay or salary rates previous literature suggests limited direct involvement of agencies. It seems likely from the literature available that the involvement of agencies in pay setting will vary according to where agencies fit in the typologies outlined above.
- The headline finding from the case studies conducted for this pilot project was that agencies had a fairly limited role to play in setting hourly wage rates for temps.
- The role of agencies in pay setting was, generally, more limited in public sector contracts compared to private sector ones.
- Agencies did tend to have more of a role in pay setting in some managed service contracts, where pay setting was sometimes more of a 'partnership' between agencies and client firms.
- Under 'neutral vendor' contracts, there was also a role for the agency in advising on hourly rates, and for benchmarking pay rates. Neutral vendors also played a role in standardising the mark ups charged by agencies for national insurance and annual leave.
- The involvement of agencies in pay setting varied across the economic cycle. Agencies appeared to have a greater role in pay setting in periods of economic growth. There was also evidence of a greater role for agencies in setting hourly rates in shortage occupations (such as skilled craft occupations) and in particular sectors where there was a tradition of agencies or individuals setting pay rates.
- The competitive strategies pursued by agencies impacted upon their involvement in

wage setting. Agencies competing on the basis of undercutting wages of permanent staff in organisations tended to play a greater role in wage setting.

- Agencies did have a greater role in setting their margins, although these were increasingly being affected by factors such as the nature of contractual relations. In hands-on contracts, client pressure often resulted in reductions in margins. In the case of neutral vendors, the 'raison d'être' for these intermediaries was to exert downward pressure on agency margins.
- In terms of non-wage benefits, all the agencies provided holiday leave, which was at least at the level required by the Working Time Directive. Additional benefits, such as sickness benefit, shift allowances, and training were offered by some agencies, with many being driven (and paid for) by the client rather than the agency.
- There is a need for more detailed evidence on the factors that shape the involvement of agencies in pay setting, to examine in more detail some of the issues raised in the report, and to explore emerging issues that have not been covered here.
- As for the likely effect of the Directive, some agencies have adapted their pay setting activities to anticipate the likely effects of the Directive (e.g. some of the larger, multinational agencies). However, other agencies (notably those that are competing on the basis of minimising wage costs and establishing clear wage differentials between temporary and permanent staff) are not currently prepared for equal treatment provisions. This suggests that the Directive would have considerable benefit in terms of its stated aims of ensuring equal treatment between temporary and permanent staff, since many agencies are not currently paying agency staff equal pay to comparable permanent employees.
- Some agencies appear to be *prepared* for the Directive (in terms of having thought about the likely implications of the Directive for their activities), but there is a difference between this and the actual implementation of equal treatment provisions.
- One possible effect of the agency working directive is that wage rates for agency workers, on average, should end up rising. If the amount per hour charged to agencies remains the same, then by extension the agency margin might be squeezed. Alternatively, if the agency margin remains the same, then the price charged to client firms will need to rise. The balance of power in pay setting between agencies and firms will determine which of these two possibilities (or a combination of adjustments to both the margin or the overall price charged to the firm) occurs in practice.
- In strong economic conditions, or where agencies have bargaining power by virtue of a long-term contract with client firms, or where agencies are supplying a niche occupation or sectoral market, then agency power to maintain their margin may be greater. The factors that determine the balance of power between employers and agencies in pay setting should form a priority for future research.

1. INTRODUCTION

This report examines the role played by temporary employment agencies in pay setting for agency workers. The potential and actual role of agencies in pay setting has been the subject of much recent debate in light of the imminent implementation of the European Agency Working Directive in the UK. An Agency Working Directive was proposed by the EU as early as 2002, but failed to progress past the Council of Ministers in 2003 (see Eurofound, 2009). Whilst supporting the notion of equal treatment for temporary workers in principle, the UK government expressed concerns over balancing the needs of the UK's flexible labour market with the provisions of the Directive (House of Commons, 2007). In May 2008, a compromise was reached between the UK business and trade union social partners (the TUC and CBI) providing for equal treatment for temps in the UK to be effective after a period of 12 weeks into assignments. A revised directive was accepted by the EU Council in June 2008. In January 2010 the Agency Workers Regulations 2010 were laid before Parliament, and are due to come into force on 1 October 2011. This followed earlier consultations (May - July 2009) on proposals for implementing on the basis of the CBI/TUC agreement; which also invited views on when the Regulations should come into effect. This in turn was followed by a Consultation Paper (October – December 2009) on draft Regulations, and which also invited views on issues to be covered in Guidance. In June 2010, the new government indicated that the implementation of the Agency Working Directive was under review:

'The Government is currently considering the issue of the Agency Workers Directive implementation. It is aware of concerns in parts of business community about some aspects of regulations laid before the Election, but will need to balance those with possible risks of reopening the package as a whole – bearing in mind basis of the Regulations on the agreement between TUC and CBI' (BIS, 2010).

The main purpose of the Agency Worker Directive (AWD) is to ensure the appropriate protection of temporary agency workers through the application of the principle of equal treatment and to address unnecessary restrictions and prohibitions on the use of agency work. The AWD follows similar directives on fixed-term and part-time work (which were based on European social partner agreements). Under the Directive 'equal treatment' relates to basic working and employment conditions of temporary agency workers (e.g. working time). The Directive does not affect the employment status of temporary workers. After 12 weeks in a given job, an agency worker will be entitled to equal treatment (at least the basic working and employment conditions that would apply to the worker concerned if s/he had been recruited directly by that undertaking to occupy the same job).

Little is known about the role played by agencies in pay setting activities, despite the potential importance of this role for economic outcomes. In some sectors and occupations, for example, agency working comprises a significant proportion of overall employment (e.g. construction, IT workers). Are agencies in these sectors able to exert greater power over pay setting? Do larger agencies, with greater geographical reach, or significant local market power, have greater influence over pay setting? What are the effects of this power in terms of pay? Under what circumstances do agencies seek to drive up or drive down wages? Do they seek to maximise wage rates, or the margin between wages and the rate paid by the client to the agency? It may also be the case

that the role of agencies in pay setting activities varies across the economic cycle. The agency industry is pro-cyclical, expanding in a strong economic climate (see Forde and Slater, 2010). Are agencies able to exert a greater role over pay setting in stronger economic conditions?

It is clear then that there remain important gaps in our understanding in relation to the role played by employment agencies in pay setting issues. At a very basic level, very little research has been conducted to address the question of whether agencies do indeed play a role in pay setting. Beyond this, there are questions about those particular *aspects* of pay setting where agencies do play a role, and those aspects where they do not. Previous research (see e.g. Forde, 2001; Purcell *et al.*, 2004; Kirkpatrick *et al.*, 2009) has highlighted the diversity of the employment agency sector in terms of: the global/regional/local span of employment agencies; the type of contractual relations being developed by employment agencies with client firms; and the occupational and sectoral distribution of agency employment. In order to gain a clearer understanding of the behaviours of agencies, there is a need for the development of clearer typologies of the employment agency sector to reflect these different dimensions. The first section of this report undertakes to identify these typologies. Subsequent discussion on the agencies' role in pay setting are then considered in relation to the typologies. Given the exploratory nature of the study, these typologies are naturally imperfect, and in many cases overlapping, but they do provide a useful heuristic device for mapping and exploring the key features of the agency industry. For example, what different forms of contractual relations are commonplace? How do 'master vendor', 'neutral vendor', 'preferred supplier' and other contractual relations operate in practice, and how do they impact upon pay setting activities?

The findings in this study are the outcome of a small pilot study of agencies and employers to investigate the role of agencies in pay setting. The research was funded by Acas and involved 25 in depth interviews, within case studies of six agencies and two companies. The research was exploratory rather than explanatory in nature, with a key aim being to highlight important issues for investigation in a larger-scale project. The empirical data were gathered between September 2009 and March 2010.

The report is organised in six chapters. Following this introduction, the structure of the temporary employment agency industry is examined in Chapter 2. We chart the evolution of the industry, and set out a number of important features of the industry which frame our subsequent empirical work. In particular as discussed earlier, we establish typologies of the temporary employment agency industry in terms of geographical reach, and contractual arrangements between agencies and client firms. We also look at the occupational and sectoral composition of agency employment in the UK.

In Chapter 3, we conduct a brief literature review into the role of agencies in pay setting. The starkest finding in this chapter is the limited number of studies that have directly examined pay setting activities of agencies in the UK context. We summarise research which looks into the role of agencies in setting margins, fees and pay, before examining the extent of pay differentials between agency staff and permanent employees in the UK. We conclude the chapter by looking at how the typologies established in Chapter 2 might impact upon pay setting activities.

In chapter 4, we set out our methodology, and provide details of the six agency and two

company case studies. Our case studies provide a good coverage of the sector in terms of the typologies identified in chapter 2. However, it is important to emphasise that the aim of the study was not to provide representative data. Rather, it was to illuminate aspects of pay setting behaviour through qualitative case studies.

In Chapter 5 we present our main findings. We begin by looking at the nature of contractual relations between agencies and client firms, before presenting overall findings on the role of agencies in setting hourly wage rates or salary rates for temps. We then move on to look at factors that shape the level of involvement of agencies in pay setting. We look at seven factors, namely: differences across the public and private sectors; differences across contract form; changes in pay setting roles over the last 10-15 years; providing workers at short notice; occupational and sectoral differences; the competitive strategies of employment agencies; and pay setting amongst agencies that 'employ' their temps directly.

We then move on to look at the role of the case study agencies in setting margins and the role of agencies in setting non-wage benefits. Finally we consider a number of other issues related to the role of agencies in pay setting, namely, temp to perm fees, perceptions on the likely impact of the Agency Working Directive, and the impact of the economic recession on employment agencies.

In Chapter 6 we draw some conclusions. The key finding from the study is that whilst temporary employment agencies appear to have a limited direct role in pay setting, the sector is very diverse. Our findings highlight how factors such as contractual relations between agencies and clients can impact directly or indirectly upon pay setting. The study also highlights wide variations in practice, both in relation to pay setting and benefits setting across different forms of agencies.

Finally, the study also highlights the need for further analysis of the role of agencies in pay setting. This is important given the imminent implementation of the Agency Working Directive. Will the role of agencies in pay setting alter significantly once the Agency Working Directive is implemented? What 'workarounds' will be developed by agencies and how will this affect their role in pay setting? The study calls for more detailed qualitative research to unpack these factors and explore variations. In addition, statistically representative evidence, perhaps from large-scale nationally representative survey data, on the role of agencies in pay setting activities would be valuable.

2. THE STRUCTURE OF THE TEMPORARY EMPLOYMENT AGENCY INDUSTRY IN THE UK

2.1 The evolution of the temporary employment agency industry

Employment intermediaries have a long history in the UK labour market. As early as the 1920s, intermediaries were hiring out workers on short-term contracts, to firms in return for the payment of a one-off fee (see Forde, 2008). However, it was only in the post World War Two period that the model of the temporary employment agency that is commonplace today in the UK was developed. In the 1950s, employment agencies began to hire out staff to firms on a temporary basis, in return for a mark-up on the workers' hourly wage (see Gonos, 1997; Forde, 2001). At this time, temporary agency work was concentrated in London, in clerical and secretarial occupations. Agencies tended to be small businesses, operating on a local or regional level, rather than on a national or international basis (Ward, 2003).

Over the last three decades, the temporary employment agency industry has experienced rapid growth. Forde *et al.* (2008) chart rises in the number of agency workers, using data from the Labour Force Survey, and find a 500 per cent rise in the number of agency workers between the mid-1980s and 2007, from 50,000 to 250,000. Agency working grew particularly strongly in the labour market recovery of the 1990s. The latest economic recession has seen a decline in the numbers of agency workers, but the most recent data shows that the numbers of agency workers began to rise again in 2009 (see Forde and Slater, 2010). By 2009, agency workers comprised just over one per cent of the employed workforce. Kersley *et al.* (2005) report that temporary agency staff are utilised in 17 per cent of all workplaces, representing no change since 1998.

2.2 Typologies of the temporary employment agency industry in the UK

The temporary employment agency sector has changed markedly over the last 20-30 years. We argue that three particular dynamics of the sector are likely to be important to developing an understanding of the role played by agencies in pay setting. These are: the geographical span of temporary employment agencies; the nature of contractual relations between employment agency businesses and client firms; and the occupations and sectors to which agencies supply temporary staff. We look at each of these dynamics below, and in chapter 3, we propose three typologies as a means of summarising the complexities of these different influences and the dynamics of the sector; and to assist in exploring the likely role of agencies in pay setting. These typologies are not intended to be comprehensive, either in terms of their coverage of all forms of agencies, nor of the issues which influence pay setting. Rather, given the exploratory nature of the study, these typologies are naturally imperfect, and in many cases overlapping. They do however, provide a useful heuristic device for mapping and exploring the key features of the agency industry. These typologies are summarised in Table 2.1.

Table 2.1 Typologies of the agency industry

Geographical span	Contractual relations between agencies and firms	Occupational and sectoral focus
Multinational National Regional/Local	Preferred supplier Sole supplier Framework agreements Neutral vendor Agency as 'employer' of agency labour Spot contracts	'Generalist' and 'specialist' agencies (specialist agencies serving individual occupations/industries)

2.2.1 Geographical span

In the 1950s and 1960s, most employment businesses tended to operate on a local or regional basis. In the 1970s and 1980s, multinational agencies became more prominent in the UK agency sector. Some of these multinational agencies had originated in the UK, and began to expand into emerging markets in other countries (Forde, 2008). By the early 2000s, the largest 20 global agencies accounted for 39 per cent of the global agency market (Coe *et al.*, 2007).

Whilst there has clearly been a rise in temporary agencies operating on a global basis, this is not to suggest that these largest agencies totally dominate the UK sector. Ward (2005) reports that the top 8 agencies in the UK account for 25 per cent of the national market. Compared to other industries, concentration ratios are relatively low, and the industry remains dispersed. Furthermore, whilst multinational agencies are clearly important in the UK, the supply of agency staff remains very local in nature (Peck *et al.*, 2002; MacKenzie and Forde, 2009). Agencies – from large global operations through to smaller local businesses – tend to recruit staff and supply to firms within a relatively narrowly defined local labour market.

Drawing on data from a range of sources on the structure of the employment agency sector in the UK (Recruitment and Employment Confederation, 2009; Coe *et al.*, 2007; Forde, 2001; Mintel, 2004) we propose the following basic typology for understanding the geographical reach of agencies:

- **Multinational agencies:** an agency which operates both in the UK and in other countries. These agencies will have multiple branches in the UK (often many hundreds of branches). A recent market research report (Keynote, 2010) lists the largest global agencies in the UK as: Allied Healthcare; Adecco; Hays; Impellam Group; Pinnacle Staffing Group; Pertemps; Best Connection; Capita Group; Kelly Services; and Morson Group. All of these have operations outside of the UK. Some of these include multiple agencies (for example Impellam includes around 20 different brands of agencies).
- **National agencies:** agencies which are based solely in the UK, with office branches at a national or regional level. These agencies have multiple branches (typically over 10).

- **Local/regional agencies:** agencies which are based solely in the UK, with office branches at a local level. These agencies usually have a single branch, although some may have multiple branches (typically less than 10).

Figures from the Recruitment and Employment Confederation show that in absolute terms, local agencies make up the majority of the sector in the UK. The most recent REC survey (REC, 2009) indicates that there were 10,000 employment businesses in the UK, operating a total of 15,000 offices. 65 per cent of these offices were single-branch companies. From our own analysis, we estimate that the largest 20 agencies in the UK operate around between 3,500 to 4,000 branches, or around 25 per cent of the branch total. This implies that a maximum of 10 per cent of branches are operated by regional/national agencies.

2.2.2 Contractual relations between agencies and client firms

A second important dynamic in the sector, with potential implications for pay setting behaviour is the nature of the contracts that exist between agencies and client firms. The starting point for much economic analysis of the agency sector is that the relationships between clients and agencies can be understood in terms of 'spot' contracts. Here, the potential buyer of agency services (the client firm) can choose between many different suppliers of agency labour (see for example Williamson, 1985). In recent years, there has been a proliferation of contractual arrangements between agencies and client firms in the UK, many of which bear little resemblance to the 'spot' contracts described above. A notable trend in the 1990s, picked up in studies of the US agency industry, was that many agencies began to develop long-term contracts with firms to supply large numbers of temps to firms on a quasi-continuous basis (Henson, 1996; Peck and Theodore, 1998).

Similar trends could also be observed in the UK. Forde (2001) in a study of temporary employment agencies in two areas of the UK found that all had at least one contract with a client firm to supply 30 or more workers. Purcell and Purcell (1999) reported contracts between a large multinational agency and client firms to supply 300 or more workers. In these large contracts, temps were often seen as 'permanent temps', undertaking core roles in the client firms where they were working (see Druker and Stanworth, 2001; Grimshaw *et al.*, 2001; Purcell *et al.*, 2004). For agencies, the continuation of these contracts was heavily dependent upon them being able to meet the company's need for an (often rapidly varying) headcount, but also, crucially, upon them supplying 'repeat' (i.e. the same) temps to firms each day (Forde, 2001). The contracts typically involved a more hands on role for the employment agency in the day to day management of temps. Many contracts involved a manager from the employment business working 'on-site' in the client firm, and in some cases the agency undertook other aspects of HR activities, such as payroll management, training, appraisal (Forde, 2001; Purcell *et al.*, 2004; Hoque *et al.*, 2008)

Over the last decade, these embedded, 'hands-on' contractual relations between agencies and client firms have expanded further (see Hoque *et al.*, 2008; Kirkpatrick *et al.*, 2009; Druker and Stanworth, 2001; Purcell *et al.*, 2004; Forde, 2001; CIPD/REC, 2009). Drawing on these sources, we propose the following basic typology of contractual forms:

- **Preferred Supplier** In preferred supplier arrangements, a client firm will utilise multiple agencies to source their temporary staffing requirements, but will develop a close relationship with one of these agencies. This lead agency will, as Kirkpatrick *et al.* (2009) note, '...get first bite at the cherry ...while others act as secondary suppliers, filling roles that the primary agency cannot fill'. For the

client firm, the potential advantage of developing a relationship with a preferred supplier is that discounted rates (i.e. a reduction in the 'multiplier rate') can often be negotiated for the supply of temps, particularly where the client firm is 'buying in bulk' and arranging for large numbers of staff to be supplied on a long term basis (see Purcell *et al.*, 2004; Kirkpatrick *et al.*, 2009). Preferred supplier arrangements also allow the client firm to specify quality standards in terms of training and qualifications (Kirkpatrick *et al.*, 2009). These arrangements are commonplace in both the public and private sector.

- **Sole Supplier** These are similar to preferred supplier arrangements, but here the client firm contracts with a single agency, and this agency has a monopoly on the supply of agency labour to the client. These are less common in practice than preferred supplier arrangements, possibly due to the risks to having a single agency sourcing all temporary labour requirements. One of the principal benefits of sole supplier agreements is that they often give client firms a larger multiplier discount.

Preferred supplier and sole supplier arrangements are often termed 'master vendor' contracts, indicating that one agency has a lead relationship with the client firm (even though that agency may contract with other agencies, in the case of preferred supplier deals) (see CIPD/REC, 2009).

- **Framework agreements** Within the public sector, interactions with temporary employment agencies increasingly take place in the context of framework agreements. A framework agreement establishes the terms governing contracts to be awarded during a given period (typically a year or two years) in particular with regard to price and quantity. A framework agreement is therefore a general term for agreements with suppliers which set out terms and conditions under which specific transactions can be made throughout the term of the agreement. Framework agreements will specify which agencies a public sector organisation can contract with. Essentially, framework agreements establish a list of 'preferred suppliers', although they do not typically place one agency in lead position over the others. Gaining access to framework agreements is seen as highly lucrative, and there is intense competition amongst agencies to be included within framework agreements. As Kirkpatrick *et al.* (2009) note, public sector firms may have some leeway in practice over using an agency which is not part of the framework agreement. However, there are strong financial and transactions costs incentives for using agencies which are in the framework agreement, since these agreements are often accompanied by discounted multiplier rates. Standardised terms and conditions may also generate efficiencies in day to day contracting between agencies and client firms.
- **Neutral vendor** Under neutral vendor arrangements, an additional 'layer' of procurement is placed between the agency and the client firm. A neutral vendor will take on responsibility for all of a company's temporary staffing needs, arranging procurement systems, negotiating with other agencies over the supply of labour to the client firm, and implementing all HR activities associated with the supply of temporary labour (CIPD/REC, 2009). Crucially, unlike master vendors, a neutral vendor does not supply agency temps itself (Kirkpatrick *et al.*, 2009). Rather, it organises, via e-procurement systems, auction processes in which other agencies compete for the business of supplying temporary staff. The term 'neutral' is used because the vendor does not initially favour one agency over another when seeking to fill vacancies for a client (however, over time, e-procurement systems may reward those agencies that are able to supply at the

best price by offering them 'first bite at the cherry' at future contracts). Neutral vendor arrangements have become particularly common within the public sector, often driven by a need to reduce spending on agency staff. Neutral vendors claim that their competitive bidding processes can drive down the margins charged by agencies. Further efficiencies may come from having a single firm organising all temporary staffing needs. Most neutral vendor arrangements operate on a 'gainsharing' basis, whereby client firms and the neutral vendor share the savings which result from the contract.

- **Vendor Managed Services** are often used as a 'catch all' term for all forms of neutral and master vendor contracts.
- **Agencies that employ their temporary staff.** A further dynamic in the sector is that a number of agencies purport to act as an employer to the temps that they hire out to third party firms. Manpower, for example, one of the largest suppliers of temporary agency labour in the UK, and globally (see Ward, 2005), markets itself as an employer of the temps that it hires out, providing holiday pay, training and a range of other benefits. As an employer of agency labour, the role of agencies in pay setting is likely to vary compared to agencies that act as a third party intermediary. However, the extent to which agencies are indeed the employer of the agency labour they hire out has been the subject of much debate and recent case law (see Davidov, 2004; Forde, 2008).
- Beyond these more formal, longer-term contractual arrangements, there are many relationships between agencies and firms can be characterised as 'spot contracts', where workers are supplied 'on demand'. These relationships still involve contractual agreements between clients and agencies (setting out terms of business, payment rates etc.), but do not typically 'lock in' agencies or firms for a particular length of time.

How common are the contractual arrangements identified above? Evidence is very patchy, perhaps because many of these contractual forms have only emerged over the last 5-10 years. Kirkpatrick *et al.* (2009) find that 39 per cent of local authorities used a neutral vendor, whilst 17 per cent had a master vendor contract. In one of the few studies to look directly at preferred supplier arrangements, Druker and Stanworth (2001), using an original survey of agencies and client firms in the UK, found that 35 per cent of agency using organisations with 200+ employees had a preferred supplier arrangement in place. For firms with less than 200 employees, the proportion of firms with a preferred supplier arrangement in place was much lower, at 17 per cent, but significant nonetheless. Forde (2001) in a study of 8 agencies in two areas of the UK found that the majority had at least one preferred or sole supplier arrangement with a client for the supply of large numbers of temps on a long-term basis.

2.2.3 The sectoral and occupational focus of agencies

A third dynamic which is likely to shape pay setting activities relates to the sectoral and occupational focus of agencies. Which sectors do agencies serve and in what occupational areas do agency temps work?

Turning first to the sectoral composition of agency employment, the use of agency labour is long-standing (see for example, Pollert, 1988) and there is broad consensus that the use of agency labour has expanded rapidly over the last two decades (see Forde and Slater, 2005). Some have argued that this rise has been driven by 'demand' factors, such as budget constraints, which have placed limits on the ability of public sector organisations to recruit permanent employees, and labour shortages in particular areas.

Other have argued that the rise in the public sector is largely 'supply' driven, with more workers in the public sector opting for agency contracts in preference to permanent employment (Kirkpatrick and Hoque, 2006, for example describe a 'retreat from bureaucracy', with some social workers choosing agency contracts due to dissatisfaction with management and bureaucracy connected with permanent roles). Recent survey evidence, summarised by Forde and Slater (2010) reveals that 25 per cent of agency workers work in the public sector.

Forde and Slater's (2010) analysis of Labour Force Survey data provides more detailed evidence on the sectoral and industrial composition of agency employment. It is important to recognise that there is much uncertainty over the overall number of temporary agency workers. BERR's (2008) report finds between 1.3 and 1.5 million agency workers in the UK, whilst LFS data reports much lower numbers of agency workers (around 250,000 workers). Here we report LFS data as it gives more detail on sectoral/occupational breakdowns. These findings are summarised in Table 2.2 below. Compared to directly employed staff on permanent contracts, in terms of occupations, agency workers are under-represented in managerial, professional and associate professional occupations (in other words, the proportion of agency workers in these three occupational groups is significantly lower than the proportion of permanent staff in these three occupational groups). Agency workers are also under-represented in these occupations compared to some other forms of temporary contract, notably fixed-term contract workers. Agency workers are heavily over-represented in clerical, semi-skilled and unskilled occupations, when compared to permanent employees. Two thirds of all agency workers are to be found in these three occupational areas, compared to only one-third of permanent employees. In terms of industries, agency workers are over-represented in manufacturing, transport and business service areas, although the industrial distribution is not markedly dissimilar to permanent employment.

Table 2.2 The occupational and industrial composition of agency employment, Labour Force Survey, 2008

	Permanent employees	Agency employees	Fixed term contracts	Seasonal/casual	Other temp workers
Occupations	proportions sum to 100%	proportions sum to 100%	proportions sum to 100%	proportions sum to 100%	proportions sum to 100%
Management	16	1	7	1	8
Professional	13	10	33	5	21
Associate professional	15	8	18	7	12
Clerical	13	25	12	10	10
Skilled	8	4	3	4	5
Sales	8	4	13	18	10
Personal	8	10	5	12	13
Semi skilled	7	15	3	4	5
Unskilled	12	24	7	39	17
Industry	proportions sum to 100%	proportions sum to 100%	proportions sum to 100%	proportions sum to 100%	proportions sum to 100%
Agriculture	1	0.4	1	2	0.4
Construction/mining/gas & water	7	6	4	3	5
Manufacturing	13	17	7	4	7
Wholesale/retail	16	7	6	20	12
Hotel & catering	4	2	1	21	6
Transport	7	9	3	4	3
Finance	5	5	2	1	2
Real estate, business services	11	21	11	7	9
Public administration	8	6	9	2	7
Education	9	9	32	10	22
Health	13	13	17	9	17
Other community	5	4	8	17	8
N (weighted)	24,016,548	236,663	598,298	388,643	163,462

Forde and Slater (2010), using Labour Force Survey data

A complicating factor in seeking to develop an understanding of the role of agencies in pay setting is that most agencies in the UK supply workers across multiple occupations and industries. Coe *et al.* (2007) make the distinction between 'generalist' and 'specialist' agencies. In the UK, the majority of agencies are 'generalist' in nature (see REC, 2009). Thus, it is not straightforward to determine the role of agencies in pay setting by making a distinction on the basis of occupation or sector, since the likelihood is that agencies are supplying a wide range of workers, across multiple sectors. In the following chapter, we use aspects of these typologies in an initial examination of the role of agencies in pay setting.

3. A BRIEF LITERATURE REVIEW ON THE ROLE OF AGENCIES IN PAY SETTING

3.1 Introduction

In this chapter, we review the existing evidence on the role of agencies in pay setting. There are very few studies to date which have directly addressed the question of the role played by agencies in relation to pay. Those studies that have examined this issue have tended to focus on the role of agencies in setting their margin levels, rather than their role in setting hourly rates for temps. We begin by looking at the role of agencies in margin setting, before moving on to look at pay differentials between agency workers and permanent employees. In the absence of direct evidence on the role of agencies in pay setting, the chapter finishes by considering how the factors examined in Chapter 2 might be expected to impact upon pay setting.

3.2 The role of agencies in setting margins

To understand the role of agencies in pay setting, it is important to distinguish between 'fee-setting' activities of agencies, and 'pay-setting' activities. Client firms are faced with an overall price for the temporary labour they take on which can be represented as:

$$P_t = P_w + P_{nw} + M$$

where t is total cost to hirer, w is wage cost, nw is non-wage cost and M is the margin gained by the agency¹.

For the agency, it might be argued that the aim is to maximise P_t and to minimise P_w and P_{nw} . By extension, this allows the agency to maximise M , the margin charged. For firms, where P_t exceeds the cost of the hourly wage and non wage costs of alternative permanent employee (or other forms of workers available), then it is likely that this is a premium the hirer is prepared to pay either to get the skills they need, or to secure the flexibility they need at short notice.

What are the implications of this for the pay setting activities of agencies? One possibility (which needs to be investigated in empirical work) is that agencies will look to set P_w at a level just high enough to secure sufficient labour supply – a hypothesis that would suggest that agencies have significant potential for driving down wage levels. An alternative hypothesis is that agencies may look to set P_w at a higher rate in order to attract 'good' temporary workers on to their books, as a means of building reputation and securing lucrative longer term contracts with client firms. A further alternative is that agencies have little role to play in setting P_w , and that client firms effectively determine P_t , P_w and P_{nw} , as a condition of contracting with them.

Historically, temporary employment agencies have exerted considerable influence over the size of their margins, (M in the equation above) (see Gonos, 1997; Forde and Slater, 2005). However, these margins are affected by a range of factors including broader economic conditions, the sectors being supplied and the nature of contractual arrangements between agencies and clients. A report conducted amidst the economic growth period of the early 2000s found that the average margin for employment agencies had declined during these years, from 22 per cent on top of the workers' hourly wage/salary in 2000 to 17.9 per cent in 2003 (Mintel, 2004). A significant factor which was exerting pressure on margins were seen to be the increasing cost of social

¹ We are grateful to Tim Harrison, at BIS, for suggesting this formula.

regulation (for example, such as the requirement to provide annual leave, and more stringent regulations on the recording of personal data) (Mintel, 2004). This increased administrative burden was said to be eating into profit margins rather than being passed on to the customer. Whilst margins recovered over subsequent years, the economic recession of the last 2 years has had a negative impact upon margin levels (REC, 2009). Further pressure on margins has come from the rise of long-term contractual arrangements between agencies and client firms (see below).

3.3 Agency working and pay differentials

Underpinning much of the interest in the role of agencies in pay setting is the hypothesis that there are differentials in pay levels between agency workers and directly employed staff, which need to be explained (see for example, BERR, 2008; Acas, 2009). It may be the case that agencies are able to attract a premium wage for agency staff, perhaps due to their specialist skills, or their flexibility (see Purcell *et al.*, 2004). An alternative possibility is that whilst agencies typically charge clients a fee in excess of the hourly wage for directly employed staff, only a portion of this is passed on to the agency worker, with the result that agency workers receive less pay than directly employed counterparts.

Table 3.1 Hourly wages by contract type and gender, UK, 2007

	All	Men	Women
A) Hourly wage (£)			
Permanent (p)	11.47	12.70	10.15
Agency (a)	7.80	7.49	8.26
Fixed term (f)	11.44	12.64	10.48
Seasonal/casual (sc)	6.42	6.86	6.06
Other temporary (o)	8.80	8.74	8.85
B) Wage difference (£s) (proportional gap between permanent and temporary in brackets)			
(p) – (a)	3.67*** (-32%)	5.22*** (-41%)	1.89*** (-19%)
(p) – (f)	0.03 (-0.3%)	0.07 (-0.6%)	-0.33 (+3%)
(p) – (sc)	5.05*** (-44%)	5.84*** (-46%)	4.09*** (-40%)
(p) – (o)	2.68*** (-23%)	3.96*** (-31%)	1.30*** (-13%)
C) Wage differentials after controlling for worker characteristics (hourly wage gap between permanent and temporary work, %)			
Agency	-10.0***	-12.4***	-5.5**
Fixed-term	-3.3**	-4.4	-2.4
Seasonal/casual	-6.9***	-2.6	-11.4***
Other temporary	-12.9***	-16.2***	-10.9***

Source: Labour Force Survey, pooled quarterly datasets Jan/March – Oct./Dec. 2007.

Notes: Wages in constant (Spring 2007) pounds; data are weighted. Panel B: significance test of difference in average wage included; Panel C: estimated by ordinary least squares regression; significance test shown is of difference of estimate from zero: * indicates significant at 10% level **significant at the 5% level *** significant at 1% level (no star signifies result is not statistically significantly different from comparator). Full results available on request from authors.

What does the evidence on pay differentials suggest? Comparable data for temporary jobs is available from Forde *et al.* (2008), using the Labour Force Survey. Table 3.1 compares the hourly pay for various forms of temporary job, including agency jobs, to permanent jobs. Panel A shows the mean hourly wage by contract type. On average, all forms of temporary job, with the exception of fixed-term contracts are paid considerably less per hour than permanent employees. The 'raw' hourly wage differential is reported in Panel B, both in pounds and as a proportion of the permanent wage. The average hourly wage gap between permanent and agency workers is £3.67 per hour (a 32 per cent differential) and this figure rises to £5.22 per hour for male agency workers (a 41 per cent differential). For female agency workers the hourly wage gap is £1.89 (a 19 per cent differential). Panel B also indicates whether the differences reported between temporary and permanent workers' average pay are statistically significant. In the case of agency workers, they are statistically significant, so a high degree of confidence can be placed on the estimated differentials.

However, it is not sufficient to focus simply on the absolute wage differentials. A proportion of the wage gap will be due to the different characteristics of agency and permanent workers, such as qualifications, age, job tenure, occupation, industry etc. Panel C reports the results of analysis that takes these variations into account (using multiple regression analysis). As expected, the size of the differential between agency jobs and permanent jobs drops (compare with Panel B), but a marked difference remains. Controlling for differences in characteristics, agency pay is 10 per cent lower per hour. For men, the gap is over 12 per cent whilst for women it is nearly 6 per cent. Overall, then, this analysis shows significant wage differentials for agency workers even after controlling for a range of factors that might explain the 'raw' differences.

3.4 Who sets pay: the agency, the worker or the client firm?

As noted above, there are very few studies that directly examine the role of agencies in pay setting. Qualitative studies of the nature of agency working tend to support the notion that the pay setting process is driven by the client firm rather than the agency, with the former largely dictating hourly rates or salary levels to the agency (i.e. P_t and P_w in the equation above) (see Kirkpatrick *et al.*, 2009; Forde *et al.*, 2001; Purcell *et al.*, 2004). These and other studies hint at the possibility of a greater role for agencies during strong economic conditions, where there might be shortages of labour. Agencies (and in some cases individual agency workers) may also have a greater role within particular occupations or sectors, where norms, industry standards, labour shortages or skill levels may provide the agency with greater bargaining power to influence wage rates (see for example Contractor UK, 2008; Institute of Interim Management, 2010).

In terms of the typologies set out in Chapter 2, these might be expected to have some impact upon the involvement of agencies in pay setting. Studies have shown that a key facet of the growth strategies of the largest agencies has centred on developing high 'added value' contracts with client firms. Within these contracts, the agency often assumes responsibility for payroll activities and the day to day management and performance of temps (see Druker and Stanworth, 2001; Purcell and Purcell, 2004) and thus it seems reasonable to expect that this might be accompanied by a greater role for the agency in pay setting activities. A recent report by the CIPD and REC, which examined the rise of master vendor, neutral vendor and other embedded relationships between agencies and clients noted, for example, that agencies are increasingly offering to provide pay benchmarking services to client firms (REC/CIPD, 2009). Studies of these embedded relations have also highlighted some correlation between formalised contracts and the provision of additional benefits by agencies to temporary staff. Preferred and sole supplier agreements, for example, may involve the agency providing workers with

some of the benefits enjoyed by permanent staff, and providing training activities (see Forde, 2001; Druker and Stanworth, 2001). Where an agency employs temps directly, we might also expect the agency to play a more central role in setting pay rates (for debate on this particular issue, see Forde, 2008).

Finally, it may be the case that unions shape the extent of involvement of agencies and client firms in pay setting. In a comprehensive study of the agency industry and collective bargaining across the EU, Arrowsmith (2009) notes that in 11 European countries, employer organisations representing the agency industry conduct collective bargaining with trade unions. These are Austria, Belgium, Germany, Denmark, Spain, Finland, France, Italy, Luxembourg, Netherlands and Sweden. In the UK, the employers association representing agencies (the Recruitment and Employment Confederation) has no mandate to bargain collectively for agency workers. Individual unions in the UK have established campaigns to draw attention to temporary work, and there is some evidence that unions are beginning to adapt their strategies to encompass agency workers, rather than exclude them (Heery, 2009). As Arrowsmith notes, the first tripartite agreement between unions, government and employers associations was in relation to the EU Agency Working Directive in June 2008.

The review above highlights the complexities and dynamics of the employment agency sector, which have implications for the role of agencies in pay setting. As noted above, there is limited direct evidence on this issue to date. Some of the ideas are tested in the case study research reported in Chapter 5.

4. METHODOLOGY AND RESEARCH DESIGN

The report sets the findings from a 'pilot' study investigating the role of agencies into pay setting. The project starting point was that there was a need for a more detailed understanding of the temporary employment agency sector, and its role in pay setting. In chapter 2, we set out a number of important dynamics of the agency sector that might impact upon the pay setting activities of agencies. These were geographical span, contractual relations between client firms and agencies, and the sectors and occupations that agencies served. The key aims of the empirical work were three fold. The first aim was to illuminate these dynamics of the temporary employment agency sector. The second aim was to explore how these dynamics impacted upon pay setting issues. A third aim was to examine the challenges faced by agencies in pay setting activities, and to identify any innovative solutions developed by agencies with regards to pay setting activities. The need to develop knowledge on all of these issues was felt to be particularly important in the context of the future implementation of the EU Agency Working Directive within the UK.

To explore these issues twenty five semi structured interviews were conducted with stakeholders in the employment agency industry. These interviews were conducted primarily within 8 case studies. Six of the case studies were temporary employment agencies and two were companies using agency workers.

A case study approach was felt to be appropriate given the exploratory nature of many of the issues under study. As Chapter 3 revealed, there has been very limited research to date on the role of agencies in pay setting. The aim of the study was not to test well established hypotheses about agency working. Rather, the aim was to try and illuminate a range of issues relating to pay setting and agencies, which could be examined in more detail in a longer, more extensive study. In selecting cases, the overarching aim was to provide coverage of as many of the dynamics of the industry identified in chapter 2 as possible. In other words, we sought to provide coverage of: local, regional/national and global agencies; a range of contractual arrangements between agencies and client firms; and agencies supplying workers in a diverse set of industries and occupations in both the public and private sectors. Whilst the cases of companies are more limited in number, the rationale for these was to provide an alternative, company based perspective on the role of agencies in pay setting. Previous research has highlighted the importance of examining different perspectives in the 'triangular' relationship that exists between agencies, client firms and workers (see Forde, 2001; Gonos, 1997). Whilst the study does not examine the worker perspective directly, it does gather evidence from the other two actors: the client firm and the temporary employment agency.

In each organisation, contact was made by email and/or telephone to a senior manager. The nature and scope of the project was explained to each participant, and a draft interview protocol was provided. In some cases, contact was established with head office representatives, whilst in other cases approaches were made at branch level. Peak level bodies were also used to facilitate access in a number of cases. Participation was, in most cases, secured on the basis that the results would be anonymised, and that individual agencies/companies would not be identified. In Tables 4.1 and 4.2, a breakdown of the sample is provided, mapped against the typologies described in Chapter 2. Precise details of the companies are not provided to maintain anonymity.

The 6 agencies comprised 2 local/regional agencies, 2 national and 2 global agencies. One of the global agencies was a neutral vendor which did not supply temporary workers itself, but contracted with other agencies. The agencies were involved in a diverse mix of contractual arrangements. All six of the agencies had developed some 'long-term' contractual arrangements with at least some of their clients. In some cases, these had been formalised as preferred supplier or sole supplier arrangements. Three of the agencies offered vendor managed services of one form or another. All of the five agencies that supplied staff themselves described themselves as generalist in nature, covering a range of sectors and occupations. Nonetheless, these agencies tended to specialise in some of these areas. The main areas of specialism are identified in the final two columns of table 4.1.

Two final points about the sample of agencies are worth mentioning as they are picked up in more detail in the results chapter. First, in common with findings from other studies (see MacKenzie and Forde, 2009), some of the agencies were large suppliers of migrant labour. Agency 4 specialised in the supply of migrant workers, almost exclusively from Poland and currently supplied over 100 staff. Agency 6 supplied over 1800 workers a week, and around half of these were economic migrants. Secondly, two of the agencies *directly employed* all or some of their temporary staff. Agency 4 was the direct employer of all 100 temporary workers, and took responsibility for paying wages, holiday pay and some other benefits. These workers were hired out to firms on a temporary basis, but were still paid by the agency if they were not working within a client firm. Agency 1 also directly employed some of its temporary workers, in some of its managed service contracts.

Table 4.2 provides details of the 2 case study companies. Company 1 is a global manufacturer with head office outside the UK. It employs 5000 workers in sales, distribution, finance, and human resources activities (but not in manufacturing, which takes place outside the UK). Of the 5000 staff in the UK, between 10-15 per cent are typically on non-regular contracts. The largest component of the non-regular workforce by far is agency workers, who comprise approximately 10 per cent of the total workforce. Company 1 contracts with a number of different employment agencies and has a preferred supplier arrangement with one of these agencies. Company 2 is a not-for-profit organisation owned by a local council in England. Company 2 has a framework agreement in place which governs relationships between the organisation and agencies.

Table 4.1 Characteristics of the agencies sampled

Case	Geographic span	Branches in UK	Contractual arrangements with clients	Sectors supplied	Main occupations covered by temps
Agency 1	National	80	Preferred supplier, sole supplier, vendor managed services	Industrial, office Public and private sectors	Clerical/secretarial Managerial Professional
Agency 2	Global	-	Neutral vendor, vendor managed services	Mostly public sector	-
Agency 3	National	Circa 20	Preferred supplier, sole supplier, other long-term contractual arrangements	Mostly private sector Construction, engineering	Trade related occupations, skilled, semi-skilled and unskilled
Agency 4	Local	1	Some long-term contracts, but no preferred supplier/sole supplier contracts Employer of all its temporary agency workers	Mostly private sector Construction, engineering, industrial, IT	Various trades Skilled, semi-skilled
Agency 5	Global	>100	Preferred supplier, sole supplier, vendor managed services	Public and private sector, Office, Catering, Industrial Construction, Manufacturing	Clerical/secretarial Managerial Professional Routine assembly
Agency 6	Regional	3	Preferred supplier, sole supplier, vendor managed services	Public and private sector, Commercial Industrial, Managerial	Clerical/secretarial Managerial Professional Routine assembly

Table 4.2 Characteristics of the companies sampled

Case	Number of employees in UK	Public/private sector	Use of agency workers
Company 1	5000	Private	10 per cent of workforce
Company 2	1100	Public	Less than 1 per cent of workforce

In each of the eight cases, interviews were conducted, where possible, with a senior manager at head office level and/or with managers in branches or establishments. In practice, for the agencies, this entailed interviews with one or more of the following: managing director, regional manager, head of operations, branch manager, recruitment consultant or contract manager. In the interviews conducted at head office level, respondents were asked about practices within individual branches as well as general company policy. In the case of companies, interviews were conducted with senior HR and/or employment relations managers.

The interviews were semi-structured in nature and gathered data on a number of key issues. In the case of agencies, the interviews covered:

- Background and contextual information
- The nature of relations with client firms, including size and number of contracts, formalisation of contracts, examples of preferred/sole supplier arrangements, master and neutral vendor arrangements
- The role of the agency in pay setting and how this was evolving
- The role of the agency in broader terms and conditions setting
- Aspects of pay setting and issues of comparability with directly employed staff
- Any other issues.

A more detailed interview schedule, with indicative themes and questions can be found in Appendix 1.

In the case of companies, the interviews covered:

- Background information
- Use of agencies, including rationales for use, changes in the use of agencies
- Nature of contractual relations with agencies
- Pay setting and the role of agencies in this process
- Equal treatment and comparability
- Any other issues.

Interviews lasted between 30 minutes and 2 hours. Some interviewees were interviewed on multiple occasions, with the additional discussions used to clarify points from the first interview, or to cover additional themes, following feedback from an interim project steering group meeting in January 2010. Where possible, interviews were recorded (with the permission of the respondent) and transcribed. In around half the interviews, however, this was not possible, and notes were made by the interviewee during and immediately after the interview. Interview data were analysed, and key themes were identified. These were supplemented with background data, gathered from publicly available sources. Initial themes and findings were discussed with the project steering group at a meeting in January 2010.

In examining issues around pay setting, a number of respondents were concerned about the sensitivity of the issues being raised. The research team assured the respondents of confidentiality. Thus, the findings below exclude any details that would allow the identification of individual agencies or companies.

5. RESULTS

5.1 Introduction

In this chapter we set out the main findings from the empirical work. We begin by looking at the nature of contractual relations between agencies and client firms, before presenting overall findings on the role of agencies in setting hourly wage rates or salary rates for temps. We then move on to look at factors that shape the level of involvement of agencies in pay setting. We look at seven factors, namely: differences across the public and private sectors; differences across contract form; changes in pay setting roles over the last 10-15 years; providing workers at short notice; occupational and sectoral differences; the competitive strategies of employment agencies; and pay setting amongst agencies that 'employ' their temps directly.

We then move on to look at the role of the case study agencies in setting margins, defined as the difference between the total amount paid per hour by the client firm, and the sum of wage and non wage costs to the agency per hour. Finally we consider a number of other issues related to the role of agencies in pay setting, namely: temp to perm fees; perceptions on the likely impact of the Agency Working Directive; and the impact of the economic recession on employment agencies.

5.2 Client/agency relations

All six of the agencies interviewed for this study had developed 'long-term' contractual arrangements with client firms for the supply of temporary workers on a quasi-permanent basis. For five of the agencies, formal contractual arrangements for the supply of temporary staff formed a central part of the agencies' competitive strategies, evidenced through the development of master vendor, neutral vendor, vendor managed services, preferred supplier or sole supplier arrangements. For a sixth agency (Agency 4), a relatively small local agency, long-term relations with clients for the regular supply of temps were very important, but the agency had not formalised these in terms of preferred/sole supplier status.

Most of the agencies interviewed agreed that the move to deeper, longer-term contractual relations with clients was one of the key strategic developments that had shaped the industry over the last decade. Furthermore, there was a perception amongst the majority of the interviewees that such managed contracts were a potentially lucrative part of their business, since these contracts allowed for the development of 'added-value' services, such as the provision of HR and training services. This was one reason why agencies had actively sought to develop and win these contracts. The certainty of a regular contract (often six months, twelve months or longer) with a client, involving the supply of a large number of workers was another key reason why these contracts were increasingly being developed and promoted to clients by agencies:

'Managed services are definitely the big growth area.....there were some of these 10 years ago, but it was only your big players who were doing them. What's changed is that most agencies will now try and take some of this market....it's a massive area' (Manager, Agency 5)

'We're providing temps, but we're also doing a lot more...we can manage payroll, we can do basic training, and we can manage everything on site if needs be' (Manager, Agency 1)

'We give the client a single point of contact for all their temporary staffing needs...it takes the hassle away from them, and we work with all the agencies for them' (Manager, Agency 2)

Both of the companies interviewed for the project also had developed long-term formalised contractual relations with client firms. Company 1 had a preferred supplier arrangement with one agency, but also worked with a number of other agencies outside of this arrangement. Company 2 had a framework agreement in place which lasted for three years. As part of this framework agreement, Company 2 had developed long-standing contractual arrangements with three employment agencies, which set out standard terms of business, pay rates and margin levels. Whilst Company 2 could and did utilise other employment agencies, they currently tended to use those agencies in the agreement. The margins charged by the agencies to the organisation were lower than normal terms of business.

Vendor managed solutions involved the greatest amount of involvement by the agency in the day to day management of contracts. In most vendor managed contracts, the agency assumed total responsibility for all aspects of the contract, including supervision, training, and, as shall be seen below, payroll issues. In preferred and sole supplier agreements, some on-site management by agency staff was also commonplace. Neutral vendor contracts were very different. As a 'layer' above agencies, and beneath the client, the neutral vendor (Agency 2) did not supply temps itself. Thus, the agency had no involvement in the day to day management and supervision of temps. The main role of the neutral vendor was in the management of the procurement process, although as we will discuss below, it did have some involvement in issues relating to pay.

The agencies interviewed contracted with a diverse range of clients. Three of the four national and global agencies interviewed (Agencies 1, 3 and 5) had a large national network of branches, in one case involving over 100 branches across the UK. These branches supplied anywhere between 50 to over 1000 temporary staff per week, with some individual contracts with a single employer running to 500 or more staff. All of them supplied both the public and private sector. In the case of the two local/regional agencies, there was considerable difference between the size of the operations. Agency 4 supplied around 100 temporary staff weekly, mostly in the private sector. Agency 6 supplied 1800 staff to around 170 firms, making an average of 10 temps per client. The neutral vendor did not operate a high street branch network, since it was not itself seeking to recruit and supply temporary staff. It worked with both public and private sector firms, although its largest contracts were with public sector bodies.

5.3 The role of agencies in pay setting

Before examining the role of agencies in pay setting, it is worth reiterating the basic distinction between the margin charged by agencies and the wage received by temporary workers. As set out above, an agency fee typically comprises three elements: the hourly wage rate for the temp; contributions for national insurance and holiday pay and any other benefits; and the agency mark-up or margin. We begin by looking at the role of agencies in setting hourly pay rates for temps, before moving on to look at the role of agencies in setting margins.

5.3.1 The role of agencies in setting hourly pay rates

In general, the agencies interviewed suggested that agencies had a limited role to play in pay setting. Rather, the process was client-led:

*'the client comes to us with a figure and says we need someone at this rate'
(Agency 5)*

*'they will say, right, we want 20 at the minimum wage or just above or
whatever the rate is and then we will just respond to that' (Agency 6)*

In many cases, there was a range within which agencies were able to work to find a suitable applicant. For Company 2, a public sector organisation, agency staff were recruited to a particular grade on the council's nationally agreed salary scales. Within this grade, there were a number of specific salary points. An agency was typically contracted to find a person at a suitable grade, but there was recognition that it was not always possible to identify a particular salary spine point in advance, and that in this sense, the agency had some (limited) discretion:

*'They might come back and say we can't find one at this rate, what about
this....but it isn't really them coming to us at the outset and suggesting it'
(Company 1)*

The main exception to this relatively limited role in hourly pay setting was Agency 4. As discussed below, Agency 4 employed its temps directly, and hired them out to user firms on a subcontract basis. The business model adopted by Agency 4 was centred around offering staff at an hourly wage rate below that of comparable workers employed directly within client firms. This involved the manager of Agency 4 actively setting rates below those offered to permanent staff (although the hourly rates and benefits offered to temps were still typically above those paid for comparable work in Poland – the home country of many of these workers). The process followed by the agency was as follows. First, the agency would inform the client of the rate it would charge and what this would cover, as well as the rate that the agency would pay the employee. Secondly, the agency would discuss how the worker would be managed by the firm and set out any mentoring role that the agency would play. Thirdly, the agency would then supply one of its employees on a long-term basis, if a skills match was available, or would seek to find a suitable worker using networks and agencies in Poland.

Below, we seek to unpack this headline finding about the limited role of agencies in pay setting by examining particular factors which shape their involvement in pay setting in more detail.

a) Public and private sector differences

In general, the supply of temps to public sector organisations involved a more limited role for the agency in pay setting than in the private sector. Public sector organisations increasingly used framework agreements, typically determined by local authorities, which specified in advance terms and conditions of business. Agencies recognised that these framework agreements constrained their role in setting hourly pay rates, and that these agreements also often involved a reduction in their standard margin rates:

*'there's little room for manoeuvre with some of these (public sector)
organisations.....everything gets squeezed....but you can get on board for a
long time which is good for us' (Manager, Agency 1).*

b) Differences across contract forms

The role of agencies in pay setting also varied depending upon the type of contract in place. Longer term contractual arrangements offered agencies a potentially greater role in pay setting. Vendor managed service contracts typically provided agencies with a

direct role in pay setting. At Agency 1, for example, a number of vendor managed contracts involved the agency transferring staff away from being employed by the client, to being employed directly by the agency. The agency then took on responsibility for all payment issues for the temps. Typically, this involved workers being paid a similar hourly wage rate to that which they had in employment in the client firm. However, often, add on benefits were less than those they enjoyed in direct employment in the client firm. In most cases, however, the benefits received by the temps directly employed by the agency were greater than those received through other agencies. Hence a key advantage of these contracts for firms, was flexibility rather than cost: the temporary workers were often not included in headcount figures, which allowed the company to expand through the use of temps, whilst still meeting corporate headcount targets.

Under preferred supplier and sole supplier arrangements, and framework agreements within the public sector, there was a more limited role for the agency in pay setting of the hourly rate. On site management activities, and the 'added value' services offered by agencies under preferred supplier and sole supplier arrangements did mean that the agency typically organised all payroll activities for temporary workers. The long-term nature of these contracts often meant that over time, the agency took on more of a role in pay setting, working alongside HR managers in the client firm to agree hourly rates. This was particularly the case where agencies had a manager or managers on site within the client firm, managing the day to day contract:

'it becomes more of a partnership...definitely.....we can advise on pay rates....if we're supplying 200 workers we're responsible for more workers than the client so we are going to be involved' (Account manager, Agency 5)

The nature of this relationship can be seen in the example of Company 1, where there were clear cost and strategic rationales for using agency staff. 10 per cent of the 5000 strong workforce were agency workers. The use of agency staff allowed the company to quickly vary numbers to meet changes in demand. Crucially, the use of agency staff also allowed the company to vary numbers of staff whilst simultaneously meeting strict headcount targets imposed by Head Office which placed upper limits each year on the number of directly employed workers that the company can use (but no limits are placed on the number of agency workers). Over the last decade, the company had evolved a strategy which relied on the heavy use of agency temps to allow them to flex numbers without overshooting head office direct employment staffing targets. Similar strategies have been revealed in other case studies of employers' use of agency staff in the UK (see Grimshaw *et al.*, 2001; Purcell, Purcell and Tailby, 2004). Most of the agency temps at Company 1 had long tenure levels at the company (typically more than a year), with some agency temps acquiring tenure levels of 10 years or more. Most were employed on core tasks.

The company made a relatively arbitrary distinction between 'temp temps' (who were seen as disposable by the company, and who are typically on contracts of less than a year) and 'perm temps' (on contracts of a year or more). The responsibility of the agency centred on arranging pay for the temps, which was below the level of that for permanently employed staff, and on implementing benefits for these temps. Given the long tenure levels of many temps, this required a long-term contractual relationship to be developed with an agency. The company had a preferred supplier agreement with one agency, and also used a number of other agencies to provide temps in specialist roles. 'Perm temps', who formed the majority of the agency workforce in Company 1 received some but not all of the fringe benefits enjoyed by permanent staff.

In neutral vendor contracts the role of the agency in pay setting was quite different. Positioning itself between the agency and the client, the role of the neutral vendor was to put temporary vacancies out for agencies to bid for. Interviewees emphasised the meaning of the term 'neutral' in the context of a neutral vendor:

'We don't prefer one agency over another...our systems select agencies objectively on three criteria: price, value and quality' (Manager, Agency 2)

The e-procurement system used by Agency 2 ensured that those agencies that met these criteria most effectively would be placed first in the queue for future vacancies that needed to be filled. The hourly rate to be charged was determined by the client. However, as contracts developed over the long-term, Agency 2 was able to advise on wage rates, and this was offered as a standard part of its service. Indeed, prior to acting as a neutral vendor for clients, Agency 2 typically undertook audits of organisations' use of temporary agency labour. These audits involved an analysis of pay rates and charge rate data from all of the different suppliers used. These were then benchmarked against Agency 2's procured industry rates. Data were then further analysed to examine spend per supplier, reliance on specific suppliers, total spend on temporary labour by skill set, and average supplier margin by temporary skill set. These processes were then reviewed to highlight potential efficiency gains and both direct and indirect cost savings. These savings were typically in areas such as: vendor procurement and performance management, time sheeting, and invoicing. Crucially, the agency did not play a direct role in pay setting, rather, this was an advisory role.

One area where the neutral vendor did have a role in broader terms and conditions setting was in seeking to standardise agency charge rates for national insurance contributions and holiday pay. The perception of Agency 2 was that agencies often overcharged a client for these, adding a standard percentage above the hourly wage which more than covered the employer's NI contribution and to meet the requirements of the Working Time Directive. Agency 2 reduced this percentage charge by insisting on a standard charge to cover these elements.

c) Changes in the pay setting role over the last 10-15 years

Respondents were asked not just about their current role in pay setting, but also how this had evolved over time. Reflections from respondents suggested that during periods of economic growth, the role of agencies in pay setting activities tended to be greater. The agency industry is highly pro-cyclical, with the number of temps supplied and turnover in the industry increasing during strong economic times. During strong economic conditions, there was often a shortage of workers, which meant that a number of agencies had been able to direct clients much more on pay rates. During the economic recession of the last two years, their role in pay setting had been much more limited:

'if you go back 6 years ago, you know we had a lot to do with pay and very often that was us advising people....the biggest problem was availability.... with unemployment being quite low we were literally spending £225,000 a year on local paper adverts just trying to drum people up, and we could dictate rates to clients.. Rising unemployment and the accession of the Eastern European states means that the labour availability just isn't an issue now. We don't do so much pushing of rates now...' (Manager, Agency 6)

'Yes what seems to be happening nowadays is they don't even talk about the pay rate. They just say if you want my business it has got to be XX or if you

want to keep the business it has got to be XX. Just look at the invoice rate'
(Manager, Agency 5)

For agencies providing low-skilled staff, legislation introduced over the last 10-15 years had also impacted upon pay setting activities. One agency manager noted that in the early 1990s, his company had played a greater role in pay setting on contracts for the supply of low skilled manufacturing workers. The introduction of the National Minimum Wage had meant that there was less discretion over pay setting for the agency at the lower end of the labour market:

'...you had the minimum wage introduced....and that has gone up quite significantly...basically more and more businesses now are just on a minimum wage it has sort of taken the science out of it...its just a standard rate' (Manager, Agency 6)

d) Providing workers at short notice

Providing workers at short notice was another occasion on which agencies might have more scope to set the pay rate. A number of the agencies were able to charge a premium rate (some of which was added on to the worker's hourly rate, and some of which was added on to the margin) when they were asked to supply workers at very short notice. In many of the long term contracts, particularly preferred supplier and sole supplier arrangements, the agency was expected to meet the client's staffing requirements at very short notice (e.g. one agency gave an example of a request for workers made at 10pm in the evening for employment at 9am, the next day). In preferred supplier arrangements, this often resulted in a complex set of relations and margin/hourly rate arrangements between the firm, lead agency and lower tier agencies:

' we would negotiate with another agency if we couldn't supply what we needed because we have massive peaks and troughs in seasonal work.... so some times we would need 200 people at short notice....and we wouldn't be able to fill them all so we would go to a secondary agency and we would give them a percentage..... we wouldn't gain anything from having those agency people working through us because the second agency would get paid for it but what we would get would be client satisfaction' (Manager, Agency 5)

e) Occupational and industrial differences

The occupations and industries supplied by the agency also had a big impact upon the role of agencies in pay setting. All five of the agencies that supplied temps were generalist agencies, which supplied workers across a range of areas. There were some occupational areas where they had had a large role in pay setting, although many of these were also limited to particular time periods, during periods of economic growth, or where there was a shortage of particular groups of workers. During the late 1990s and early 2000s, for example, a number of agencies identified a shortage in IT workers, which had meant that they could charge a premium wage rate and margin for such workers. Highly skilled interim managers were also able to command a premium wage. For both these groups, wage rates had, at various points over the last decade, exceeded those of comparable permanent employees, and agencies had played a direct role in helping to establish such differentials.

Another factor which shaped the involvement of agencies in pay setting was whether agency workers were working as self-employed contractors. Agency 3 provided a lot of workers within the construction industry, and noted that involvement in pay setting was greater in cases where agency workers were operating as self-employed contractors:

'in construction trades it's all about the contract form..it's quite different to other sectors. Where your worker is self-employed, the agency can sometimes lead more on pay...it varies from place to place' (Manager, Agency 3)

A number of public sector occupations had also commanded premium wage rates at times over the last decade, such as agency nurses and locum doctors. The nature of agency contracts with public sector organisations had changed dramatically over recent years, however, and, as mentioned above, framework agreements within the public sector generally meant that the process was now led by the client rather than the agency. However, there were circumstances in which a specialist agency worker (for example, certain locum doctors or specialist educational consultants) could command a premium rate.

In the current economic climate, one area where workers remained in short supply was in skilled craft occupations. Agency 4 specialised in providing skilled craft workers from Poland, and played an active role in establishing 'preferential' rates of pay for such workers (electricians, plumbers etc). The manager had a detailed knowledge of local wage rates for occupations and industries. He actively canvassed local employers, providing details of the wage rates he charged:

'Of course we set the wage rates....I benchmark all the occupations I supply in.....the rates are lower than what the companies pay their own staff but they're considerably more than other agencies or what the worker would get in Poland' (Manager, Agency 4)

Overall, then, there appeared to be some correlation between skill levels and the amount of influence an agency had over pay setting. For higher skilled jobs, there did appear to be more of a potential role for agencies, albeit only at particular points in time, or in particular sectors. As set out above, for low skilled jobs around the minimum wage, whilst historically agencies had played a role in pay setting, now there was little discretion, according to some respondents.

'I think there used to be more of a differential (between agency workers and permanent staff) and you know I used to go in and advise companies because very often they were getting supply problems or retention problems and I'd say well let's have a look at what you are paying your own people and lets see what you are paying the (other) agencies...and they'd end up with agency workers being paid £1.50, £2.00, £2.50 an hour less than their own people... I think because minimum wage has gone up...rates have become more standardised' (Manager, Agency 6)

'I think it come downs to an individual basis...if you have an individual who has the skills but won't take the pay then there will be negotiation...but generally it is very much driven by the client you know the agency has pretty much no say in what pay you can give' (Manager, Agency 5)

f) Competitive strategies of agencies

The model of business being used by agencies also had a clear impact upon their pay setting activities. One of the agencies interviewed explicitly stated that it gained its competitive advantage by providing temps who were paid less per hour than permanently employed staff, and one of the employers interviewed also used agencies for this reason. Agency 4, which specialised in recruiting workers from Poland, claimed it was able to undercut wage rates offered by local firms to permanent staff, whilst still

offering agency workers a wage rate that was higher than that available through other agencies. It is important to note that it was the company's reliance on Polish migrant workers that allowed it to compete on this basis, since the hourly rate available was seen by economic migrants as favourable compared to rates available for similar work in Poland (either in permanently employed jobs or through agencies). The company also emphasised the strong work ethic of the migrants it supplied, and this was also a key feature of its business strategy, a finding in line with other studies (see McKay, 2009; MacKenzie and Forde, 2009).

For company 1, one of the key rationales for using agency staff was to make cost savings, and this resulted in a clear differential between agency and permanent staff in terms of hourly pay rates. However, in this case, the differential appeared to be driven more by the company rather than the agency. As with the strategy employed by agency 4, agency temps were offered rates which were higher than those available through other local competitor agencies, but was still able to maintain a differential with permanently employed staff:

'the pay element is an issue, we are really good at giving benefits to employees, permanent, temporary, agency whatever we are really good at doing it but we are not very good at pay.... I mean we pay really well as a Company and yet we don't pay our agency very well. But compared to other agencies they do very well ...to get a temporary job in (Company 1) is quite sought after' (Manager, Company 1)

The heavy use of migrant labour by agencies had also had an impact upon the pay setting activities of agencies. An account manager at Agency 5 noted how the increasing reliance on migrant labour by local competitor agencies had forced their agency (a large global agency) to adapt their temporary staffing strategies. The agency now utilised significant proportions of migrant workers on many of its largest contracts. For the agency, this had allowed it to continue to market its managed contract services as a high value added product. The company had been able to reduce the headline margin figure it charged to firms, whilst simultaneously lowering some wage rates through the use of migrants. This had allowed it to maintain its overall mark up on lucrative managed contracts.

The project did not directly examine umbrella companies or companies operating very wide ranging travel dispensations under the mobile workers tax relief scheme. However, case agencies did note how the practices of competitor firms, particularly those operating umbrella companies, had impacted upon their own strategies. Umbrella companies employed temporary workers themselves, and, since the temporary workers were contracted to work in another location, certain expenses (such as travel, subsistence and accommodation) could be claimed before taxes are applied. This, according to one of the agency managers, placed these umbrella companies at a considerable advantage in terms of pay setting and securing business from client firms:

'I've seen (a rival) payslip and this particular person they have earned £480 for a week's work and what has actually happened is that through expenses they have put expenses through as £94.6, for travel to work and meal allowances which brings the taxable pay down to £299.00 from £425.00 and then the agency has pocketed the savings on employers national insurance which is about £20.58...and they have charged the worker £32.21 processing fee, they won't call it a processing fee they will call it a membership fee. ...the agency's benefitting by £52.79 so it can charge the client a lower rate and still come out on top' (Manager, Agency 6)

'Someone comes along and says how much do you pay and you know we say £7.70 and (the rival umbrella company) say "well we could do it for £7.20 saving you X" and then what happens is the client comes back and says "well we like your service but you are very expensive". You know you have either got to sort of lose the business or try and make the price but because we haven't got that leeway that the umbrella company has' (Manager, Agency 6)

There are clear regulations governing the activities of umbrella companies, and the circumstances in which they can deduct allowances for travel and subsistence and accommodation. Most importantly, expenses must be incurred wholly, necessarily and exclusively in the performance of services in order to be allowable. Agency 6 was the only agency in the case studies to raise the issue of umbrella companies, although it the activities of umbrella companies have been widely debated at a policy making level, and within the agency industry (see for example, REC, 2008). The evidence above suggests some abuse of these regulations by competitors of the case study companies. The activities of umbrella companies might be an issue for further investigation in a larger scale project.

g) Agencies employing temporary workers

The final factor that impacted upon wage setting was whether the agency workers were employed by the agency. Two of the agencies employed some (Agency 1) or all (Agency 4) of their temps directly. Thus, as an employer, it could be argued that these two agencies had total responsibility for pay setting. In the case of Agency 4, the agency paid all employee tax deductions, national insurance contributions, holiday pay and sickness benefit. The client firm simply paid an hourly rate, including a margin. In both cases, however, pay setting was undertaken using the reference point of comparable wage rates within the client firm. In Agency 1, hourly wage rates for temps employed by the agency on managed service contracts were often identical to those they enjoyed when employed directly by the client firm. Whilst agency 4 did appear to have more discretion over pay setting, again, wages were set in relation to those in the client firm – in this case the agency sought to undercut these wages. This strategy, of paying hourly rates below those of permanently employed workers, but above those charged by other local agencies, was used to secure contracts with local firms, and to attract workers onto the books of agencies.

5.3.2 The role of agencies in setting margins

The discussion to date has focused largely on the role of agencies in setting hourly pay rates. In terms of the margin above the hourly wage rate there appeared to be a much greater role for agencies. All of the five agencies that supplied agency workers had notions of their 'standard' mark up, which ranged from a few per cent, to a premium of up to 50 per cent above the hourly wage. Fee rates varied according to the skill level of the temp, the nature of the contract between the client and the agency, and the involvement of the agency in the contract. High value added contracts, where the agency offered a 'managed service' were typically associated with higher margins:

'we can charge a higher rate as we're providing more than just the temporary worker...its a full service model...all singing all dancing' (Manager, Agency 5)

'I'm doing more than most agencies...I do the CRB checks, I get references which look at trustworthiness, reliability, timekeeping, I get all qualification certificates translated into English equivalents and sometimes I do English language tests...this is reflected in the price and my margin' (Manager, Agency 4)

Even in the case of margins, which were seen by most agency respondents to be the prerogative of the agency to set, there was increasing pressure from clients for reduction in these. These pressures had increased with the rise of formalised contracts, particularly those in the public sector. Where client firms were 'buying in bulk' and contracting for the supply of large numbers of agency workers, there was an expectation that margins would be lowered. This was particularly noticeable at contract renewal periods, for example at the renegotiation stage of a framework agreement in the public sector:

'they will say...what can you do for us, can you reduce the margin a bit more'
(Manager, Agency 1)

'the margins on these (preferred supplier) contracts are so small...they've been trimmed to the bare minimum, that's the downside of them' (Manager, Agency 5)

The activities of the neutral vendor are particularly interesting in this respect. Agency 2 noted that it was the 'raison d'être' for the neutral vendor to push down margins. As part of their contracts with client firms, the neutral vendor guaranteed the charging of lower margins by agencies that it contracted with. The e-procurement systems used by the neutral vendor ensured that this happened in practice, since the competitive process of bidding to supply workers to the client firm rewarded those who could supply at the best price. Given that the wage rate was determined by the client firm, the only other variable that bidding agencies could adjust was their margin. Since future opportunities to bid were given first to those agencies that had successfully bid before, the presence of the neutral vendor exerted a clear downward pressure on margins, sometimes reducing average margins by up to fifty per cent of their original levels. Most neutral vendors (including Agency 2) operated gainsharing models, whereby the savings generated by the neutral vendor process were shared between the client firm and the neutral vendor. Agency 2 also advised companies on the margins being charged, and benchmarked margins of competitor agencies.

5.4 The role of agencies in setting non-wage benefits

Beyond wage rate setting, agencies did appear to have an important role to play in the provision of other benefits, such as holiday pay. However, the exact roles of the agency and the client firm in this respect were often difficult to disentangle. Many of the agencies had included provisions for holiday pay, whilst others included shift allowances, and training provisions. In the case of some of these, such as provision of holiday pay, the agency role was largely limited to compliance with the requirements of the Working Time Directive. In the case of other benefits, their role was more complex. In some cases, agencies provided a sub-set of the benefits offered by client firms, with the mix of benefits often being driven by the client firm rather than the agency. Agencies, in practice, offered different benefits to temps dependent upon the client they were working with (for example at Agency 5). In the case of some contracts between agencies and firms, a key reason for using agencies was that temps would be offered a much more limited range of benefits than those available to comparable permanent employees. In other cases, agencies offered benefits that were different to those offered to permanent employees. In this section, we look at the provision of benefits by agencies in more detail, and outline some of the innovative solutions adopted by agencies towards providing benefits to temporary workers.

Taking holiday pay, agency workers are entitled to holiday leave as part of the provisions of the Working Time Directive. Implementing this entitlement has proved challenging for many agencies, given the frequent gaps between assignments for many agency temps,

and the reality that many agency temps work for multiple agencies. The majority of agencies interviewed for this study charged an additional amount on top of the hourly wage rate to cover holiday pay. For most agencies this had, since the implementation of the Working Time Directive, been set at 9.2 per cent, on the basis that this was equivalent to providing – pro rata - 20 days of paid holiday for a full-time employee, the minimum leave entitlement initially set out in the Working Time Directive. (It should be noted that these leave entitlements have subsequently increased.) This standard rate, paid for each actual hour worked by the temp, overcame any potential difficulties with calculating gaps between assignment. There was relatively little variation between the agencies with regard to this rate, and the 9.2 per cent mark up to cover leave had (until recent changes to leave entitlement) become almost an industry ‘standard’ approach to dealing with the provisions of the Working Time Directive. One of the agencies that employed its temporary workers directly did offer a greater amount of annual leave, beyond the minimum of 20 days initially stipulated in the Working Time Directive (pro rata). Agency 4 offered temporary workers 28 days paid holiday per year, and also offered sickness benefit, as an employer of its staff, and this was not provided as a percentage on top of the hourly wage. For the agency, whilst these benefits added to the cost charged to the client for using agency labour, the agency was still able to supply temps at a price below that charged by the client firm for using permanent staff. The premium benefits offered by the agency allowed them to attract what they perceived to be high quality, reliable workers, mostly from Poland (see MacKenzie and Forde, 2009, for a discussion of the rhetoric of the ‘good’ worker, in relation to migrant labour).

Other benefits were also available at some agencies, although the role of the agency in setting the level of these services was often minimal. One example of additional benefits was allowances for shift working. These were offered by some agencies, but not to all their temporary workers. Rather, these allowances were attached to particular contracts with clients. Agency 5, for example, provided shift allowances of 15 per cent above the hourly wage rate on one of its contracts supplying production workers. This was seen as compensation for the shift working associated with this contract, and was driven, in this case, by the client firm. However, this was not a standard rate offered to Agency 5’s temps working on shifts with other clients. Indeed, in many cases, the use of temps by clients was undertaken because the agency could provide flexible workers, able to work unsocial or hours or on difficult to fill shifts, without the need to pay an expensive shift allowance.

The case study agencies did play a role in providing training for temporary staff, and there were marked differences between agencies in their approach towards training. Two of the agencies (Agency 1 and Agency 5) had bespoke training systems offered to all their temporary workers, covering areas such as IT skills and CV writing. In both these agencies, occupation and industry specific training was also provided where appropriate. Both these agencies had a long-established position in the employment agency sector, and had sought to gain market share and competitive advantage through the provision of training for temps. Beyond this, specific training was provided to temporary workers to meet the needs of clients on particular contracts. In other words, as with some of the additional benefits outlined above, this additional training was driven (and mostly paid for, in terms of the margin charged by the agency) by the client. This additional training was particularly a feature of larger contracts, particularly managed service contracts. Agency 1, for example, had a number of managed service contracts with client firms and provided a tailored induction programme for any temp who was going to work on one of these contracts. These programmes were developed jointly between the agency and the client firms.

The two case study companies also provided insights into the provision of benefits and training by agencies. In general terms, benefits were less generous for agency temps than for staff directly employed by both companies. In Company 2, 'permanent temporary' workers (those who had been working through an agency with the company for a long period) were entitled to broadly similar levels of benefits to permanent staff, including leave and payment for maternity leave. But they were not included in some company schemes such as the company car ownership scheme. Supporting the findings from the agency case studies, this differential was driven by the firm, and administered by the employment agency:

'it is managed through the agency so we tell the agency what an employee would get and they would give them those things and we would pay for that'
(Manager, Company 1)

In Company 2, an allowance to cover leave was included in the rates provided to employment agencies. Fees charged by agencies on the framework agreement included a nine per cent to cover leave, and leave arrangements were administered by the employment agency.

As for training, in Company 1, agency workers received minimal training, even if they were a 'permanent temp', with long tenure at the company. This strategy stood in stark contrast to the strategy towards training adopted for permanent staff, as explained by the employee relations manager:

'We have a massive budget for training generally for the whole company. We are very into training, but yes you wouldn't get (access to this) if you were a temp...you wouldn't get on to those training courses...you would get on the job training and that would be it' (Manager, Company 1)

At Company 2 agency workers were generally expected to have the necessary skills on arrival in the company. Training provision was concentrated on full-time and part-time directly employed staff. Training would be provided to agency staff to meet health and safety and to comply with legislation, however, the expectation of the company was that they were 'buying in' skills from the market when using non-regular temporary, agency and self-employed workers.

Overall, then, the case studies of agencies and employers revealed some important differences in treatment between agency temps and directly employed staff in terms of benefits. In a number of cases these differences stemmed directly from the business strategy being pursued by the agency and the rationales of firms in using agency labour – to provide cost savings for the client. Further examples from one of the case study agencies and one of the case study employers can be used to illuminate this point. Agency 1 sought to develop managed service contracts with clients. A key marketing message used by Agency 1 when selling these services to potential clients was that whilst pay rates might be similar for agency workers compared to directly employed staff (although in some cases, these rates were lower) companies could expect to make considerable savings by using the agency, since benefits provided to agency workers by the company were much more limited than for directly employed staff with the client.

A key rationale for Company 1 in using agency staff was to reduce cost levels. A sharp distinction between agency and permanent staff was reflected in the differential terms and conditions for these groups of workers. The company had actively developed a category of workers called 'permanent temps' who were engaged on long-term agency

contracts (often of 5 years or more) with the company. Alongside this group, there were also 'temporary temps', on shorter, more disposable, agency contracts with the company. Whilst the company utilised permanent temps on many core tasks, they were only entitled to some of the benefits enjoyed by permanently employed staff.

5.5 Temp to perm fees

Whilst the Agency Working Directive will not impose any restrictions on the ability of agencies to charge temp to perm fees, these fees do, in some cases, impact upon the total price charged by agencies to clients for using agency labour. Forde (2001) found that some agencies did charge temp to perm fees when a worker moved onto a direct contract with firms. In other cases, temp to perm fees were waived, but only after agency workers had been on a contract for a certain length of time. A minimum length of contract was sometimes specified as a means of 'compensating' the agency for the hourly fees they would lose when a worker moved onto a direct employment contract. As a result, agencies participating in this study were asked about the nature of temp to perm fees in their cases. All of the agencies supplying temps had provisions for the charging of temp to perm fees when a worker made the transition from temp to direct employed status within a client firm. In Forde's (2001) study, these temp to perm arrangements were formalised, and often enforced through the development of temp to perm schemes where a worker was employed for an extended period of time, guaranteeing a stream of assignment income for the agency. Ten years on from this study, the position of temp to perm arrangements appears to be somewhat different. Whilst all the agencies interviewed had provisions for temp to perm fees in practice these were rarely enforced, particularly in large contracts. At Agency 5, the agency indicated that it was often difficult to enforce 'signing on fees', and that in long-term contracts, the agency was willing to ignore these fees. Agency 6 noted that temp to perm fees were still a feature in some sectors, but were 'not an issue' in the case of industrial and manufacturing contracts. The flexibility of the agency in the enforcement of temp to perm fees (and the lack of such a fee in practice) was noted in one of the company case studies, where around 10 per cent of workers were employed as agency temps:

'it happened once last year and we tried our utmost to get out of paying the transfer fee...we try to avoid it..... we have got quite a good relationship with the agency so they are quite happy to waive the fee to keep the business. Very sought after business I think because we pay quite well'
(Manager, Company 1)

5.6 Perceptions on the likely impact of the Agency Working Directive

All of the agencies interviewed were aware of the main features of the forthcoming Agency Working Directive, particularly in terms of the areas that would need to be covered by equal treatment provisions. Some of the agencies had responded to the consultation exercises over the Directive. Agencies that were member of trade associations such as the REC had been briefed over the likely coverage and impact of the Directive. For some of the case study agencies there was a perception that whilst their systems would need to be adapted to meet the requirements of the Directive, the Directive would not pose major challenges to their business model. Agencies were aware of the need to identify comparable permanent workers, and that the regulations would cover equal treatment for pay and some benefits.

All of the agencies indicated that they already complied with the requirements of the Working Time Directive, providing temps with annual leave allowances. Whilst there had

been suggestions at the time of the implementation of the Working Time Directive that this would have a major impact upon businesses, in practice, most agencies had adapted their policies in a relatively straightforward way to meet the requirements of the Directive. Some of the case study agencies were approaching the Agency Working Directive with a similar viewpoint. Many agencies had adapted their position towards the Directive from opposition to pragmatic acceptance, as it had become apparent that the Directive was likely to be implemented. A number of agencies expressed the view that they needed the longest possible time period available before the Directive was implemented, to give them time to adapt their recruitment processes to comply with the regulations. In cases where the agency was an employer of the temps it hired out, there was also some confusion over the implications of the Directive for the identification of comparable workers – would it be a worker within the client firm in which these workers were placed, or would it be a comparable worker employed by the agency?

A number of the agencies interviewed discussed possible 'workarounds' to the provisions of the Directive. A manager at Agency 6, for example, suggested that with equal rights for agency workers starting after 12 weeks of employment, 'there will be a lot of 11 week contracts'. There was also a perception that some firms would move away from using agency labour since the cost advantage of using agency temps to firms would be diminished:

'...it is going to be more difficult, I can see them (agencies) losing out to people taking them in house' (Manager, Agency 6)

This possibility was a particular concern for agencies adopting a business model based on undercutting wages of directly employed staff. Agency 4, as noted earlier, competed by supplying migrant workers to client firms at wage rates below those offered to directly employed staff. Agency 4 put the possible impact of the Directive in stark terms:

'if this Directive comes in, I am likely to go to the wall. I just can't see how I continue to do what I do at the moment. I'm discussing options with my employment lawyer at the moment to see what is possible' (Manager, Agency 4)

For company 2, who utilised large numbers of agency temps to cut staffing costs, there was also recognition of the potential costs of the Agency Working Directive, for which the company, to date at least, seemed relatively unprepared:

'...that is going to be a problem because we have such a lot of people that are not getting paid comparably to permanent employees' (Manager, Company 1)

5.7 The impact of the economic recession on the practices of employment agencies

The agencies interviewed for this study reported quite different views about the impact of the economic recession. For some agencies, the recession had seen a decrease in the number of temps supplied, and a reduction in the use of agency services by clients. Agency 6, for example, suggested that a key impact of the recession was on the length of some agency contracts:

'I would say prior to the recession there was a definite trend towards people keeping temps on longer term...but that has been hit a lot in the last couple of years' (Manager, Agency 6)

In contrast, other agencies noted that amidst recruitment freezes in many public and private sector organisations, the use of agencies was one means through which firms could increase or decrease their headcount. Agency 3, for example reported a number of instances where client firms had begun to use their services due to freezes on recruitment for directly employed staff.

Both of these processes appeared to be at work in the two case study companies. In Company 2 the economic downturn and associated budget cuts within central and local government had led to strategic attempts to streamline the use of non-regular workers, including a reduction upon dependency upon agency staff. The HR manager interviewed indicated that temporary staff would typically be 'the first to go' if jobs cuts were needed, although other factors were also important, including skills and performance. However, it was also noted that restrictions on permanent recruitment during the recession had meant that Company 2 had extended its use of temporary and agency staff in some circumstances, as a means of filling important roles. In the current economic climate, there was more flexibility for Company 2 to employ a worker on a temporary contract than there was to employ someone on a permanent basis.

At Company 1, agency temps were treated in a similar way to permanently employed staff in the context of the economic recession:

'It has been a total decrease in headcount...so we have had...a couple of compulsory redundancies...we are losing the same percentage across the board of fixed term, agency and permanent heads' (Employee Relations Manager, Company 1)

The strategy adopted by the company, of employing agency temps on long-term contracts also meant that many had acquired firm specific skills. There were incentives, therefore to retain these workers:

'...so we do try and get rid of agency first, but it doesn't always work that way, because you have got someone who has been working here 10 years they have got the skill set that you need so it is quite difficult' (Employee Relations Manager, Company 1)

5.8 Conclusion

In this chapter, we have highlighted the role of agencies in pay setting, drawing on evidence from our case studies. Whilst the headline result from the study indicates a relatively limited role for agencies in pay setting, the empirical work has allowed for an initial exploration of the factors that shape the involvement of agencies in pay setting. There are marked differences in involvement in pay setting, for example, across different contractual arrangements. The empirical work has also shed light on the role of agencies in setting non-wage benefits and has highlighted a range of practices of agencies in this area.

CONCLUSIONS

This report has examined the role played by temporary employment agencies in pay setting for agency workers, in light of the imminent implementation of the European Agency Working Directive in the UK. The starting point for the project was that there are important gaps in our understanding in relation to the role played by employment agencies in pay setting issues. The aim of the project was to develop clearer typologies of the employment agency sector, and to establish a detailed understanding of how, if at all, factors such as geographical reach, contractual arrangements, and the occupational and industrial composition of agency employment shape agencies' role in pay setting.

The findings reported here are the outcome of a small pilot study of agencies and employers to investigate the role of agencies in pay setting, involving 25 in depth interviews, within case studies of six agencies and two companies, and gathered between September 2009 and March 2010.

Drawing on previous literature, the report has set out a number of typologies which are useful in developing an understanding of the dynamics of the temporary employment agency sector in the UK. First, there is the geographical reach of agencies, in terms of whether agencies are global, national, or regional/local in nature. Secondly, agencies vary in terms of the contractual arrangements they develop with client firms. There is a clear trend towards more embedded hands on contractual arrangements, including master vendor (preferred supplier and sole supplier) arrangements, and neutral vendor services. Thirdly, the agency sector in the UK is diverse in terms of occupational composition (although this is heavily concentrated on clerical/secretarial, semi-skilled and unskilled occupations) and sectors.

There is limited direct evidence from other studies into the role of agencies in pay setting. A brief review of the literature in chapter 3 found that agencies did have a large role in setting margins. However, in terms of hourly pay or salary rates previous literature suggested limited direct involvement of agencies.

Turning to the findings from our case studies of agencies and companies, the main finding was that agencies did appear to have a limited role to play in setting hourly wage rates for temps. However, the picture was much more complex than this headline finding suggests. The role of agencies in pay setting was, generally, more limited in public sector contracts compared to private sector ones, particularly given the recent rise in framework agreements which governed many agency-client relations. Agencies did have more of a role in pay setting in some managed service contracts. Here, there was more of a 'partnership' between agencies and client firms. Agencies took on some responsibility for payroll issues, and also advised over pay rates as contracts developed. Under neutral vendor contracts, there was also a role for the agency in advising on hourly rates, and for benchmarking pay rates. Neutral vendors also played a role in standardising the mark ups charged by agencies for national insurance and annual leave.

There was some evidence to suggest a connection between the economic cycle and involvement in pay setting. During periods of economic growth, agencies argued that they had played a greater role in pay setting, due to widespread shortages of labour. In this environment, they had more bargaining power over wage setting. There was also evidence of a greater role for agencies in setting hourly rates in shortage occupations

(such as skilled craft occupations) and in particular sectors where there was a tradition of agencies or individuals setting pay rates.

The competitive strategies pursued by agencies also impacted upon their involvement in wage setting. Agencies competing on the basis of undercutting wages of permanent staff in organisations tended to play a greater role in wage setting. A number of agencies also employed their temps directly and then hired them out to third party firms. Here, the agency had total responsibility for pay setting, although rates of pay were clearly set in relation to comparable workers within the client firm.

Agencies had a greater role in setting their margins. In practice, this did also have an impact on pay rate setting, since agencies were often faced with an overall price for agency labour, determined by the client firm. Margins were increasingly being affected by factors such as the nature of contractual relations. With embedded, hands on contracts, pressure was often put on by clients for a reduction in margins, particularly around contract renegotiation stages. In the case of neutral vendors, the 'raison d'être' for these intermediaries was to exert downward pressure on agency margins.

In terms of non-wage benefits, the study has highlighted a variety of practice of agencies. There was some notion of a 'standardised' industry level of holiday pay, set at the level of minimum compliance with the Working Time Directive. This was particularly the case within national and global agencies. Additional benefits, such as sickness benefit, shift allowances, and training were offered by some agencies. Some benefits were driven by the client rather than the agency (for example, shift allowances were generally offered by some clients, rather than being offered by the agency to all its temps working on shifts). Other benefits were attached to particular managed service contracts with clients.

Whilst the majority of agencies were already beginning to adapt their processes and systems in preparation for the implementation of the Agency Working Directive, some agencies felt that the Directive was going to significantly impact upon their business. This seemed to be the case when agencies were competing on the basis of supplying temporary workers at rates below those offered to comparable workers on permanent contracts.

Overall, then, whilst the study suggests a fairly limited role of agencies in pay setting, it is clear that the involvement of agencies in pay varies according to a wide range of factors, which reflect the diversity of the sector. A fairly obvious recommendation is that there is a need for more detailed evidence on the factors that shape the involvement of agencies in pay setting. For example, through six case studies, this research project has only begun to look at the complexities of contractual relations between agencies and client firms, and how these shape pay setting. Furthermore, as the economy in the UK emerges from recession, will the role of agencies in pay setting begin to change? The role of trade unions in pay setting for agency workers has not been examined in any detail in this study, yet there are signs that unions are beginning to represent agency workers more effectively (see Heery, 2009). Will these new strategies of unions towards agencies impact upon the pay setting activities of agencies?

Finally, what effect will the Agency Working Directive have on pay setting? The respondents in this study were able to speculate about likely effects, but there will be a need for more robust evidence on the effects of the Directive on pay setting following

implementation. Beyond the comments made by respondents, the pilot study can hint at possible effects. First, it is clear that whilst some agencies have adapted their pay setting activities to anticipate the likely effects of the directive (e.g. some of the larger, multinational agencies), other agencies (notably those that are competing on the basis of minimising wage costs and establishing clear wage differentials between temporary and permanent staff) would not be not prepared for equal treatment provisions. This suggests that the Directive would have considerable benefit in terms of its stated aims of ensuring equal treatment between temporary and permanent staff, since many agencies are not currently paying agency staff equal pay to comparable permanent employees. Some agencies appear to be *prepared* for the Directive (in terms of having thought about the likely implications of the Directive for their activities), but there is a difference between this and the actual implementation of equal treatment provisions.

As for the likely effects of the Agency Working Directive on wage rates, we return to the equation set out in Chapter 2. Client firms are faced with an overall price for the temporary labour they take on which can be represented as:

$$P_t = P_w + P_{nw} + M$$

where t is total cost to hirer, w is wage cost, P_{nw} is non-wage cost and M is the margin gained by the agency.

For the agency, it might be argued that the aim is to maximise P_t and to minimise P_w and P_{nw} . By extension, this allows the agency to maximise M , the margin charged. Using this equation, it appears likely that P_w should end up rising. If P_t remains the same, by extension the agency margin (M) will be squeezed. Alternatively, if M remains the same, then P_t will need to rise. The balance of power in pay setting between agencies and firms will determine which of these two possibilities (or a combination of adjustments to both P_t and M) occurs in practice. In strong economic conditions, or where agencies have bargaining power by virtue of a long-term contract with client firms, or where agencies are supplying a niche occupation or sectoral market, then agency power to maintain M may be greater. The factors that determine the balance of power between employers and agencies in pay setting should form a priority for future research.

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APPENDIX 1: INTERVIEW SCHEDULE FOR ACAS RESEARCH INTO THE ROLE OF AGENCIES IN PAY SETTING

1. BACKGROUND

Can you us about this employment business/labour provider

When established

How many branches in UK/International

Probe as to whether global, national, regional or local agency.

At this branch:

- How many workers are on assignment in an average week
- How many are on the books
- How do these figures fluctuate seasonally
- How many staff do you employ directly as recruitment consultants/managers in this branch
- Do you offer permanent placement as well as temporary work
- What occupational areas/industrial activities do you supply workers for (try to get proportions, and most important areas of business)

2. THE NATURE OF YOUR RELATIONSHIP WITH CLIENT FIRMS

Can you describe the structure of your business in terms of your relationships with client firms

Do you have large contracts with client firms, which make up a significant proportion of your business, and which involve the supply of significant number of temporary staff

Probe these contracts in more detail:

- When was each established, how has it evolved
- What industries are client firms in
- How many temps on assignment at any one time
- How is the contract managed Arms length. On-site management. Mixture of both
- Are you a preferred or secondary supplier on any of these contracts

Are you a 'master vendor' on any contracts with client firms (NB. some of the above large contracts are likely to be master vendor contracts)

- When was each established, how has each evolved
- What industries are client firms in
- How many temps in total are on assignment at any one time
- How many do you supply How many are supplied by others
- How is the contract with client firms managed (arms length, on-site management, mixture of both
- How is the relationship with other agencies managed
- How are shortfalls in numbers filled by other agencies
- Auction process Hierarchical relationship, 'first come first served' etc
- Are you a secondary agency that provides temps for a master vendor

Are you involved in any 'neutral vendor' arrangements. If so, probe in more detail, using the questions above. Smaller, non vendor contracts: beyond these contracts, can you tell us about other contracts with client firms, such as long-standing regular contracts, 'one-off' contracts etc.

3. PAY SETTING

What role do you play in setting pay in the various contracts you are involved in with client firms

Do you have recommended pay rates for particular jobs/occupations

- How are these determined
- To what extent are these fixed when agreeing pay rates with client firms
- Do you currently seek to identify comparable permanent workers in agreeing terms and conditions for agency workers
- Do you seek comparability with workers in client firms, or with other agency workers on your books
- What are the challenges in establishing comparable workers and what solutions have you developed in this area
- 12 week period for comparability
- Temp to perm
- Where you have sought to establish comparability, what aspects of pay are covered in comparability (e.g. basic pay, bonuses, shift allowances, holiday pay). Which aspect have been most difficult to establish comparability, and which most straightforward

As moves to implement the AWD have approached, have you changed your strategy towards pay setting for agency temps. If so, in what ways. Probe:

- 12 week period for comparability (continuous employment with single firm, or continuous employment with agency)
- Temp to perm
- Hypothetical versus actual comparators.

4. ASPECTS OF PAY SETTING

To what extent are pay rates negotiated between agency and client, or are pay rates driven by the client, or by the agency

How does the level of negotiation over pay levels vary across contracts

What factors determine the degree of involvement of agencies in pay setting (in other words, under what circumstances do you have a greater role to play in pay setting)

- Size of contract
- Long-standing relations with clients
- Public versus private sector
- Global, national, regional agency. Role of head office in determining local pay rates. Discretion at branch level.
- Industrial activities of clients
- Occupational level/skill level of temp
- Trade union recognition at client firm
- Trade union recognition/involvement at agency

Which of your staff are most involved in pay setting activities

- Temp staff consultant
- General agency manager
- On-site manager

Is there a greater role for your agency in pay setting in master vendor/neutral vendor/preferred supplier arrangements

If so, in what ways is there greater involvement (NB, try to establish whether pay rates for temps are variable in such contracts, or whether it is the agency margin that is variable).

5. OTHER ISSUES

How the pay setting experiences compare with wider terms and conditions setting

How much knowledge do you have of pay rates in client firms and what might be the issues/implications of finding out about these.

