

## Negotiating Wages in Times of Higher Inflation

Ted Clark

The negotiation of wage increases to be implemented over the term of the parties' new collective bargaining agreement is almost always a contentious issue, but it is especially so during times when the cost-of-living is higher than normal. The annual increases in the Consumer Price Index for All Urban consumers (CPI-U), the most widely used index to measure changes in the cost-of-living, has increased somewhat significantly since 2018, as the following tables demonstrates:

YEAR	ANNUAL PERCENTAGE INCREASE
2018	1.50%
2019	2.29%
2020	1.36%
2021	7.04%
2022	6.45%
2023	4.04% (annualized based on 10 months' data)

While the average percentage increase in CPI-U on a yearly basis (December to December) is decreasing since 2021, it is still significantly above the Federal Reserve's target of 2.0%.

In defending against union demands for wage increases based on inflation, the following are among arguments that public employers might consider making. First, while it is true that the cost-of-living has increased above historical norms, there have been many years in which the negotiated wage increases exceeded the annual CPI-U increase, especially in the years prior to 2021. This contention is obviously fact-based. Consider whether it is something your jurisdiction can use in negotiations.

Second, while the national CPI-U has increased 3.24% in the past 12 months (October to October), be sure to check the CPI-U for your geographical area since it may have increased by a significantly lower percentage. For example, the most recent 12-month increase in the CPI-U for the Chicago metropolitan area rose only 2.443%. Again, this is very dependent on what the facts are for your geographical area.

The Bureau of Labor Statistics (BLS) issues numerous CPI indexes based on geography and demographic characteristics. For example, in addition to the indexes for major metropolitan areas, the BLS also issues monthly CPI index numbers by region and size for the Northeast, Midwest, South, and West. And, the CPI index numbers for each of these regions is further broken down, e.g., for the Northeast, there is a further breakout of two indexes based on city size, one for New England, and one for Middle Atlantic. The BLS, however, cautions against use of such local indexes:

Local area indexes are byproducts of the national CPI program. Each local index has a smaller sample size than the national index and is, therefore, subject to substantially more sampling and other measurement error. As a result, local area indexes show greater volatility than the national index. Therefore, the Bureau of Labor Statistics strongly urges users to consider adopting the national average CPI index for use in escalator clauses.

Despite the limitations on the use of local area indexes, they do not prevent management negotiators from selectively using one or more of them for bargaining purposes.

Third, while CPI-U is typically used for measuring changes in the cost-of-living, the BLS also issues a separate CPI-W index, which is the U.S. city average for urban wage earners and clerical employees. For the most recent 12 months CPI-W increased by 3.09%, i.e., somewhat lower than the CPI-U number. Since public sector bargaining units only include wage earners, one could logically argue that CPI-W is the more appropriate index to use for cost-of-living purposes in collective bargaining.

Fourth, the cost-of-living as measured by the BLS is made up of a fixed basket of goods and services. As such, the fixed basket is static and does not change even though consumer preferences change based on the cost of specific goods and services. The Bureau of Labor Statistics (BLS) understands this phenomenon and issues a separate monthly chained CPI-U specifically designed to capture changes in consumer preferences and the impact they have on the cost of living. As explained by the BLS, the “C-CPI-U is designed to be a closer approximation to a cost-of-living index in that it, in its final form, accounts for any substitution that consumers make across item categories in response to changes in relative prices.” For example, when the price of meat is expensive and the price of poultry or fish is lower, consumers tend to substitute poultry or fish for meat.

The difference in the cost-of-living as measured by CPI-U and C-CPI-U can vary significantly from one 12-month period to another 12-month period. Thus, for the 12-month period between October 2022 and October 2023, C-CPI-U was up 3.1%, just slightly lower than CPI-U. However, for the 12-month period between January 2021 and January 2022, CPI-U was up 7.5%, but C-CPI-U was up only 6.8%.

Fifth, in negotiations it is important for public employers to take full credit for all the fringe benefits for which they pay all or a significant portion of the cost. For example, the BLS

market basket of goods and services includes health care and clothing. To the extent that the public employer is paying the full cost or a substantial portion of the cost of these fringe benefits, these are costs that employees do not have to bear. Obviously, the list of employer-provided goods and services is jurisdiction-dependent, but in addition to health insurance and work uniforms, it can include such things as dental/vision care (either insurance or reimbursement), take-home cars, reimbursement for college tuition, transportation costs, and employer provided childcare facilities, etc. All these employer-provided fringe benefits lessen the impact on employees of increases in the cost-of-living. As Arbitrator Steven Briggs observed in *Arlington Heights and IAFF*, Case No. S-MA-88-89:

It is also important to recognize that no matter what the ultimate mix of the parties' respective final offers the Arbitrator selects for inclusion in their contract, Arlington Heights Firefighters will receive more in monetary benefits than reflected in salary increases alone. When benefit costs are added, the percentage increase in total package cost is undoubtedly higher than cost-of-living increases as measured by the CPI-U or the CPI-W.

Sixth, in computing the cost wages increases, it is important to take into account the impact of compounding on wage increases over the course of the contract term, step increases, longevity increases, and any other increases tied to increases in the employees' hour rate (e.g., overtime, holiday pay, etc.). In terms of the impact of compounded wage increases, assume an employer offers increases of 3%, 3%, and 3% for a three-year contract. While it might be characterized as an overall increase of 9%, in actuality it is an increase of 9.27%, by virtue of compounding, i.e.,  $1.03\% \times 1.03\% \times 1.03\% = 9.27\%$ .

It is even more important to take credit for the additional cost of step and longevity increases that bargaining unit employees will receive during the term of the proposed contract. This is what well-regarded Illinois interest arbitrator Edwin Benn refers to as "the real money." In *Cook County Sheriff/Cook County and AFSCME Council 31* (Arbitrator Edwin Benn, May 16, 2016), to cite only one of many Benn interest arbitration decisions on this topic, Arbitrator Benn ruled that the percentage wage increases offered by the parties "do not take into account a most important factor from the employees' standpoint, i.e., increased wages paid as a result of step movements over and above general wage increases—which in prior awards, I have referred to as "the real money." Since these wage costs are significant, negotiators for public employers should take credit for these additional costs in computing the cost of their wages viz-a-viz increases in the cost-of-living.

Seventh, public employers should take full credit for their annual costs for funding public employee pension plans. As Arbitrator Marvin Hill stated in an arbitration case I handled a number of years ago in *Village of Schaumburg*, Case No. S-MA-10-299 (Arb. Marvin Hill, September 19, 2011):

There is an additional consideration in salary and benefit analysis that rarely gets mentioned in interest arbitrations but will demand more consideration in the future—pension obligations of the government entity.... Although the Village has not entered an inability-to-pay argument regarding pension obligations ..., defined-benefit pension costs that increase with salaries should be recognized as an increased obligation on a government employer. *Id.*, at pp. 30-31, n.19.

Depending on the pension laws in your jurisdiction, the annual cost of funding the public employee pension plans, especially for fire and police pension plans, can amount to 30-40% or more of the annual cost of wages alone.

Eighth, and finally, to reduce the cost of wage increases due to higher inflation, an approach that some jurisdictions have used is to split the wage increases into two or more increases over the course of a year. Support for this approach is based on the fact that the cost-of-living does not go up by the annual amount on January 1, but rather it goes up gradually over the course of the entire year. For example, assume CPI-U is annually going up at the rate of 4%. On a monthly basis it is only going up by an average of one-third of one percent (0.333%) per month, i.e.,  $12 \times 0.333\% = 4\%$ . Accordingly, to keep pace with the cost-of-living, an increase of only 0.333% would be needed as of January 1. To simplify this example, suppose the employer proposed a 4% lift over the course of one year, but split the increases, e.g., an increase of 2% effective January 1 and another increase of 2% effective July. The employer's cost for the year in question would only be 3% because the second 2% increase is only effective for the last six months of the year. However, keep in mind that the full impact of the 2% July 1 adjustment would be incurred in the first six months of the following year. Nevertheless, the employer in this example would have reduced the cost of the first year's lift in wages by 1% percent excluding the slight cost of compounding the 2% July 1 adjustment (unless the 2% July 1 adjustment is computed based on the wage rates in effect on December 31 of the preceding year).

In summary, there are a host of facts and arguments that public sector negotiators should consider making in countering union wage demands based on higher CPI numbers. These suggestions, however, are not a "one size fits all." As a result, the suggestions in this article must be tailored to facts and circumstances in your jurisdiction.