The Economic Analysis of Employee Rights

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Labour economists and industrial relations scholars tend to pay little explicit attention to "employee rights", generally treating this issue as a background notion, the nature of which is left to labour lawyers to explain. This situation is unsatisfactory at a time when the ability of unions to defend employee rights is declining; employers are being subjected to increasing pressure to undermine labour rights that supposedly raise production costs; and the notion that the state has a duty to defend the rights of employees is being subjected to a level of scrutiny unknown since the early years of the twentieth century. Given these developments, a more conscious consideration of the nature of employee rights and their economic rationale is required. This paper aims to assist this process by offering some introductory comments on the origins of employees' rights; the claim that the market and individual bargaining are the most effective instruments for ensuring that workers obtain an optimal mix and level of these rights; and the notion that respect for "core" labour standards should be linked to the right to engage in international trade.

The nature and source of rights

The term "employee rights" can be used in a number of different ways. Lawyers normally take it to mean a claim deriving from a rule or law which can be enforced in the courts; philosophers equate the term with a legitimate claim that is based on religion or morality; while everyday speech tends to use it in a manner that blends the legal and moral element. An employee right is a "good" that may accrue to a worker by way of contract or as a consequence of the fact that the worker belongs to a particular group. Given the divergence in conception and utilisation associated with the notion of worker rights, it would appear the term has specific meaning only in relation to the context in which it is used. This fact can be a source of acute distress to employees who incorrectly believe they enjoy certain rights because they belong to a particular group. This is exemplified by the High Court's 1994 decision to deny workers' compensation payments to an injured employee on the grounds that the worker was an illegal migrant and hence not part of the

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population able to legally undertake employment in Australia. The individual involved had believed that being a waged employee he or she had a right to compensation when in fact as an illegal worker he or she was not part of the subset of humanity that has the right to make a legitimate claim on the Australian workers' compensation system.[3]

For the purposes of this paper, employee rights are defined as claims or privileges that a person who is legally able to take employment possesses as a consequence of the fact that they are an employee and that they may exercise as protection from the established workplace governance. This understanding holds firstly, that employee rights are only possessed by employees and that the loss of one's employment will invariably result in the loss of these rights. This was a vital lesson highlighted by the national airline strike of 1989 when the striking pilots made the disastrous mistake of resigning and by so doing ceased to be employees and hence forfeited their right of access to the Industrial Relations Commission. Also inherent in the definition is that employee rights are claims that may be exercised in opposition to or as limitations on the ordinary use of legitimate power within the workplace and may be advanced legitimately irrespective of whether the employer wishes to cede or deny these claims. In the following section we examine the origins of employee rights and suggest that they emanate from four major sources, the workers' humanity (human rights), the state (statutory rights); contract (contractual rights), and employers (enterprise rights).

Human rights

The most fundamental rights associated with the employment relationship are those human rights recognised in any civilised society as necessarily belonging to all human beings. These include both those "background" rights, such as the right to life and liberty, and the "institutional rights" created by such bodies as the United Nations. Since 1945 the UN has been the key international body that has institutionalised and defended human rights. It has done so by formulating convenants which it has encouraged member states to ratify and enforce. In relation to the rights of employees the primary instrument utilised by the UN to advance this process has been the International Labour Office. Examples of UN human rights covenants that are of direct relevance to employees include the International Covenant on the Rights of the Child; the Occupational Safety and Health Convention; the International Convention on the Elimination of all Forms of

3 Creighton W B and Stewart A *Labour Law: An Introduction* (Federation Press, Sydney, 1994) p 143.

Discrimination Against Women; and the Freedom of Association and Right to Organise Convention.

The Australian Government has ratified a number of UN conventions and by so doing has provided a constitutional basis for legislation that has direct and significant implications for the employment relationship. Appreciation of the importance of this fact was brought home in 1993 by the Federal Government's decision to use the external affairs power in the Constitution to ratify the Termination of Employment Convention. Ratification guaranteed employees certain minimum standards in relation to unfair dismissal. This was an action subsequently embodied in Part VI of the *Industrial Relations Act* 1988. It was also an action that caused acute distress amongst employers and induced the conservative political parties to promise to repeal the legislation should they come to government. In the federal election campaign of 1996 this promise became the source of some heat when Justice Murray Wilcox, Federal Court judge and Chief Justice of the Industrial Relations Court of Australia, observed that the dismissal provisions in the Industrial Relations Act were not at odds with the needs of business. He insisted the law was only "at odds with bad business, and the problem is there are too many bad managers who don't have enough respect for their employees". Wilcox also observed that the dismissal legislation introduced by the federal government had merely granted the minimum required to comply with the rights provided for in the convention.

Employers were particularly distressed by the Labor Government's action because a ratified UN convention can only be renounced for a one-year period every decade. Consequently, it is not possible to eliminate this form of employee right merely by lobbying or replacing the government of the day. This is a lesson that should not be lost on employees or their unions. Nor should the point be missed that in the Foreign Affairs Power there now exists a constitutional foundation upon which can be established in Australia an employee human rights regime that provides a powerful instrument that can be utilised to protect workers' rights from the vagaries of political life and vacillating governments.

Statutory rights

Human rights exist as rights even if they are not recognised in the statutes of nations as they have a moral existence that *should* be recognised in any civilised society. By contrast, statutory rights include only those claims which have been given legal force by the state. Beginning in the early years of the nineteenth century it came to be generally accepted that capitalist societies could not permit the employment relationship to be governed solely by market forces or morality. The needs of nations, individual employees and capitalism itself required that the state place legal

constraints on the employment relationship. The extent to which this notion has been accepted by governments has differed across nations and over time. Since the early 1970s the pendulum has swung towards greater reliance on the market and self-regulation and away from the enactment of legislated rights. However, this trend has not been unidirectional even in the nations that have led the return to reliance on the market. Thus the last decade has seen important reforms enacted in the US that have provided workers with a number of significant new rights. Examples of these statutory rights in the US include the amended *Age Discrimination in Employment Act* (1986), and the *Worker Adjustment and Retraining Notification Act* (1988), the *Americans with Disabilities Act* (1990), and the *Family Leave Act* (1993).

These laws have directly expanded the rights of those employees who are covered by the relevant legislation. Their value is of great significance at a time when the market is providing workers with decreasing employment security and declining bargaining power. In this adverse economic environment it is of critical importance that workers strive to ensure that statutory rights that protect their interests are not taken from them by those who would deny them protection from the demands of the employer under such banners as the "right to choose" and "equality of opportunity". At the same time employees and their allies must be aware that the value of statutory rights is limited by inherent problems associated with their enforcement. What all nations have discovered is that providing workers with legal rights does not necessarily grant them the capacity to realise these rights. Consequently, it is imperative that there exist enforcement mechanisms capable of ensuring that workers can achieve this realisation. This is a particularly difficult problem when the legislation granting a particular right is complex, not accepted as being morally just by large sections of the community, or is not backed by sufficient force to compel compliance from those who stand to gain from its infringement.

Statutory rights are most effective when they are designed to regulate the more simple and easily quantifiable aspects of the employment relationship, that is when they deal with such issues as minimum wages and maximum hours. With these issues the state has been able to provide workers with important rights and establish instrumentalities that are able to act as effective defenders of employee statutory rights. However, while the state has had a high rate of success in defending those rights where fixed standards can be established and infringement of which is relatively easy to detect, it has had less success with more complicated and less quantifiable issues. An important and much studied example in this regard is occupational health and safety. The difficulty associated with this complex area of employment has led governments to embrace "Roben's style" laws which seek to ensure employees realise their right to work in a safe environment by simplifying legislation and administration and by promoting self-regulation. It is an "approach

to occupational health and safety regulation which seeks to combine a significant degree of standard-setting and enforcement by external agencies with a substantial measure of standard-setting and implementation at the level of the workplace."[4] In practice the Robens model has had some success but experience has shown there is a tendency for self-regulation to atrophy in practice and an even stronger tendency for governments and inspectorates to provide inadequate support for the process of self-regulation at the workplace.[5] Given this difficulty it is clear that, while employee statutory rights are of critical significance and that it is generally in the interests of workers that they be retained, it remains the case that the realisation of the potential inherent in these rights cannot be left solely to the goodwill of the state. In short, the defence of employee rights also requires contractual bodies that can enforce realisation.

Contractual rights

Employee rights gained by contract may be based on individual bargaining or may involve a collective agreement. In either case the contract generates rights only if its provisions are enforceable. Individual contract bargaining has become of increasing significance in recent years and has now been accepted by the Industrial Relations Commission as a recognised part of the Australian industrial relations system. Nevertheless, collective bargaining remains a primary and important feature of the employment relationship in all developed nations and the right to bargain collectively is emerging as a significant employee demand in the newly industrialising states.[6] The present trend away from collective bargaining in the highly industrialised nations is largely a consequence of the fact that the Keynesian age with its low unemployment, high productivity growth and stress on demand management has come to an end. During the economic boom that lasted from 1945 until the early 1970s, an unprecedented proportion of the workforce refused to accept that individual bargaining and the market alone were capable of providing the mix and level of rights they desired. Provided with greater market freedom by the sustained level of low unemployment, these employees chose to express their freedom by joining organisations of collective representation. In short, given enhanced freedom of choice, employees chose to join unions in numbers previously unknown.

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4 Creighton W B and Stewart A *Labour Law: An Introduction*, (Federation Press, Sydney, 1994) p 301.

5 *Ibid*, p 302.

6 Levine M J *Workers Rights and Labour Standards in Asia's Four New Tigers: A Comparative Perspective* (Plenium Press, New York, 1997).

During the Keynesian age the governments of the advanced industrialised capitalist nations accepted that workers should be able to join unions and utilised these bodies as agents of demand management through incomes policies. In the English-speaking nations, however, government support for unions was conditioned by an understanding that these bodies would confine themselves to issues of distribution. In short, the state conceded workers an expansion of their right to participate collectively in the management of the distributive side of the employment relationship but did so on the condition that unions accept they had no rights, or at least very few rights, in relation to the creation of wealth. Control of the supply side, with its concern with such issues as staff selection, training, the development of career paths, etc was seen as being the right of management.

While the Keynesian age was sustained, this compromise went largely unchallenged. However, as one nation after another found that the productivity growth underpinning the boom was difficult to sustain, the maintenance of the compromise began to be re-examined by both employers and workers. As a consequence, governments became increasingly concerned with supply-side issues and solved the problem of how to contain the power of organised labour by reconstituting the reserve army of labour. In this new supply-side world, the positive role that unions had played as agents of demand became of decreasing significance. Where unions appeared to have little to offer on the supply side, moreover, governments and employers became less enthused at the notion that organised labour should play a major role in the wage-setting process. This development was particularly pronounced in the US and the United Kingdom where there was a tendency for employers and their sympathisers within the intelligentsia to extend to the labour market the ideas of nineteenth century classical economic liberalism.

In response to the employers' offensive against employees' collective bargaining rights, the international union movement has responded by seeking to expand employee rights on the supply side. They have revived the notion that employees and their unions should have the right to participate in the resolution of problems relating to the supply side. More specifically they have advanced the demand that workers should have increased rights to bargain collectively over such issues as training, careers paths and firm-specific and national investment policies. Seeking to gain support for this strategy, unions have striven to develop a convincing case to justify an expansion of employees' supply-side rights. Their argument has two basic elements. First, it is argued that it is just that workers should participate collectively in the determination of wealth creation because this process necessarily involves issues of critical importance to their well-being. As they came to appreciate the little weight such arguments carry with governments and employers, they have

emphasied the point that the German and Japanese experience has shown that effective development of the supply side in fact requires this form of employee involvement. It is insisted that the latter nations have shown that ceding unions a right to participate in the resolution of supply-side issues is of vital necessity if the creation of the committed and co-operative workplaces, necessary to improved competitiveness and productivity, is to be achieved. Likewise, they have sought to convince governments to enact legislation that will increase the legal rights of employees to bargain collectively over supply-side issues.

Internationally, employers have accepted there is some truth in the supply-side arguments put forward by the union movement, though the response has differed greatly across nations. US employers generally dismiss the claims while the Europeans and Japanese are more sympathetic. Australia's leading employers are somewhat receptive to the argument but at the moment are of the opinion that while the strategy has value it is not necessarily suitable for all. Thus the Business Council, when commenting recently on workers' right to participate in the management process, asserted that "results can be achieved by various routes . ... and it is 'horses for courses' as far as each enterprise's choice is concerned".

Enterprise rights

Grants or promises which employers cede unilaterally but do not write into a contract of employment are a fourth important source of employee rights. These "enterprise rights" are not simply the custom and practice of the trade but rather are "goods" employers explicitly and voluntarily cede to their employees but which can be revoked at the employer's will precisely because they have not been written into a contract. Over the twentieth century, enterprise rights have become of ever greater importance both in extent and scope. This point is highlighted in Edwards R *Rights at Work: Employment Relations in the Post-Union Era*, (Brookings Institution, Washington DC, 1993) which contrasts the negligible rights enjoyed by a non-union worker in a Ford plant, a leading corporation of the 1920s, with the rights enjoyed by a similar worker in a leading company of the 1990s, such as Hewlett Packard. These rights have also been highlighted by Lazonic W *Competitive Advantage on the Shop Floor* (Harvard University Press, Cambridge Massachussets, 1990) which has observed that many non-union firms in the United States have voluntarily provided their employees with such rights as tenure, and access to vertical job structures and systematic grievance procedures.

To a significant extent the increased prevalence and scope of enterprise rights has been a consequence of employer attempts to capture the enhanced employee goodwill and productivity that the unilateral granting of employee rights can generate. It has also been a result of the fact that many employers believe granting

enterprise rights is an effective way of convincing employees they have no need to join a union. The unilateral granting of employee rights, moreover, is attractive to employers because such rights are weakly founded in law and hence employees who challenged firms who renege on enterprise rights can do so only if they are willing to risk significant legal costs.

The unilateral granting of enterprise rights in order to avoid unionisation remains a popular employer strategy and this is especially so in the US where it has been a major element in the highly successful anti-union campaign sustained by employers since the 1960s. Dating from the middle 1980s, however, the attractiveness of this strategy has been undermined somewhat by the fact that US courts have become favourably inclined to the argument that enterprise rights should be given greater legal enforceability and the passage of litigation in relation to these rights needs to be made both easier and cheaper for the employee. Edwards[7] reports that this shift in legal thought is a product of the fact that the judiciary has acknowledged that as a consequence of decreased government enthusiasm for statutory rights and the decline in union leverage, the claim that US workers and employers bargain with any degree of equality has become increasingly difficult if not impossible to sustain. The courts consequently have moved to provide workers with new rights that they can hold up against the authority of the employer.

The foregoing is a development not always welcomed by unions or employers. The former because they believe the courts may undermine the attractiveness of unionism for workers and the employers because an enhanced role for the courts and common law threatens their prerogatives in the employment relationship. Heterodox and pro-labour radical economists, such as Edwards, on the other hand, have asserted that these developments are generating an important new means for defending worker rights. They argue that companies should be compelled to make public they enterprise rights they offer their employees. By so doing, the labour market will function more effectively as workers will have greater knowledge of what is being offered and the courts will be better able to enforce these rights as constituting implied contracts.

The economic rationale for employee rights

In a world in which it is widely accepted that individuals should have as much control as possible over their own lives, the notion that individual bargaining is the most just method of ensuring workers attain an optimal mix and level of employee

7 Edwards R *Rights at Work: Employment Relations in the Post-Union Era* (Brookings Institution, Washington DC, 1993).

rights has proven of great attractiveness to many employers, intellectuals and workers. This notion also has particular appeal to orthodox neo-classical economists who tend to argue that individual bargaining and unfettered market forces will lead to maximum efficiency for an economy. The significance of this belief was enhanced on 23 January 1996 when the Australian Industrial Relations Commission confirmed in the Comalco Weipa case the right of employees to negotiate individual contracts. By so doing, the Commission made it clear that individual contracts are a part of the Australian industrial relations system.

Given the increased cultural and institutional acceptance of individual bargaining and market determination, advocates of publicly provided employee rights need to explain why the former instruments will not achieve economic optimality in relation to rights. This is a task undertaken effectively by Edwards who has shown there is substantial reason to believe market forces and individual bargaining alone will not deliver an optimal mix and level of employee rights.[8] He notes that the neo-classical argument is based on strong assumptions which include full employment of all factors of production, perfect substitutability of all factors, perfect knowledge of technology and market conditions, as well as freedom of entry to markets and homogeneous products. The absence of any of these conditions makes it impossible to achieve the greatest efficiency from any given bundle of factors of production (Pareto efficiency) through the market. Consequently, singular reliance on the labour market may not only produce outcomes that many would consider unjust, it may also produce results that are economically sub-optimal.

> In brief, this market is characterised by long-term relationships in which, for job-seekers, the conditions for market contracting are distorted by asymmetries of information, inequality in bargaining status, and a lack of contract enforceability; for job-holders the opportunities for recontracting are limited because of a weak "exit" threat due to the personal cost of worker mobility; and bargaining by workers for their rights is not optimal because of public good and economies of scale characteristics of workers' rights.[9]

Markets alone, in other words, cannot be relied upon to determine the optimal level and mix of workers' rights and hence the market needs to be supplemented by other social institutions. The following section of this paper draws closely on Edwards' argument. It begins by outlining three factors that combine to prevent the market providing the optimal level and mix of rights and then proceeds to detail why singular reliance on individual bargaining is an inappropriate mechanism in the area of rights.

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8 *Ibid.*

9 *Ibid,* p 44.

Whether it is possible to rely on individual bargaining and market forces to provide the right mix and level of employee rights is dependent, in the first instance, on whether the circumstances facing job seekers and employers creates the conditions for efficient market competition. Edwards has observed that the existence of three structural features of labour markets (asymmetric information, structural inequality and lack of contract enforceability) give reason to believe that this is unlikely to be the case.

Asymmetric information

In many cases workers do not have the information regarding rights that is essential to the efficient functioning of the market. This is a difficulty even where employees have a statutory right to information but the knowledge that is needed to bargain effectively is complex and hence interpretation requires special skills. It is of even greater significance where the market generates asymmetric or "private" information, as tends to be the case with enterprise rights. The latter form of rights has particular appeal to advocates of unrestrained markets because it is freely offered up by employers. The problem, however, is that, because of the proprietary nature of corporate employment practices, job seekers have no right of access to reliable information regarding these firm-specific rights. They therefore cannot compare the availability of such rights across different employers. It should be noted that this is not simply a problem of the cost of obtaining information. Rather, with enterprise rights there are legal and other institutional barriers that prevent access to this information. Given this knowledge barrier to a form of rights that is becoming of ever greater significance, it would appear that the market will invariably fail to provide individuals with the basic information they need to bargain an optimal mix and level of rights.

Structural inequality

The difficulty resulting from the fact that the market cannot provide job seekers with basic knowledge regarding an area of employee rights that is both significant and continuing to increase in significance is compounded by the fact that there typically exists a fundamental inequality in the bargaining power of employers and individual job seekers. This imbalance is such that it is common for job applicants not to enquire too closely as to the conditions of employment for fear that to even ask for such information will adversely affect their chances of obtaining a position. That job seekers would fear to negotiate such basic issues as right of access to a grievance or dismissal procedure is understandable. It is a fear that has been greatly enhanced over the last two decades as a consequence of the fact that mass unemployment has returned as a normal feature of the labour market in capitalist economies. Hence, fear

emanating from the imbalance of power in the socially structured institution that is the labour market undermines the capacity of individual bargaining to ensure an optimum mix and level of rights.

Lack of contract enforceability

It cannot be expected that the market process will achieve efficient outcomes, if as a matter of routine, it is found that bargains or contracts are unenforceable. Yet lack of enforceability is common in relation to enterprise rights, that is, those important rights that are voluntarily ceded by the employer and which the latter can revoke or change at will. It is true that some market enforceability is exerted by "reputational affect" and by the possibility that the arbitrary revoking of enterprise rights might adversely affect productivity where these rights constitute a significant productivity wage element. The former mechanism is likely to have significant impact, especially when new workers are being employed, and the latter when the right being revoked or changed is of major significance. For example, if a promised right to job security is arbitrarily withdrawn, this well might affect the ability of an enterprise to subsequently attract appropriate staff. In general, however, the value of reputational effect must be considered to have only marginal influence, given the willingness of even "good" employers, such as IBM and the Australian Federal Public Service, to engage in compulsory large-scale retrenchments.

As for the enforcement capacity supposedly inherent in the danger that employees' productivity might be affected adversely by the arbitrary abrogation of rights, again it is difficult to believe this factor is greatly effective. Certainly, where market forces have been allowed to dominate both the employment and capital markets, the enforcement impact of this factor has been all but negligible. This has proven to be a particular difficulty in the US and the United Kingdom where the need for firms to focus on the needs of the short-term money market have constrained their ability to develop long-term effective human resource policies. What this experience suggests is that it is in the long-term interest of employers, workers and society at large that there exist some exogenous institutional influence that will contain the willingness and ability of employers to bow to short-term market forces. Experience also suggests that, at least as regards employee enterprise rights, the lack of any effective market enforcement mechanism is an issue of substantial concern and significance. Finally, it justifies Edwards' observation that a market process devoid of legal support and having weak informal mechanisms of enforcement is unlikely to arrive at optimal results.[10]

10 *Ibid*, p 56.

If employment could be seen as a process of continuous recontracting, the fact that the structural problems thus far identified distort initial labour market bargains would be of much less significance. A sub-optimal situation created by market contracting could be remedied by the use of "voice" or "exit". The difficulty with this solution lies in the fact that individual employees generally have limited capacity to use these recontracting mechanisms effectively. The cost of utilising exit, that is, resigning, is extremely high and voice is a weak instrument precisely because individuals have little capacity to threaten exit given the high cost of carrying through any such threat.

The difficulties these structural weaknesses cause for the presumption that the market mechanism can deliver an optimal mix of employee rights is compounded by the fact that employee rights have a significant public good character and the transaction costs associated with these goods are subject to significant economies of scale. Given that this is the case, it is probable that individual bargaining will produce not only a sub-optimal mix of rights but also an inadequate level of these goods in markets characterised by various types of market failure. Two common causes of market failure are the public goods case and the effects of economies of scale on markets.

Public goods

By a public good is meant a product or service that when provided to one person must be provided to others and one persons consumption does not detract from anothers consumption. Food consumed is a private good and a drained malarial swamp is a public good. Employee rights tend to have significant inherent public goods aspects even if the "public" only involves other workers in the enterprise or firm. For example, to provide one worker with a workplace safe from toxic chemicals invariably means simultaneously doing likewise for all others within the workplace. This is because of the high technical, economic and/or social cost associated with individualising the benefit from this type of good. The need to universalise the benefit, however, means that it is not possible for the employer to bargain with individual employees as to whether or not they will receive these rights. The employer cannot because the individual employee necessarily obtains these rights as a given and hence need not offer up anything as a quid pro quo. In such a situation, a less than optimal quantity of employee rights will be provided. On the one side, the individual demander of rights (worker) will not reveal his/her true preferences nor demand as many employee rights as are really desired. Given the latter can reasonably hope to be a "free rider", he or she would be wise to confine the use of individual bargaining power to bargaining solely over private contract benefits. Of course, if the demand for the right desired is advanced collectively, this problem is

resolved by the fact that the workers' bargaining agent will need to make clear the amount of rights the workers truly desire. On the other side, the supplier of a public good cannot charge individuals for their consumption because there is no mechanism for excluding nonpayers. Consequently, the latter has no incentive to ensure its provision. Given this situation, it is probable an inappropriate level of rights will emanate from individual rights contracting.

Economies of scale

Individual bargaining over employee rights may also produce sub-optimal outcomes because of the significant economies of scale often associated with the supplying of these rights. Where the transaction cost of providing, implementing and otherwise operating a separate rights package for each employee is high, and to some extent is fixed, the employer will have an economic incentive to establish a standardised package. By spreading rights associated with fixed transaction costs across many employees, the employer is able to reduce per unit cost. These considerations suggest that where major economies of scale can be realised by providing employee rights in the form of a supra-contractual package, that is, applicable to many, there will be a tendency for competition to ensure that employers take up this option. On the other side of the bargaining process, it is clear workers may also experience economies of scale in bargaining over rights. To be able to bargain effectively and to ensure the enforcement of a bargain, a worker needs to have a great deal of knowledge and must be willing to make significant outlays to cover the cost of contract monitoring and enforcement. A group of workers will be able to meet these outlays at a much lower average cost by dividing up the tasks involved and sharing the accumulated knowledge and expenses. These scale issues suggest that, if bargaining over rights is undertaken purely on an individual basis, employers will tend to offer a level of rights that is less than optimal and individual employees will have inadequate knowledge to ensure that they can bargain with maximum effectiveness.

The conclusion that the foregoing argument engenders is that there are strong reasons for doubting that individual bargaining by workers and employers will produce the optimal mix and level of employee rights. As Edwards concludes, it would appear that if the market is left to itself "Too little of workers' rights will be produced and the mix, given the poor signalling mechanisms, may be wrong."[11] Consequently, the market and individual bargaining need to be supplemented by other social institutions. Further, those whose prejudices incline them to assume otherwise have no more substantial case than those whose personnel beliefs and

11 *Ibid*, p 67.

preferences lead them to assert that the state and/or trade unions will necessarily be able to generate an optimal mix and level of rights independently of the market. In short, the determination of what are the most effective mechanisms or combination of mechanisms for establishing an efficient rights regime is an open question. It is a question that can only be resolved by detailed examination of the specific situation and cannot be merely presumed or deduced solely in the abstracted world and idealised world of the neo-classical free market. In recent years, the argument on the need for government intervention to protect workers' rights has moved from calls for national legislation to demands for effective multilateral regulation linked to countries' access to the international trading system to ensure workers' rights.

International trade and the "core" rights of labour

Much of the opposition to core labour rights has been focussed on the issue of free trade and the need for developing economies in particular to maintain their competitive edge by minimising labour costs. Economists such as Bhagwati have been supported by employers and many governments, especially in developing countries, for this pro-market, free trade stance.

Given the argument for unregulated market forces is hard to sustain under real world conditions where not all factors are fully employed, there are technical and legal barriers to the substitutability and mobility of factors, knowledge is not freely available and markets are dominated by large firms controlling branded and differentiated products. Defenders of the free market use a particular second-best case of free international trade to argue against government intervention on issues such as linking human rights to trade.

The theory of international trade was developed by writers such as David Ricardo (1817),[12] to deal with the situation where relative prices for goods differed between countries and could not be equalised as they would be within a nation state because factors of production (eg, labour and capital) while free to move within a country, could not move freely between countries. Under these conditions, efficiency and welfare could best be increased by free trade in goods which would enable each country to specialise in those products in which they had a comparative advantage. Comparative advantage could result from differences in factor endowments or technology but, as long as it resulted in differing patterns of relative prices, the countries could gain from trade in goods.

12 Ricardo D *Principles of Political Economy* (Penguin Books, Harmondsworth, 1971).

The Stopler-Samuelson theorem holds that trade based on comparative advantage should result in factor price equalisation in the long run as returns to abundant factors rise and returns to scarce factors fall. This is the source of concerns from both developed and developing countries about the impact of trade on labour. In trade between developed and developing economies, labour is the scarce factor and therefore expensive in developed economies and the abundant factor in developing economies, and therefore cheap. Developing countries argue that for them to grow they must take advantage of their cheap labour to gain markets and increase their productivity so that their living standards can rise and they can be internationally competitive against producers in developed countries. Therefore, they have traditionally opposed international standards designed to protect the rights of labour, on the grounds that it would increase labour costs without increasing productivity, and this would reduce their competitiveness. It is the threat of lower wages for labour and in particular for unskilled labour, which has aroused opposition to free trade from trade unions in developed countries and several European governments.[13] Their fears have been supported by empirical evidence that wages for unskilled labour have fallen and jobs have been lost in manufacturing industries in the US and Europe,[14] and this has added to pressure from American and European trade unions for human rights and labour standards to be added to the international trade agenda.

It is not only heterodox economists now who accept that a case can be made that adherence to human rights and labour standards can increase market efficiency. Swinnerton makes a strong case, using standard neo-classical assumptions, that efficiency and therefore the size of the "economic pie" would be increased by action on the defined list of core labour standards. He reviews the argument that "discrimination" is less than optimal for employers and reduces productivity, as well as arguing that child labour is not only against the best interests of the child but also has efficiency costs for an economy.[15]

He also argues that "discrimination" is less than optimal for employers and reduces productivity, as well as arguing that child labour is not only against the best interests

13 See Castle R Chaudhri D P and Nyland C "Labour Clauses, the World Trade Organisation and Child Labour in India", (1997) *Indian Journal of Labour Economics.*

14 Wood A *North-South Trade, Employment and Inequality,* (Clarendon Press, Oxford, 1995) and Wood A "How trade hurts unskilled workers", (1005) 9 *Journal of Economic Perspectives,* Sachs J and Shatz H "Trade and Jobs in US Manufacturing", *Brookings Papers on Macroeconomic Activity,* Washington DC, 1994.

15 Swinnerton K A "An Essay on Economic Efficiency and Core Labour Standards", (1997) 20 *The World Economy,* p 83

of the child, it will also have efficiency costs for an economy. This is related to the argument that adoption of core labour standards can lead to better development of human capital. The economic argument used to justify this is that action on labour standards by developing countries can actually be a win-win situation for labour in developed and developing countries, because action on areas such as the right to bargain collectively, prohibitions on forced and child labour and anti-discrimination measures can raise productivity and therefore offset any extra costs to employers.[16]

The argument on the benefits of collective bargaining Swimmerton derives from the well-known work Freeman & Medoff, *What Do Unions Do?* (Basic Books, New York, 1984), which indicated that unionised labour is more productive than non-unionised labour. This can come about because unions give a "voice" to workers, which reduces industrial disputes and grievances, and therefore increases productivity. If the employer has monopoly power in the product market, then redistribution of some of these gains to labour rather than capital will not affect investment or overall efficiency. In other words, union action which redistributes excess profits earned by a monopolist to labour may actually increase output and productivity if the workers feel that some of their grievances are being met. This is a strong argument for efficiency gains from collective bargaining, especially in the formal sector, in developing countries, where a large number of multinational firms operate, producing for a global market. This is one reason why American multi-nationals, such as Nike, have been willing to enter into voluntary codes of practice affecting workers producing their products in countries such as Vietnam and Indonesia.

It is the formal trade-oriented sectors which in practice would be most affected by the adoption of international labour standards by developing countries. The impact on the informal and small-scale sectors which produce mainly for domestic markets would be small at first but better standards may spread over time as unions become stronger and enforcement of laws relating to labour standards is taken more seriously. This would, in part, meet demands from Western unions that fair trade requires protection for workers as well as for capital. The expansion of international trade laws under the World Trade Organisation to cover trade-related investment measures to protect internationally mobile capital gives moral strength to the arguments of those calling for social clauses which incorporate minimum labour standards, and this can also be justified on efficiency grounds.

A further argument that labour standards can increase efficiency which is accepted even by many neo-classical economists is that such standards may lead to better

16 *Ibid.*

development of human capital. Economists such as Gary Becker[17] have demonstrated the strong link between productivity and investment in human capital through education. Abolition of child labour, if accompanied by measures to ensure school attendance, can increase basic literacy and numeracy skills for labour in any economy and encourage the use of better technology. Child labour is largely confined to backward, low productivity sectors such as agriculture, brick and tile making and building, with only a small minority (about 10%) being employed in the highly publicised manufacturing sector.[18] Even within the manufacturing sector, child labour is largely confined to low productivity industries using old technology, such as in carpet, jewellery and clothing manufacture. While effective restrictions on child and bonded labour might send some of the weakest employers into bankruptcy, it would encourage others to invest in newer technology which requires more highly skilled labour. There is no question that in a poor society, child labour can provide an integral part of family income, but in the long run its abolition will not only benefit the children, it will raise productivity and efficiency in the economy. By removing child labour, which undercuts wages for adults in the informal sector as well as parts of the formal sector, countries will encourage 'fair' employers to invest in new technology and pay better wages to retain the more skilled labour they require to operate that technology.[19]

International action to develop and enforce key labour standards through links to trade is likely to be more effective in raising labour standards than the alternative of leaving it to individual countries. This has been the experience with child labour where countries such as India have long had legislation against child labour, but have lacked both the resources and political will to enforce it until recently.[20] The threat of trade restrictions, either imposed unilaterally by the US using the *Child Labour Deterence Act* (1993) or multilaterally through the WTO/ILO, has reduced the political power of industries which use child labour and is causing countries to reassess the actual benefits from the use of child and bonded labour and the real gains from a lack of reasonable health and safety standards and the absence of free collective bargaining.

Despite the scepticism and opposition of many market-oriented neo-classical economists, there is now some empirical evidence to support those who argue that

17 Becker G *Human Capital and the Personal Distribution of Income* (University of Michigan Press, Ann Arbor, 1967).

18 ILO, World at Work, Special Issue on Child Labour: Global Offensive, No 4, June 1993.

19 Scherrer C "The Economic and Political Arguments for and against Social Clauses", (1996) *Intereconomics* p 11.

20 Castle R Chaudhri D P and Nyland C, *op cit.*

the adoption of core labour standards is not detrimental to developing economies.

It is perhaps surprising that so little empirical work has been done to test the effects of adherence to human rights and labour standards on economic performance. Indeed, the authors of a recent OECD report observed that "economic research in this area is practically non-existent".[21] The OECD study itself recognised the difficulty in determining the degree of enforcement of standards even where these have been legislated, but was able to conclude that improving core labour standards can assist economic growth by increasing human capital and raising productivity. The OECD report found that:

> These results imply that concerns expressed by certain developing countries that core standards would negatively affect their economic performance on their international competitive position are unfounded; indeed it is theoretcially possible that the observance of core standards would strengthen the long term economic performance of all countries.[22]

A pioneering study by Adriana Marshall in the *International Labour Review* examined the link between labour standards and economic performance in seven South American countries in the 1980s. She concluded that:

> During the 1980s when most Latin American countries faced serious obstacles to development, it is not apparent that individual labour law had identifiable effects on the performance of aggregate manufacturing productivity. Factors such as low investment, low labour costs (thus not stimulating labour substitution) regressive restructuring of manufacturing, rationalization of employment and opening up of the economy played a much more crucial role than individual labour law is determining trends in productivity.[23]

These studies provide some support for the growing theoretical acceptance of the notion that the adoption and enforcement of core labour standards is not necessarily deleterious to the economic performance of a developing economy at any level of development and may actually enhance productivity and growth. Much more

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21 OECD, *Trade Employment and Labour Standards: A Study of Core Workers' rights and International Trade*, Paris 1996.

22 OECD, *Trade Employment and Labour Standards: A Study of Core Workers' rights and International Trade*, Paris 1996 13.

23 Marshall A "Economic Consequence of Labour Protection Regimes in Latin America" (1994) 133 *International Labour Review*, p 71.

empirical work is required but ideologically based assertions by economists about the superiority of market forces and liassez faire in achieving labour rights will continue to be challenged on both empirical and theoretical grounds.

Conclusion

The issue of employee rights has been increasingly contentious in recent years both within Western developed nations and between developed and developing countries. As much of the legislative framework developed in Western economies to protect employee rights has come under pressure from increased international competition, unions and some governments have explored new paths that can protect and advance workers' rights in all countries. This followed the assault on existing employee rights by employers as international competition and rising unemployment weakened the bargaining powers of workers and unions in the 1980s and early 1990s. This assault was justified by reference to an Anglo-American version of free market economics which stressed non-intervention by governments and argued that existing worker rights were a barrier to productivity improvement and international competitiveness.

This analysis has been challenged recently by both neo-classical and heterdox economists and this has provided theoretical support for the push by unions and some Western governments for enforceable national and international action on minimum labour rights and for linking of certain minimum labour rights to access to the international trading system. The trade link to labour standards has been championed by the United States and has led to a strengthening of the International Labour Office and a growing international concensus on a list of a core labour standards for countries at all levels of development. This internationalisation of the employee rights agenda offers new hope that labour rights can be maintained and extended in all countries despite the increased competitive pressures raised by globalisation. ●