1. Introduction: the economics of labor and employment law

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The law governing the employment relationship and labor relations is a natural field for the application of economic analysis. At bottom, labor and employment law governs voluntary contractual relations within labor markets and firms. That law is often bound to affect both the price and the cost of labor – whether or not it aims to do so – and thus to affect both the supply of and demand for labor. The price, cost, supply and demand for labor are all crucially important for firms, workers and the society at large. So it might seem inevitable and uncontroversial that economic analysis would make up a major part of legal scholarship in this area.

Although the integration of these two disciplines may have been inevitable, it was hardly uncontroversial. The entry and gradual integration of neoclassical economic analysis into the field of labor and employment law, beginning some 30 years ago, looked very different from the perspective of the two disciplines – law and economics. One reason for early controversy was that the two disciplines were far more distinct 30 years ago than in today’s cross-disciplinary era. The first foray of modern economic analysis into labor law came from a particular wing of economics – one that was far more sanguine about the competitiveness of labor markets, and more critical of the body of labor and employment law that had evolved since the New Deal, than the median labor economist, not to mention the majority of labor law professors. The latter were especially disposed to stress the differences between labor markets and other markets.

Today, however, economic analysis in diverse forms has become widely accepted and integrated into labor and employment law scholarship. This volume reflects both the integration of economic analysis into the field of labor and employment law as well as the diverse forms of economic analysis that take place in the field. By way of introduction it is worth briefly recounting the recent history of economic analysis of labor and employment law, both as it played out in the law schools and as it appeared from the vantage point of modern labor economics. We say “recent history” because economic analysis of a different sort was crucial in shaping labor law in its formative period of the New Deal. We will return to this point below.

The initial foray of law-and-economics scholars of the modern era – what we may call the “Posnerian Era” – into the field of labor law in the early 1980s was fraught with acrimony, but also innovation.¹ For this University of Chicago-based wave of law-and-economics scholars, labor law was emblematic of the ill-conceived New Deal approach to economic activity: It rejected the elegant logic of property, contract, and the market in favor of government-sponsored cartelization of the labor supply (Epstein, 1983, 1984; Posner, 1984). For established scholars in the field of labor law, the intervention of law and economics appeared shockingly oblivious to the history, institutional realities, and values that animated labor law (Getman & Kohler, 1983; Verkuil, 1983). The quest for

economic efficiency seemed to sweep away traditional labor law concerns like labor-management cooperation, industrial democracy, fairness and solidarity.

This acrimony, however, was partly a conflict over methodology. Posner's innovative project was to see how far economic analysis could go to shed light on legal issues. His approach was to take the competitive model, with few transaction costs, as his starting point for legal reasoning. As a benchmark, the predicated competitive outcomes were thus a gauge for evaluating other outcomes. In some areas of law such as contract and corporate law, the new cross-disciplinary approach caught on quickly and with few fireworks. In these fields, the relationship between the primary parties is entirely consensual, and the law provides a set of defaults that the parties can adopt as a low transaction form for contracting. In the economic paradigm, parties can then easily contract around the legal defaults to gain the private ordering that they seek. But the assumption of voluntary relationships within competitive markets is hardly a good starting point for analyzing labor law, where relationships need not be consensual and markets – especially, the internal labor markets where people are actually employed – are not competitive.

In the initial clash of values and disciplines in the early 1980s, labor law scholars and law-and-economics scholars found little common ground, and both retreated to their respective strongholds or moved on to other battlegrounds. But the disciplinary walls had been breached, and labor law scholarship would never be the same. The opening skirmish between labor law traditionalists and the law-and-economics scholars marked a watershed not only in labor law scholarship but in the policy environment for labor and employment issues in the early Reagan era, shortly after the pivotal PATCO showdown.² Economically inspired scholars, particularly those with limited institutional knowledge of the labor market, along with deregulatory policymakers, took the offensive and put the proponents of labor market regulation and of collective bargaining on the defensive. The former had defined a new battlefield with unfamiliar rules of engagement, and the latter had to decide whether to cede that ground or to join the fray – to become conversant with the assumptions and analytical tools of economic analysis.

The academic labor lawyers who decided to join the fray soon found that the Chicago School was far from the last word on the economics of labor markets. Richard Freeman and James Medoff, with their 1984 book *What Do Unions Do?*, introduced much of the labor law academy to more congenial strains of thinking and research within labor economics and industrial relations. Building on the pioneering work of Albert Hirschman, and especially his highly influential (1970) book, *Exit, Voice, and Loyalty: Responses to Decline in Firms, Organizations, and States*, Freeman and Medoff applied the insights to the labor union as an organization and gave a vocabulary to those who sought to defend unions and collective bargaining against the economic critique: Unions promoted worker *voice* in response to discontent, and those voice mechanisms offered a constructive alternative to *exit*, or quitting. Indeed, by rewarding experience, reducing turnover, and inducing workers to share their skills, collective voice (and the job security, seniority protections, and greater benefits that voice allowed workers to secure) could actually contribute to productivity. If unions could raise wages, could they also assist workers in raising productivity to offset the cost of the higher wages?

Freeman and Medoff surveyed the existing empirical research and found some support for a union productivity effect, though not enough to offset the union wage

premium.³ They also made the case for other positive societal contributions of unions such as representation of workers in the democratic political process.

The contributions of Freeman and Medoff on the economics of unions, although perhaps new to those in the field of labor law, were as well known in standard labor economics as were the works of Posner and the Chicago School. Whereas Posner stressed the forces of competitive markets in labor law, Freeman and Medoff helped in part to elaborate the idea that additional factors (both economic and non-economic) outside of the traditional competitive market analysis are important in considering the economic effects of unions. The standard economics model and the similarly standard notion of externalities were now joined. To the labor law scholars who favored collective bargaining as the best regime for governing employment relations (including those who criticized the labor laws from the left for its inadequate support for workers' collective activity), this body of research appeared for a time to offer a simple answer to the law-and-economics critics of unions and collective bargaining: If unions could boost output while increasing workers' share of that output, then society had good reason to promote unionization even though employers might have reason to oppose it.⁴ Beginning in the mid-1980s, Freeman and Medoff quickly became a standard cite in the labor law literature for the virtues of collective voice over exit and the potential productivity benefits of unions, and a standard rejoinder to the law-and-economics critics.

Alas, the positive productivity story suggested by early studies proved to be "overly optimistic," as subsequent empirical research showed productivity gains in the union sector to be small or non-existent (Freeman, 2007; Hirsch, Chapter 4 in this volume). As a consequence any such gains were too small to offset the union wage premium, or the gap between the collectively bargained wage in the union sector and the prevailing market wage, consistent with Freeman and Medoff's conclusion about unions' negative effect on profits. Not coincidentally, the non-union sector of the economy continued to grow and prosper as the union sector declined.

The decline in union membership, well underway by the 1980s, was one of the most important institutional changes in the American economy over the past 60 years. As the slide continued, it became increasingly clear that, if labor unions did provide positive externalities to the American economy and polity, then their protection and promotion would require affirmative societal intervention – and intervention that was strong enough to counter powerful *and rational* employer resistance arising from higher labor costs.

The first comprehensive response to the law-and-economics critique in the legal academy was mounted by Paul Weiler (1990) in his important book *Governing the Workplace*. Weiler was not the first labor law scholar to take up the cudgels, but his extended critique of the Chicago School view of labor markets, and his vigorous defense of the proposition that human labor is different from other factors of production, marked an important point in the evolution of labor and employment law scholarship. Weiler took the economic critique of labor law seriously, and he responded seriously. In the process he helped to familiarize many labor law scholars with currents of labor economics and industrial relations scholarship that could be marshaled in support of laws protecting employees and fostering collective bargaining, and helped to promote engagement among labor and employment law scholars with economic analysis.

The prospects for such engagement were aided by the entry of a second wave of

law-and-economics scholars into the field. Their deeper schooling in contemporary neoclassical labor economics led to more nuanced and less thoroughly critical economic analyses of labor law doctrines (Dau-Schmidt, 1992; Hylton & Hylton, 1989; Hylton, 1993; Wachter & Cohen, 1988; Schwab, 1987). In particular, this group of scholars was more attentive to the nature of internal labor markets, in which firm-specific investments, information asymmetries, and transaction costs were pervasive and labor market competition was muffled. Collective bargaining was recognized as a potential solution to some market failures (even if it had other costs). This second wave of law-and-economics scholarship also corresponded to the rise of “employment law” as a field, and quickly began to shape debates over employment-at-will and its exceptions (Freed & Polsby, 1989; Schwab, 1993, 1996; Verkerke, 1995). Since employers in internal labor markets are only constrained from opportunism by reputational sanctions, there is a greater potential field for welfare-improving intervention in non-union labor markets.

The civil rights laws soon came under economic scrutiny as well, initially in the influential work of Chicago School professor Gary Becker. Becker’s core argument was that personal preferences could and indeed did include preferences for certain racial or ethnic groups over others in personal relationships, but that markets would punish employers that indulged such racialized preferences (Becker, 1957). His conjecture was that, without any legal intervention against discrimination, race-based differences in income would narrow over time as non-discriminating employers found that they could successfully compete by hiring workers scorned by others at lower wage rates. The great bulk of the cross-disciplinary work during this period, however, concluded otherwise. It appeared that history – specifically the history of slavery and Jim Crow – had left deep institutional marks and, in the economists’ terminology, produced sticky Nash equilibria. As in other areas of law and economics, however, the competitive theorizing of the Chicago School garnered much of the attention among labor law scholars.

Richard Epstein’s libertarian-style economic critique of antidiscrimination law (1992) provoked a wave of economically informed and empirically grounded defenses of the antidiscrimination mandate in the legal literature (Donohue, 1992; Issacharoff, 1992; Strauss, 1991; Verkerke, 1992). As new facets were added to the antidiscrimination mandate, they attracted further economic analysis, much of which raised questions about whether the laws were serving their intended beneficiaries or perhaps generating counterproductive labor market responses. Some scholars suggested, for example, that costly legal restraints on discharge or accommodation requirements for certain “protected” groups might induce employers to restrict their hiring of individuals from those groups (Donohue & Siegelman, 1991; Issacharoff & Rosenblum, 1993; Jolls, 2000).

The calculus of private market efficiency, however, was never the ultimate lodestar of economic analysis (although it sometimes seemed so to the legal scholars). Although economists prefer competitive outcomes and policy initiatives based on cost-benefit analysis, they understand that the best outcome is the one that leads to the highest position on society’s social welfare ordering. The theory of the second-best, which was introduced early into the economics paradigm, showed that, in the face of impediments to “first-best” conditions of perfect competition, a move toward “freer” competition did not necessarily promote efficiency. Moreover, economists recognized that society might prefer noncompetitive outcomes on distributional grounds. To well-schooled economists, labor law reforms would still need to be defended on cost-benefit grounds

as the best solution to a well-identified market problem, or forthrightly on distributional grounds; but the idea of reforming labor markets faced no special burden of justification.

By the mid-1990s, economic analysis had become almost impossible for labor and employment law scholars to ignore, and at the same time easier to reconcile with arguments for legal intervention on behalf of employees. It was particularly difficult to ignore the economists' predictions about the unintended labor market consequences of legal interventions for the workers they were designed to benefit. Mandatory benefits such as job security, for example, were predicted to decrease wage levels, employment levels or both. Some forms of antidiscrimination protections – particularly those that required “accommodation,” but also those that significantly increased the expected costs of discharging individuals from protected groups – might effectively tax the hiring of those individuals. The economists succeeded in drawing the attention of legal scholars to the incentives that were likely to drive market actors' responses to regulations and that could defeat or confound well-intentioned reforms.

As more researchers entered the cross-disciplinary field, it was only natural that a broader view of the economic model would replace a strict adherence to the perfectly competitive version. The economic analysis of transaction costs, public goods and collective action problems, information deficits and asymmetries, and the like have all been standard fare within labor economics since the 1970s; but they did not filter into economic analysis within the legal academy, at least in labor and employment law, until after the first Posnerian foray. Armed with those concepts, it became easier to deploy economic analysis in the defense of some existing and proposed policy interventions. It became increasingly clear to legal scholars in the 1990s and thereafter that economic analysis was no longer a one-way ratchet against legal intervention in markets, nor did it necessarily entail swearing fealty to the goal of efficiency above all.

Economics has always been a mixture of theory and empirical work; and as labor law researchers adopted a broader range of economic models, they adopted econometric analysis as an important tool. Models, conjectures, and institutional details need to be tested to see if they are predictive of how labor markets function. This work has included methodologically sophisticated data-driven studies of litigation behavior, judicial decisions, and the economic correlates of legislation or other legal developments. These empirical studies have sometimes confirmed and sometimes confounded the predictions of theorists, and have sometimes contradicted each other, for example, with regard to the economic consequences of judicial erosion of the employment-at-will rule. Facts rarely speak for themselves, and theory does not readily surrender to empirically based challenges, which are often clouded by methodological disputes. But facts and data have always brought about significant changes in economic theory across the board, notably in labor economics.

Three major and interrelated scholarly currents have also compounded the heterodoxy of economic analysis of legal rules, doctrines and institutions, both in the field of labor and employment law and beyond. One major scholarly development that has complicated and fragmented the field of law and economics – the rise of behavioral analysis – may turn into a case study of the power of facts to alter theory (though the jury is still out). Based on a growing multitude of laboratory and field experiments, behavioral scholars have drawn attention to a collection of tendencies in actual human decision making that diverge in somewhat predictable ways from the “rational actor”

model on which neoclassical economic theory is based (Jolls, 2007; Jolls, Sunstein & Thaler, 1998). Evidence of widespread patterns of “bounded rationality,” “bounded will-power,” and “bounded self-interest,” for example, helped to enrich the law-and-economics field, questioning the realism of neoclassical economic theory and blunting or contradicting many of its policy prescriptions in the labor field as elsewhere (Sunstein, 2001; Williamson, Wachter & Harris, 1975). Some consumers of behavioral analysis seemed to take this new research as a grab bag of justifications for “paternalistic” forms of legal intervention; some of the behavioral scholars themselves were more cautious in their prescriptions (Camerer et al., 2003; Thaler & Sunstein, 2008).

Two other related scholarly currents that have enriched the field of law and economics are the rise of game theory and the role of “norms.” Norms shape behavior in ways that seem both to defy the “rational actor” model and yet to facilitate private ordering. The power of norms of fairness and reciprocity in shaping human behavior was widely observed, both in laboratory experiments and in the world, including in the workplace; and those norms were seen to play an important role in sustaining the trust and cooperation on which many actual markets depended. These observations seemed to pose a serious challenge to the rational actor model at the heart of neoclassical economic theory. In one way, game theory came to the rescue, and allowed economic theorists to reclaim trust and cooperation as rational, at least among “repeat players.” That had important implications for the workplace (Rock & Wachter, 1996). At the same time, game theory and the norms literature played a potentially subversive role, for they reintroduced squishy concepts of fairness, trust and reciprocity that had been virtually banished from economic discourse in the early years of the law-and-economics revolution.

The growing influence of these newer currents in economic research and thought has made law and economics a far richer and more diverse intellectual stream than it was in the 1970s and 1980s. That has been true across the board – in the law and economics of corporate governance, consumer law, contracts, torts, property, criminal law and civil procedure – indeed, everywhere that clever and ambitious young legal scholars ply their trade. But the heterodoxy of economic analysis in the field of labor and employment law has additional roots in the field of labor economics and its role in the history of labor and employment law.

Labor economics has always been open to the rich institutional realities of the labor market. The great labor economists of the 1950s and 1960s, including John Dunlop, Clark Kerr, H. Gregg Lewis, Mel Reder, and Albert Rees, were also institutionalists who borrowed from neoclassical theory to enrich their view of the functioning of labor market institutions. It was primarily these economists who were instrumental in shaping the origins of modern labor and employment law in the U.S. Indeed, from the foundational days of economics until the current period, the study of labor issues by the giants such as Adam Smith, Thomas Malthus, Karl Marx, and John Commons has always been rooted in institutionally grounded hypotheses. The ascendancy of pure economic theory was a short-lived episode in labor economics.

In the decisive New Deal battles in which both modern labor law and the beginnings of modern employment law were forged, the then-ascendant institutionalist economic thinkers joined forces with legal realist scholars to contend for the legitimacy and wisdom of both legal support for collective bargaining and legislation of minimum labor standards (Kaufman, Chapter 3 in this volume; Hovenkamp, 2011). Although the

modern neoclassical theory of labor markets and wages was percolating during the New Deal and was about to transform economic thinking about employment relations, the institutionalists' pivotal policy role and the durability of some of the reforms that they advocated during the New Deal probably helped sustain a greater diversity of views among labor economists, compared to the rest of the economics field. This integration of theory and institutions was repeated in the 1960s and 1970s when labor economists, using cost-benefit analysis, argued forcefully in favor of many programs such as employment training, antidiscrimination policy, and welfare reform, while arguing against some reforms of the New Deal, such as industry-specific labor rules, believed to have outlived their usefulness.

Still, there are divisions between economists and most labor law scholars. Consider for example, the proposition that individual employment relations are plagued by an "inequality of bargaining power" between workers and employers. The generalized "inequality of bargaining power" claim is a *bête noire* of most neoclassically trained economists (see, e.g., Schwab, 1997; Wachter & Wright, 1990). In neoclassical analysis, external labor markets are considered competitive or competitive enough so that a worker's "bargaining power" depends on cyclical labor market conditions and supply and demand for his particular skills. Some workers have significant bargaining power. Yet at least in the midst of the Great Depression, the proposition that employers generally had more bargaining power than employees seemed self-evident to many observers, and it was a founding premise of the New Deal labor legislation.

The idea of unequal bargaining power continues to appeal intuitively to many citizens, and it continues to animate much of labor and employment law policy and scholarship.⁵ Indeed, it remains enshrined in the U.S. Code: The preamble to the National Labor Relations Act (NLRA) declares that there is an "inequality of bargaining power between employees who do not possess full freedom of association or actual liberty of contract, and employers who are organized in the corporate or other forms of ownership associations."⁶ Of course, saying this does not necessarily make it so, even if Congress is the one saying it. Congress' particular conception of the inequality of bargaining power and how to redress it is in fact the subject of close and critical scrutiny in the present volume (Wachter, Chapter 2 in this volume).

The remarkable staying power (or "ossification") of the NLRA in particular – if not of its collective bargaining model of labor relations – is testimony to the fact that labor economists have always needed to study institutions in order to understand the workings of markets and to be able to propose reforms. Although the NLRA has many negative features in the eyes of economists, the number of economists who favor repeal of the Act is very small. It is the libertarians rather than the economists who want wholesale repeal of labor and employment law. Economists recognize that the difference between mostly competitive and perfectly competitive markets is vast in terms of its policy implications.

Neoclassical economic analysis has been enriched by its attention to transaction costs, the lessons of game theory, the importance and robustness of norms, and even the complications of behavioral economics. Some of the major innovations in neoclassical labor economics since the 1960s underscore the proposition that human labor is different from other factors of production. For example, the "efficiency wage hypothesis" posits that paying workers more than the "competitive" market wage can elicit greater work effort – out of both loyalty and reciprocity to the firm and a stronger incentive to keep

the better paid job – which can potentially pay for itself in the form of higher productivity. The theory, and the underlying idea that trust, reciprocity and cooperation among workers and managers are major factors in labor productivity, is widely accepted by labor economists (at least in the non-union sector).⁷ Moreover, the labor economist's elaboration of the market failures that are endemic within internal labor markets opens the theoretical door to legal interventions that could improve efficiency and fairness in employment relationships.

In assembling the present volume, we have taken a broad view of “economic analysis” of labor and employment law. We include producers of economic theory and of empirical research and neoclassical and institutional economists. We include scholars whose training and primary point of departure is in economics and positive economic analysis of legal rules, as well as scholars whose training and focus is more normative and attentive to the economic consequences, predicted in theory or demonstrated empirically, of policy interventions.

We begin, and complete Part I of this volume, with two accounts of the economics of labor markets and some of the policy implications of those accounts. The first is by Michael Wachter on the modern neoclassical economic theory of labor markets. The second, by Bruce Kaufman, offers a counterpoint in the form of a range of skeptical observations about the neoclassical account of labor markets, especially the “Chicago School” account, from the “institutional” or industrial relations perspective. Both accounts are attentive to the transaction costs and other frictions that may skew real labor markets from the competitive ideal, but they differ sharply on the extent to which these various “market failures” interfere with the competitiveness of external labor markets in the U.S. Wachter shares the consensus view within neoclassical economics, that external labor markets are basically competitive but that market imperfections are endemic to internal labor markets. Kaufman, on the other hand, sees market failure as pervasive in labor markets, both internal and external. Wachter shares the economists’ “rebuttable presumption” in favor of labor market outcomes; thus, while he considers many legal mandates to be justified on efficiency grounds or otherwise, he resists legal enforcement of the terms of employment-at-will contracts and contends that non-legally enforceable norms can be effective in ensuring basic fairness within internal labor markets. Kaufman, by contrast, indulges no presumption in favor of market outcomes given the systematic advantages employers have over workers. From these two accounts and their engagement with each other, readers can discern the main lines of agreement and disagreement between the dominant and recessive wings of labor economics.

Parts II and III track the familiar division between “labor law,” or the law of union organizing and collective bargaining, and “employment law.” In Part II, we take up the field of “labor law.” We begin with Barry Hirsch’s comprehensive analysis of the economic literature – and particularly the empirical evidence – on the impact of unions on economic performance of firms. The picture is not encouraging for organized labor. Significant union wage premiums, and little or no offsetting productivity gains, reduce the profitability and competitiveness of union firms and facilities, and reduce investment in those facilities, with the inexorable result of declining union density. This economic story does not refute so much as it helps to explain intense management opposition to unionization, which in turn contributes to declining union density.

On Hirsch's account, the data do not support the more hopeful scenario of union productivity gains in a cooperative labor relations climate; but neither do they rule out that scenario. When non-union labor relations as well as management opposition to unions become the norm, cooperative collectivized labor-management relations become exceptional and precarious, especially in dynamic and growing sectors of the economy. Hirsch's chapter underscores the challenge that unions face in the U.S. labor law regime, which, unlike many European labor law systems, does not attempt to take wages and other labor costs out of competition, except at the very bottom of the market. The chapter also underscores the difficulty in such a labor law regime of realizing workers' right to form unions and engage in collective bargaining, to which U.S. public policy remains formally committed.

The next two chapters take up that issue from two radically different perspectives on the law of union organizing. Benjamin Sachs offers a novel analysis of what is wrong with both the current law of union organization under the NLRA *and* with the leading (and lately defeated) reform proposal, the Employee Free Choice Act (EFCA). Building on the recognition that union organization can be seen as an effort to alter the "default" status of no union representation, Sachs mines a rich literature on defaults and default-altering rules in statutory interpretation and in corporate governance to illuminate the problem of realizing employee preferences regarding union representation. The basic problem lies in the asymmetric stickiness of the non-union default, which stems from both strong employer opposition to unionization and the collective action problems that employees face in countering that opposition. Sachs argues that the law's neutrality regarding employees' free choice regarding unionization calls for the adoption of an "altering rule" – or a union organizing process – that corrects for the asymmetric stickiness of the non-union default by minimizing employer intervention in unionization campaigns. At the same time, and to the likely chagrin of EFCA supporters, Sachs questions the virtue of an open (versus secret) *decision making* process such as card check, which does not reduce the role of employer intervention but does potentially allow for interference with employee choice from the pro-union side. In closing, Sachs briefly previews the sorts of labor law reforms that would maximize employee free choice under his analysis.

Richard Epstein approaches much the same territory from quite another point on the political spectrum, reaching sharply different conclusions. His characteristic no-holds-barred blend of libertarianism and economic analysis leads him to a highly critical account of existing labor law, and an even more critical view of the major recent labor law reform proposals, including the recently deceased EFCA. He celebrates the failure of that proposal, which he contends would have made a bad law worse in terms of its interference with individual contractual liberties and its impact on the economy. Epstein would return, rather, to the pre-New Deal "common law for labor relations" (Epstein, 1983), including the "yellow-dog contract" and the right of employers not only to refuse to deal with unions but to refuse to employ union members. He would return, in short, to the liberty of individual contract within barely regulated labor markets.

The remaining two chapters in Part II begin to touch on issues of employment law as well as labor law. Morris Kleiner and David Weil compare remedies under the NLRA with remedies under other labor statutes, as well as with the demands of "deterrence theory," and find the remedies under the NLRA to be seriously deficient. In short, a rational employer who weighs the expected economic consequences of unionization

against the paltry remedies that may follow an illegal campaign to discourage unionization will not be much deterred from violating the law. The Kleiner and Weil chapter explores one set of implications of the economics of unionization (which the Hirsch chapter develops at greater length) for a public policy that purports to enable employees to choose unionization in the face of employer opposition. The chapter also illustrates one way in which the “rational actor” model, and simple assumptions about the economic incentives that drive private market actors, may support stronger public intervention in private behavior. If we take as given the law’s definition of certain conduct as wrongful, such as anti-union discrimination, the standard deterrence model may support stronger remedies or enforcement policies.

Stewart Schwab’s chapter explores a potential role for unions as “brokers” of their members’ employment law rights. By serving as gatekeeper to greater flexibility in the terms and conditions of employment, and to a less costly and disruptive means of adjudicating employment law disputes, unions might be able to offer something of value to both employers and workers. Schwab usefully reviews the economic and non-economic rationales for existing employee rights and labor standards laws, explaining how the logic of those rationales tends to dictate the non-waivability of the protections. For example, if a workplace safety law aims to secure public goods for workers, it does not make sense to allow individuals to waive those protections, for that would reintroduce the very collective action problems the law was designed to avoid. In some cases, however, unions may be able to overcome those problems and to waive legal rights only when doing so makes workers better off in the exchange. Schwab explores a range of cases in which union waiver of employment rights is permitted under existing law, and contends for a cautious expansion of this strategy for introducing flexibility and vitality into the law.

In Part III we turn directly to the field of employment law – once the arriviste and now the dominant component of the labor and employment law field. Employment law is obviously a diverse field, but much of it consists of mandates which can usefully be sorted into two categories: minimum labor standards such as the Fair Labor Standards Act (FLSA), the Occupational Safety and Health Act (OSHA), and the Family and Medical Leave Act (FMLA); and individual employee rights such as those embodied in Title VII of the Civil Rights Act and other antidiscrimination statutes, various anti-retaliation statutes and doctrines, and a smattering of employee liberties and privacy rights. The economics of employer mandates has long been grist for the law-and-economics mill.

At the heart of employment law, however, is the employment contract; and at the heart of the employment contract in the U.S. is the reigning presumption of terminability-at-will. Employment-at-will, and the employer’s power to condition continued employment on acceptance of its chosen terms, makes the employment contract largely modifiable at will and non-legally enforceable. Employment-at-will also sets the default position against which all employer mandates, employee rights, and constraints on “wrongful discharge” operate. Indeed, the distinctively American proliferation of antidiscrimination and anti-retaliation laws and doctrines, as well as wrongful discharge litigation, are historical by-products of the employment-at-will default rule, which in its original and absolute form tolerates the exercise of employer power that society has found to be intolerable. Economic analysis has long been a major element of debates between the defenders of employment-at-will, more or less absolute, and the proponents of some

version of “just cause” protection that prevails in nearly every other developed country in the world.

We begin the book’s treatment of employment law from a methodological perspective. Christine Jolls’ chapter, “Bias and the Law of the Workplace,” looks at some major features of the employment law landscape through the lens of behavioral economics, and in light of well-documented deviations of actual human cognition from the “rational actor” construct at the heart of neoclassical economics. In particular, she shows how the law of the workplace sometimes works – and might work better – by reducing or counteracting widely shared cognitive biases. For example, the law of employee handbooks might respond to “optimism bias” in employees’ apprehension of disclaimers, and better alert them to their lack of legally enforceable job security, by requiring employers to include actual examples of unjustified discharges that courts had found to be lawful. Turning to the stubborn problem of implicit racial biases, Jolls shows that the law of employment discrimination already does help to reduce such biases, most importantly by increasing workforce diversity. Exposing potentially biased individuals to African-American (or female) co-workers – or even to positive images of African-Americans or women – can reduce not only conscious biases, as the venerable “contact hypothesis” would have it, but implicit or unconscious biases as well. Through her exploration of a few bodies of behavioral research, and their implications for a few crucial areas of employment law, Jolls shows the broad potential value of behavioral economics in improving the law’s capacity to achieve its goals.

Rachel Arnow-Richman’s chapter, “From Just Cause to Just Notice in Reforming Employment Termination Law,” focuses directly on the law of the employment contract and the debate over employment-at-will. Finding the debate to be at a bit of a stalemate, Arnow-Richman charts a new direction for reform. She observes that much of the critique of employment-at-will is based on the burden and dislocation that a summary discharge visits upon the employee, while much of the defense of employment-at-will revolves around the difficulty and cost of reviewing the employer’s reasons for discharge – costs that would likely be passed on to employees. She argues that both concerns can be addressed by shifting the goal of reform from “just cause” to “just notice” – from allowing employees to contest the adequacy of the employer’s reasons for discharge to guaranteeing employees a fair period of advance notice, or payment in lieu of notice, during which they can find their next jobs. Arnow-Richman argues that a “just notice” regime would entail much lower administrative costs than a “just cause” regime, and arguably lower than the existing “at-will plus exceptions” regime (although higher than a hypothetically pure at-will regime that almost no one currently defends). Moreover, a “just notice” regime would benefit not only the fraction of employees who are fired without adequate cause, but also the many more employees whose jobs are eliminated for economic reasons. Arnow-Richman brings a comparative dimension to the debate, not only to point out the familiar fact that U.S. law is a lonely outlier in its adherence to employment-at-will, but also to explore the Canadian experience with what amounts to a “just notice” regime.

Simon Deakin approaches the same set of issues from an empirical and comparative perspective in his chapter, “The Law and Economics of Employment Protection Legislation.” Deakin traces the law-and-economics analysis of “employment protection laws” (EPL) – that is, unjust dismissal laws and laws relating to lay-off and redundancy

– through a series of stages. “First generation” analyses were highly critical of EPL as an inefficient and unjustified imposition on party autonomy. “Second generation” analyses reflected the teachings of modern neoclassical labor economics on transaction costs, asymmetric information and adverse selection, and produced a more mixed assessment of the economic impact of EPL. A “third generation” of “evolutionary models” builds on the “varieties of capitalism” literature, and views the varying approaches to EPL as “endogenously generated solutions to coordination problems arising in labour markets.” That is, different nations’ labor market institutions generate different solutions to the problem of dismissals and redundancies. Based on a review of recent empirical studies of EPL, which use new time-series datasets to supplement earlier cross-sectional studies, Deakin finds qualified support for an efficiency case for EPL-type interventions, at least in certain institutional contexts and under certain market conditions. For example, job security protections may contribute to productivity and innovation at the firm level by complementing and reinforcing a commitment (by trade unions, employer groups and government) to training and workforce development.

Alan Hyde focuses not on legal restrictions on employers’ power to discharge employees but on contractual restrictions on employees’ right to quit and compete with the employer. The latter are closely intertwined with the definition and allocation of property rights to the information that employees acquire and enhance through employment. Hyde’s review of the extensive empirical literature on innovation, growth and employee mobility finds a striking consensus: “This literature finds *no* provable social advantages in intellectual property-based restrictions on employee mobility.” Indeed, limiting employers’ proprietary claims to workplace know-how and their power to restrict employee mobility – as California law does, for example – is associated with greater innovation and economic growth.

It is interesting to compare the Deakin and Hyde chapters. In some respects the two studies reinforce each other. Both review an extensive empirical literature and reach conclusions at odds with the predictions of first-generation law-and-economic analysis. The latter in both cases had come down firmly on the side of “freedom of contract,” and for allowing employers both to freely fire their employees and to restrict their employees’ mobility. Deakin and Hyde both find that restricting employer power – to fire employees or to restrict their mobility respectively – can promote economic growth and innovation (although Hyde is far more categorical in his conclusions than Deakin).

If we focus on the relative value of job stability and job mobility, however, the two studies seem to point in opposite directions, at least at first blush. Hyde’s strong conclusions about the economic benefits of unrestricted employee mobility may seem to be at odds with Deakin’s more qualified claim that job security and stability may promote productivity and innovation. Or perhaps there is an efficiency case to be made – at least in some industries and some institutional settings – both for ensuring employees’ freedom to voluntarily move from one job to another and for legally restricting employers’ power to discharge employees. There is no logical inconsistency – though there may be an irony in some eyes – in the notion that ensuring both employees’ freedom to quit and their freedom from unjustified discharge, against employers’ contractual claims to the contrary, might serve larger societal interests. At the very least these two chapters illustrate the vigor and heterodoxy of modern law-and-economic analysis.

Turning next to employment discrimination law, Samuel Issacharoff and Erin Scharff

in their chapter, “Antidiscrimination in Employment: The Simple, the Complex, and the Paradoxical,” argue that employment discrimination law encountered increasing strain as it progressed from Title VII’s relatively straightforward attack on irrational discrimination to more redistributionist challenges to some forms of economically rational discrimination. Initially with the advent of disparate impact doctrine, then with the extension of the antidiscrimination mandate to older, pregnant, and disabled workers, and finally in the rise of explicit demands for accommodation, it became increasingly clear that employers were expected to bear significant costs in order to improve the employment prospects of some economically disadvantaged groups. But employers operating within markets cannot be expected simply to absorb those costs; they will try to avoid them or to pass them on, and in either case the losers may be the very groups the law sought to benefit. So, for example, if legal demands for accommodation of disabilities are made largely by incumbent employees, employers might rationally avoid hiring disabled workers. This result may be illegal but it is very hard to prove and rarely litigated.

Issacharoff and Scharff stress that, where society seeks to alter employment practices that are economically rational, it must consider how employers are likely to respond, and it may have to explicitly engineer the distribution of costs to avoid counterproductive responses. A forthright reckoning with the costs of promoting equal employment opportunity – and sometimes the use of vehicles other than antidiscrimination law, such as social insurance schemes – will allow society to better achieve its equal employment objectives.

The final chapter of Part III, Samuel Estreicher and Zev Eigen’s “The Forum for Adjudication of Employment Disputes,” elaborates another aspect of the costs associated with employment rights. Forum and process obviously affect the cost of adjudicating rights claims, and are obviously critical to the realization of whatever rights the law confers on parties to the employment relationship. The direct costs to employee-claimants affect employees’ ability to vindicate their formal legal rights; that takes a toll especially on low- and middle-income workers. Some of those costs may be shifted to losing employer-defendants, but whatever adjudication costs are borne directly by employers may in turn be shifted back to employees in indirect forms, through lower wage packages or reduced employment. To be sure, the high cost of being sued – including the forum-related costs of litigation – can help to motivate employers to comply with the law. But employers’ efforts to avoid costly litigation may take either productive or counterproductive forms.

Estreicher and Eigen are on balance critical of the heavy reliance on courts, juries and lawyers in U.S. employment law. In principle that reliance is counterposed by the traditional use of arbitration within the once-robust collective bargaining sphere, and the availability of administrative agencies for some rights enforcement. But in view of the ever-shrinking scope of collective bargaining and the chronic underfunding of administrative agencies, Estreicher and Eigen argue that the real alternative to the costly and slow judicial forum lies in employer-initiated arbitration and other dispute resolution systems. They review the main currents of controversy over mandatory arbitration, and come down in favor of preserving and improving these private dispute resolution systems. They close with suggestions for reform, including some that can be achieved through private ordering (such as improvements to the influential Due Process Protocol

to which reputable employers and arbitrators largely adhere) and some that borrow from recent experience in the United Kingdom.

Part IV closes the volume with two economically inflected perspectives on the field, one from each of the editors, both of which straddle the divide between labor law and employment law. Michael Wachter's ironically titled chapter, "The Striking Success of the National Labor Relations Act," begins in the cauldron of widespread and often violent labor conflict in which the NLRA took shape, but concludes with the resurgence of a non-union sector that has met workers' needs, at least well enough, to virtually eliminate serious industrial unrest. On Wachter's account, the NLRA ultimately accomplished its most widely shared, abiding and coherent objective of "industrial peace." But it did so, not so much by supporting unionization and collective bargaining as the original Wagner Act set out to do, but by curbing union power and allowing the emergence of a robust non-union sector that was almost inevitably able to outcompete unionized firms in an increasingly competitive economy. As for the other major objectives of the Wagner Act, "industrial democracy" and increasing employees' bargaining power through union representation, they were plagued from the start, says Wachter, by a built-in contradiction: The more unions increase employees' bargaining power and deliver a wage premium, the more they raise the costs and hurt the competitiveness of unionized employers, thus depressing union density and the spread of "industrial democracy" through collective bargaining.

The contradiction that Wachter identifies between increased union bargaining power and wider union representation is not universal to all labor relations systems. Wachter's primary thesis is that the workings of today's labor markets are largely a product of political choices in favor of freer market competition. After a brief failed experiment with corporatist coordination of wages and prices under the National Industrial Recovery Act, the movement from "fair competition" to "free competition" progressed with the gradual dismantling of industry regulation in transportation, communication and utilities, and the increasing commitment to free trade and globalization of product markets. But among the crucial political choices was the choice in 1947 to curb organized labor's strongest economic weapons, and thus to curtail both its ability to disrupt commerce and its ability to extend its organizing gains across the primary sectors of the economy. Thereafter, neither corporatist coordination nor industry regulation nor private collective action was going to take wages out of competition. Thus the die was cast and the long slide in union density began.

Wachter's account is a depressing one from the perspective of organized labor in the United States. Whether it is depressing to most American workers turns on the soundness of his relatively sanguine portrayal of modern non-union workplace governance. More sophisticated and worker-friendly human resource (HR) policies, and self-enforcing informal norms of fairness, have managed to keep workers at least satisfied enough to keep them in the non-union fold – that was a major purpose of those policies, after all – and to keep them from taking to the streets in large numbers. Sure, many non-union workers say they would like to have a union or some other kind of collective representation; but most of them do not seem to feel strongly enough about it to trigger the NLRA's process for union recognition, which nowadays functions largely as a kind of pressure valve to keep workers' discontent from spilling into more disruptive forms. Labor peace thus prevails.

Estlund's chapter, "Why Workers Still Need a Collective Voice in the Era of Norms and Mandates," takes a less sanguine view of the non-union workplace, at least for workers who lack scarce and valued skills and in firms with relatively little reputational capital. For employees at and below the middling levels of the labor market, there is evidence of widespread noncompliance with basic labor standards, deteriorating real wages, benefits and job security, and workplace pressures that are unbuffered by the internal labor market norms that supposedly protect workers in the non-union workplace. Estlund is also doubtful that employees' option of unionization is robust enough to activate the "union threat effect" that, on Wachter's account, helps to back up norms of fair treatment. As per Sachs' chapter, employers' aggressive resistance to unionization – economically rational though it may be – makes it enormously difficult for employees to choose union representation and collective bargaining.

If we purport to ensure employees' free choice regarding unionization and collective bargaining, and particularly if we rely on that free choice – and the real threat of unionization – to induce non-union employers to behave decently, the law must do more to restrain employers' use of threats and coercion – sticks rather than carrots – to discourage unionization. Otherwise, "labor peace" may signify not employee contentment and basically fair and decent working conditions but rather resignation in the face of employer resistance and powerful market forces and pessimism about the utility of collective action and the reality of the rights the law purports to grant employees.

In the end, what unites the contributions to this volume, and all that unites the varieties of economic analysis in labor and employment law, is that market forces – in labor markets, product markets, and capital markets – are powerful and cannot be ignored. Those forces both drive and constrain employer behavior in workplace governance, even as employers make choices that govern workers' lives. Market forces shape employer responses to, and thus the consequences of, legal rules – though not invariably as the economics textbooks would predict. Whatever goals policymakers pursue – redistribution, fairness, equality, or even efficiency, economic growth or innovation – they will be well served by serious attention to the economic incentives that operate on market participants and the aggregate consequences for economic performance and growth.

NOTES

1. One of us later described that initial confrontation, somewhat tendentiously, thus: "With the temporary zeal of missionaries, and with as little respect for the local culture, several law-and-economics scholars brought the harsh logic of the neo-classical gospel to . . . labor law and found it hopelessly mired in rent-seeking" (Estlund, 2002).
2. After the Professional Air Traffic Controllers Organization (PATCO) launched an illegal strike in 1981, President Reagan fired over 11,000 striking air traffic controllers. The incident is often credited with emboldening U.S. employers to take a more aggressive anti-union stance, and particularly to resort to permanent replacement of lawful economic strikers (e.g., Wachter, 2007, pp. 617–18).
3. Most empirical research on this point has found little or no net impact of unions on productivity (Hirsch, Chapter 4 in this volume). An important mediating variable may be the quality of labor relations: In a cooperative labor-management relationship, the positive effects of unionization might outweigh the negative, while labor-management conflict takes a toll on productivity in a variety of ways. In either case, however, the lower profitability of unionized firms and facilities has been associated with lower investment of capital and lower growth in those firms and facilities, and with the relative shrinkage of the unionized sector. *Id.*

4. The claim met skepticism in the law-and-economics camp: If unions boosted productivity, then employer resistance to unions was irrational – and that could hardly be the case (Posner, 1984). The answer to that “puzzle” was simple enough; unions increased wages and benefits by more than they increased productivity, and thus reduced profits. That answer both explained employer resistance to unions and foretold a gloomy outlook for the success of unionized firms insofar as profits were needed to thrive or even survive in competitive product and capital markets.
5. For thoughtful defenses of the “unequal bargaining power” thesis, see Michael H. Gottesman (1991) and Kaufman (Chapter 3 in this volume).
6. National Labor Relations Act, 29 U.S.C. §151.
7. Freeman & Medoff’s theory of how unions can promote greater productivity can be seen as a variation on the efficiency wage hypothesis for the union sector. In general, the idea of efficiency wages has been more salient in the non-union sector. Higher wages are said to generate employee loyalty to the non-union employer, and greater work effort in return. In the union sector, the union claims credit for higher wages, thereby weakening the workers’ motivation to reward employers with greater effort.

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