

DISCUSSION PAPER SERIES

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## ABSTRACT

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### **Worker Representation\***

We define worker representation, identify the factors that determine demand for it among workers and employers, discuss difficulties in supplying worker representation, and reflect on the implications of worker representation for worker welfare and the behavior and performance of employers.

**JEL Classification:** J5, J51, J52, J53, J83

**Keywords:** worker representation, unions, collective bargaining, voice

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## 1. Worker Demand for Representation

When a worker enters a labor contract with an employer she is offering to sell her labor power in return for a wage. In doing so, she is acting as an agent for an employer (the principal) to undertake stipulated tasks under the contract for a given period, but that contract is ‘incomplete’ in the sense that it is not normally possible for the contract to specify the terms of the exchange in an exact way (Simon, 1951; Williamson, 1975). Those terms are liable to be contested if worker and employer interests are not wholly aligned. This is the case in principal-agent theory where the agent’s utility function departs from that of the principal, as might be the case where worker effort is costly (Jensen and Meckling, 1976), and under more radical Marxian theory in which the contract is struck by parties with unequal power due to the principal’s ownership of capital. In the former case, an alignment of interests might be partially achieved where an employer rewards a worker’s marginal product through performance pay (Prendergast, 1999), albeit subject to a command-and-control basis for the exchange in which the employer can dictate most aspects of the contract including the constitution of the ‘job’ (its tasks, location etc.) and other aspects of the exchange. In the latter case, those interests can only be realigned through a fundamental reframing of the whole employment relationship.

Workers may seek representation vis-à-vis the employer if grievances or disputes arise regarding the terms of the contract and its interpretation or enforcement, if the employer wishes to consult workers over aspects of their employment, or if changed circumstances merit the renegotiation of the contract. In the absence of representation, the employer may seek to alter or add to the incomplete contract, subject to an individual’s own bargaining power, and an aggrieved employee’s only recourse is to resign.

Representation can therefore be beneficial from the workers' perspective in effectively aggregating and conveying worker preferences to the employer ('voice') or in strengthening workers' bargaining position vis-à-vis the employer, as might be the case where workers are able to threaten the collective withdrawal of their labor ('monopoly'). These two functions of worker representation, labelled the 'voice' and 'monopoly' faces by Freeman and Medoff (1984) (henceforward F&M), may generate worker demand for representation, but its supply is not guaranteed.

## 2. Problems of Collective Action

F&M assumed worker representation would take the form of a trade union, namely a voluntary association of workers, independent of the employer, constituted for the purpose of representing workers' interests. However, although trade unions are often constituted in response to worker demands for representation, the 'good' they offer in the workplace – which may come in the form of better working conditions and pay, or more equitable treatment of workers - is largely a public good. It is rarely a private excludable good solely benefiting those paying the fee to be a union member.

The absence of private excludable goods means workers behaving rationally might prefer to 'free-ride' on the organizing efforts of others rather than invest their own time and effort in forming a union. This incentive problem, which can limit the supply of worker representation by a union, is what Olson (1965) termed the first order problem of collective action. It can be overcome with state intervention supporting a 'closed shop', whereby union membership is effectively

compulsory to undertake a job in a union covered environment, but such arrangements have been outlawed in many countries. It can also be overcome through provision of private incentive goods dependent on membership, such as the insurance worker representation can offer against employer abuse of power.

The second order problem of collective action limiting the supply of union representation, also identified by Olson (1965), is the cost to the union of servicing its members' needs. Where the marginal costs exceed the marginal returns, unions may choose not to supply representation even where those workers demand it. One solution in this case is for unions to supplement their ranks of paid union officials by recruiting workers to act as lay representatives, performing the worker representation task at the behest of the union without payment, sometimes with support from the State or an employer, to fund time required for worker representation tasks (Willman et al (2020a) call this 'off balance sheet resourcing').

### 3. The Potential Value of Worker Representation to Employers

Employers may also benefit from worker representation. For instance, dealing with workers collectively via their representative(s), rather than separately, can reduce the transaction costs incurred in workplace governance and labor contract monitoring and enforcement. Employers may also find worker 'voice' pro-productive where it facilitates efficient production, solves information asymmetries, or leads to positive spillovers in the way workers feel about their jobs (in the form of commitment, loyalty and satisfaction).

If worker representation helps resolve workers' problems it offers a credible alternative to quitting, thus lengthening tenure and increasing employer returns to their investments in workers' human capital. This can be particularly beneficial to firms with skilled workers who are costly to replace.

On the other hand, if workers use the bargaining power acquired through effective worker representation to the employer's detriment – for example, to block or limit capital investments (the 'hold up' problem) - this may adversely impact firm performance.

#### 4. The Changing Nature of Worker Representation and 'Voice'

Employers with an interest in worker voice have a choice as to whether to invest in producing mechanisms capable of generating that voice or to contract out the provision of that voice to a third party, such as a union - what Willman et al. (2020b) describe as the employer's 'make or buy' decision. These 'voice' options are not fully substitutable because forms of voice other than union representative voice rarely engage in bargaining over terms and conditions with the employer. For this reason, in many cases union and non-union forms of worker representation and voice can co-exist at the workplace ('dual' channel voice, or what Willman et al. (2020b) describe as 'hedging').

The demise of union forms of worker representation, apparent in many parts of the world (OECD, 2017), may be due, at least in part, to the reduced effectiveness of unions as agents for employers in the provision of worker voice. This may have arisen due to declining union membership, and thus difficulties in unions presenting themselves as the sole legitimate representatives of workers. This, in turn, may have been due to a fall in worker desire for union representation. However, the evidence does not point to such a decline (Bryson and Freeman, 2013). An alternative possibility

is that unions have increasingly struggled to supply union representation due to their own financial difficulties as organizations, which relate in part to the marginal costs of supplying that good (part of Olson's second order collective action problem), the rising relative cost of the union good associated with unions as 'cost disease' organizations whose productivity has risen more slowly than the productivity in other sectors (Willman et al., 2020a). A further possibility is that the development of alternative, employer-manufactured voice mechanisms such as team briefings or engagement surveys, linked to the rise of human resource management (HRM), has potentially satisfied worker demand for 'voice', though evidence of HRM-union substitution is limited (Wood and Machin, 2005).

#### 5. The Role of the State in Facilitating Worker Representation

The presence or otherwise of worker representation at the workplace is not simply a function of employer preferences because the state mandates it in many instances, or else legislates to lower the costs workers face in triggering rights to representation. This may occur if the state wishes to guarantee the basic human right to representation enshrined in Article 23.4 of the United Nations Universal Declaration of Human Rights by outlawing discrimination on the basis of union membership. As noted earlier, it may also occur if the state supports the existence of the 'closed shop'. In emerging economies questions are raised regarding the independence of trade unions from the states purporting to assist them although, as in the case of China, there is increasing evidence of the emergence of an independent trade union movement conferring benefits on union covered workers (Booth et al., 2020).



Sometimes states promote worker representation in the belief that it is a pre-requisite for effective dialogue between employers and workers, as is the case in the European Union where Social Dialogue based on worker representation is regarded as key to economic and social progress (European Union, 2002). In these cases, the state may permit union and non-union representation to co-exist, or favour one over the other. In the European Union, where statute permits employees in some countries to trigger representation through a Works Council without the costs of union organization, it is common to find both union and non-union forms of worker representation co-existing at workplace level. The worker representation offered via Works Councils may benefit employers and workers where they solve information asymmetry problems and increase worker-management communication flows, whilst avoiding the problems of ‘hold up’ linked to the ‘monopoly’ face of unions (Freeman and Lazear, 1995). In the absence of a State mandate employer provision of such worker representation will be socially sub-optimal (Freeman and Lazear, 1995).

Workers may also benefit from worker representation above workplace-level in the form of sectoral collective bargaining where unions negotiate pay awards at industry-level, regardless of worker representation at firm or workplace level. In Europe it is common for the State to mandate collectively agreed pay awards in non-unionized sectors, such that workers benefit from these rates as pay minima even if they are not themselves union members. Some states also support the election of workers onto supervisory boards of large companies.

In the United States, if the majority of workers vote union in a National Labor Relations Board election the union becomes the sole agent representing workers in negotiations with the employer

over terms and conditions, precluding other forms of worker representation. Furthermore, there are no provisions in the private sector to extend those collectively agreed terms beyond the organized workplace, thus limiting the union's reach to those workplaces where the union has successfully organized the workers.

The costs unions face in organizing workers on a workplace basis, coupled with the absence of auxiliary legislation to extend union bargained terms and conditions, limits the influence of union-based worker representation in the United States. Even when the State does facilitate worker representation in Europe, there are many countries where worker representation is absent in most workplaces (Forth et al., 2017). Faced with the absence of worker representation some states have resorted to legislating for universal minimum standards, essentially substituting worker representation with employment rights regimes imposed by law and its judicial interpretation (Piore and Safford, 2006).

## 6. Evidence on the Costs and Benefits of Worker Representation

Whether worker representation results in an overall net gain from an employer perspective is the subject of a voluminous literature. It tends to show union effects differ markedly across time and country and that they are heterogenous across unions (Bennett and Kaufman, 2007; Doucouliagos et al., 2017; Barth et al., 2020; DiNardo and Lee, 2004; Frandsen, 2021).

Workers tend to benefit from a union wage premium, either as members or because they are in a job covered by collective bargaining, though this varies across time and place according to institutional settings, union bargaining strength and the business cycle (Blanchflower and Bryson,

2007; Bryson, 2014). They also benefit from other improved terms and conditions, such as more paid holidays (Bryson and Forth, 2019) and, consistent with ‘voice’ offering solutions to problems that might otherwise lead to worker quits, union workers have longer job tenure. Despite these benefits, union workers often express greater dissatisfaction with their jobs and management than their non-union counterparts, though there is considerable debate as to why this might be the case (Blanchflower et al., 2021).

Worker representation through union collective bargaining is also known to reduce wage inequalities and promote equality across worker types through what Flanders termed unions’ “sword of justice” (1970). They do so by bargaining for a standard rate for the job – what the Webbs (1902) referred to as the ‘common rule’, and through the promotion of wage standardization across industries and in local labour markets (Slichter et al., 1960). These effects, whilst still apparent (Metcalf et al., 2001), may diminish with the reduced incidence of unionization in many countries, and the accompanying diminution of the union ‘threat’ which has previously forced non-union employers competing for labour to meet union-set conditions (Fortin et al., 2021).

How much workers benefit from non-union representation is less certain, though there is some evidence for Britain that employee perceptions of managerial responsiveness is better among employees with non-union forms of ‘voice’ than among those with union voice (Bryson, 2004). Although Works Councils benefit workers in Germany in some respects, such as access to training,

these Councils are usually a hybrid of union and non-union representation because they are often dominated by union representatives (Addison, 2009).

Unions and statutorily-based forms of worker representation may also alter the way employers manage through their influence at the workplace, especially if they have representation at board level, operating as what Streeck (1997) would have termed a “beneficial constraint” on managerial decision-making. But board-level worker representation, whilst common in some European countries, is largely absent in the Anglo-American setting.

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