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ECONOMIC REGULATION, SOCIAL INSURANCE AND MINIMUM STANDARDS

Revised Chapter 16 of
Human Resource Management:
An Economic Approach

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Chapter 16: Economic Regulation, Social Insurance, and Minimum Standards

By this point in the text, the reader will be well aware of the central role played by public policy, i.e., governmental regulation, in the American labor market. Indeed, as a later chapter will point out, this characteristic is not uniquely American; in all developed countries, governments have seen fit to intervene heavily in determining the nature of the employment relationship. The laws and regulations which emerge in the U.S., however, are the product of the nation's complex system of legislative-executive-judicial interaction. What makes the American system unique is not the existence of substantial labor market regulation, but rather the way it is developed and enforced. Because of the importance of public policy to the human resource management function, this chapter and the next are devoted to a discussion of selected policies and programs.

Whether he/she approves of a particular regulatory program or not, no human resource professional can afford to be uninformed of the many legal requirements and external public policies affecting the labor market. And no general manager, in seeking to evaluate the effectiveness of the human resource management function within a firm or organization, should do so unaware of the constraints which legal regulation places on that function. On the other hand, as has been stressed earlier in this text, simply complying with the law's multiple strictures is not a complete human resource strategy - in fact it is no strategy at all. Nor should human resource professionals view their task as merely acting as internal police officers for outside regulatory authorities. There is sufficient latitude within the constraints of public policy to permit the firm to adopt approaches to human resource suited to its needs.

Teachers and administrators in public schools often bemoan the fact that they are called upon to deal with social problems that are outside the immediate concerns of educators. Behavioral and other problems which should be dealt with in the home, they say, are being left to the schools. Similar laments are sometimes heard in human resource management circles; society, so the complaint goes, is expecting - and requiring - that employers resolve grand social and economic issues that ought to be handled "elsewhere." And, of course, there is an element of truth to this charge. But, at the same time, the human resource lament overlooks the centrality of work and employment to the larger social and economic structure.

The average male will spend about half his lifetime in the workforce (including years of childhood and retirement). For women, the figure is around 40%.[1] Even those who are not employed - children, homemakers, the disabled, retired persons, and the unemployed - generally receive a major proportion of their income as a byproduct of the labor market. They receive it in the form of support from working members of their families, from Social Security, from pensions, from work-related insurance payments, and from unemployment benefits. Inevitably, the social and economic issues related to income distribution will be connected in the public mind with the labor market, and with the employer-employee relationship.

Indeed, it is difficult to draw a sharp line between those economic policies which are labor market programs, and those which are not. Economic policies which are not generally viewed as examples of labor market regulation nevertheless often have an important impact on employment. Almost any policy which affects the product market will also have an impact on the labor market. Thus, the politics of public policy in the product market often revolve around whether particular programs which are being advocated will "create jobs" or "destroy jobs."

I. Macro Policy.

Macroeconomic policy - monetary and fiscal policy - is usually viewed as regulating "aggregate demand" for the purpose of influencing the rate of unemployment and the rate of inflation. Through tax cuts and increased government spending, fiscal policy can stimulate the economy, expanding production and employment - but also, perhaps, raising the inflation rate. Expansion of the money supply by Federal Reserve open market operations is also stimulatory to real economic activity and potentially inflationary. A fuller discussion of macro policy is best left to other texts and to courses in macroeconomics. The field of macroeconomics has been in flux since the 1970s, and new interpretations and analyses have been evolving.[2] However, the interaction between macroeconomic policy and the labor market should be quite clear.

To the extent that macro policy either raises or lowers the general level of economic activity, it changes the level of labor market demand. Pulses of aggregate demand are translated into employers' human resource policies of increased or decreased intensity of utilization of the existing workforce, e.g., more or less use of overtime, and into hiring or layoff decisions. Compensation policy is also influenced by induced labor shortages or surpluses, as earlier chapters have noted.

If macroeconomic policy causes an acceleration or deceleration in price inflation, that, too, will have human resource management implications. In unionized settings, for example, there may be demands for cost-of-living escalator clauses where none currently exist, or improved escalation formulas where they already do. And in both union and nonunion settings, compensation adjustments may be made by employers to protect the real wage, or in response to rising wages of other employers.[3]

Apart from wage determination, inflation induced by macro policy has implications for deferred benefit programs such as pensions and life insurance. Thus, issues may arise concerning the status of already-retired workers whose (unindexed) retirement benefits are deteriorating in real terms, especially in collective bargaining situations.[4] As discussed in a previous chapter, inflation may also have a distorting influence on such human resource practices as determining pay increases through evaluation of employee "merit."

In short, the conduct of macroeconomic policy has obvious effects on human resource policy at the firm level. But the reverse is also true, even if it is less self evident. The conduct of human resource policy at the firm level affects - and, many economists would say, is the motivation for - implementation of active macro policy. If the labor market functioned as a classical economic auction, smoothly and quickly adjusting wages up or down in response to demand, the economy would stay at full employment. Inflation could be painlessly avoided by appropriate monetary policy. And even if inflation did occur, it is not clear that anyone would much care in the context of an auction-type labor market, since no real wage effects would result.[5]

II. Product Market Regulation and Deregulation.

Labor demand is ultimately derived from product demand. Firms want labor in order to produce goods and services. Government regulation of the product market in ways which influence product demand will inevitably influence labor demand. Even if the "intent" of regulation initially has nothing to do with any resulting employment effects, those effects will soon enough become evident and will create constituencies for or against particular programs.

Consider, for example, the "environmental" issue of requiring soft drinks to be sold in returnable deposit containers, rather than in throw-away bottles and cans. Environmentalists tend to favor such requirements on the grounds that deposit laws will discourage discarding of empty bottles and cans on roadsides, in public parks, etc. Whatever the merits of such regulation, typically unions representing supermarket employees - for whom extra work will be created to process and sort the returned bottles - <u>favor</u> laws requiring return containers. In contrast, unions involved in glass bottle production <u>oppose</u> deposit/return laws, since the demand for bottles - and, therefore, bottle makers - will be reduced by recycling.

Some forms of regulation, rather than creating more demand for a service, may instead restrict competition between suppliers. Even though such restrictions can result in higher prices and - therefore - less production and employment, reduced competition can raise the bargaining power of unions in the protected sector. Similarly, deregulation can reduce that power. Thus, in the airline industry (deregulated beginning in the late 1970s), post-deregulation employment rose more rapidly than in the economy as a whole, but wages fell relative to other sectors. As Figure 1 shows, from 1977 (the year deregulation was enacted) to the business cycle peak of 1990, airline full-time equivalent employment rose almost 5% per annum compared to a little over 2% in the overall private sector. But airline wages, which had been about 1.8 times the average private wage dropped to 1.4 times. Airline industry unions have been critical of deregulation since it was introduced, generally hoping to enlist public support through arguments related to safety and service to sparsely populated destinations.[6] The employment gains - which sometimes went to nonunion airlines and workers - have mattered less to them than the compensation losses and deterioration in working conditions which accompanied declining union bargaining power.

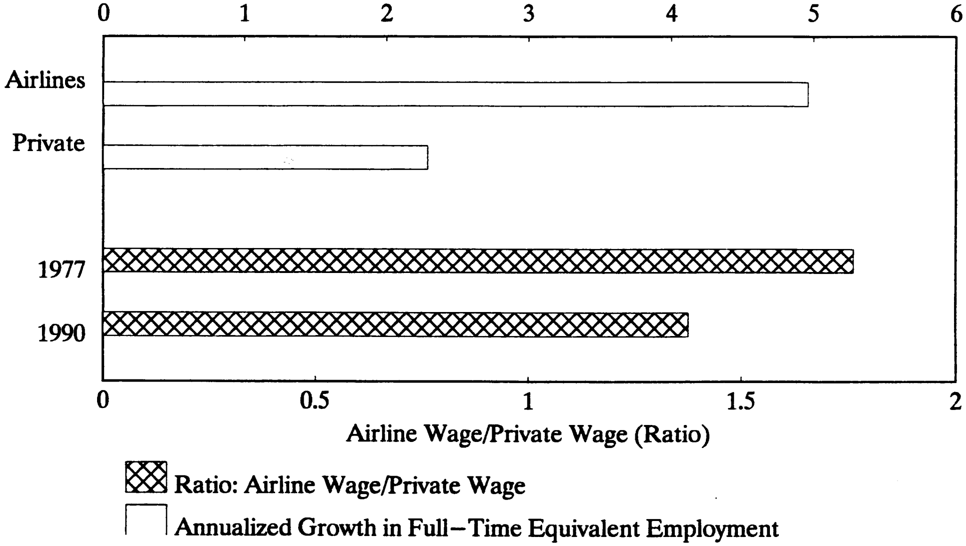
Figure 1 here

The human resource management implications of changes in product market regulation for the employment relationship go beyond unions and bargaining. Employers will adopt different human resource strategies, depending on the nature of product market competition to which they are exposed. Companies with secure,

Figure 1

The Deregulated Airline Industry:

Trend in Employment and Pay: 1977–90



Note 1: Employment refers to full–time equivalent employees.

Note 2: Wage refers to wages & salaries per full–time equivalent employee.

Source: National income accounts.

airline.cgm
airline.wk3

relatively noncompetitive, regulated product markets - such as utilities - are likely to tilt towards human resource policies favoring long-term, career employment, and job security. Some public utilities still apply this model (although even these firms have begun to feel competitive pressures). Their managers know that demand for their firms' output will continue without substantial interruption, and so they have every reason to invest both in their employees and in their relationship with their employees. With predictable long-term employment stability will probably go comprehensive fringe benefit packages. In contrast, firms in volatile, competitive industries may stress temporary, less-assured, "flexible," or contingent employment arrangements. And benefit packages are likely to be more spotty and will reflect the more transitory nature of the employer-employee relationship.

Although the connection between the product market and the labor market make it difficult to draw a precise line around labor market regulation, certain kinds of programs are generally viewed as falling into that category. Some of these programs have already been discussed in earlier chapters. The sections which follow take up social insurance programs - such as Social Security - and minimum standards programs - such as the federal minimum wage and occupational safety and health rules. In the next chapter, there will be discussion of immigration control and equal employment opportunity.

III. Social Insurance.

Life poses risks and uncertainties, and those perils which threaten a cut-off of income - or a heavy drain on income - are often seen as related to the labor market. Since the labor market - directly or indirectly - is the major source of most people's income, this public perception is not surprising. The result has been adoption of "social insurance" programs, specifically workers' compensation, Social Security, and unemployment compensation.[7] Much American social insurance dates back to the New Deal era of the 1930s.[8] However, there are elements which pre-date that period, and others which have been added more recently. The three major social insurance programs are described briefly below.

i. Workers' Compensation.

Workers' compensation is not a federal program. It is composed state-enacted laws providing benefits to workers who are injured on the job or become ill from occupational diseases.[9] State laws vary in scope. Employment coverage is generally very extensive with exemptions sometimes provided for very small employers, domestic servants, farm labor, and charitable organizations. Generally, employers obtain their mandatory insurance coverage from private carriers. Most jurisdictions permit self insurance. A few states operate state-run insurance funds to provide the compulsory coverage.[10] As Table 1 shows, over eight out of ten persons in the paid civilian population are covered by workers' compensation.

Program History.

Programs of workers' compensation arose in the early part of the twentieth century, an era in which industrial accidents were of great concern. Injured workers could sue their employers for damages, but they had to show that the employer was at fault. The employer could claim in defense that the worker was at fault, or the worker knowingly assumed the risk entailed in the job, or that some other worker was at fault. These defenses were initially very effective in fending off claims.

However, as jurors became less receptive to these defenses, the management community opted for the present day "no fault"/limited liability insurance system.[11] Under this system, workers need show only that their injury/illness was caused at, or by, the job to receive benefits. In exchange, suits for damages against employers are not permitted and employees must accept state-designated benefit schedules.

New Types of Claims.

Although the no-fault aspect of workers' compensation was intended to eliminate litigation, in fact litigation frequently occurs - not in court, but instead before state-operated tribunals. Issues adjudicated can involve whether an injury/illness was or was not work related and the severity of the injury/illness. As noted in an earlier chapter, employers have become concerned about a tendency to widen the definition of work-related injury/illness, particularly in regard to claims of "occupational stress." Under stress claims, the employee argues that medical or psychological problems such as heart attacks, strokes, or incapacitating anxiety were induced by job pressures.

Box A on blood pressure/Box B on reform here

In addition, there has been some erosion of the no-fault, specified benefit approach. Enterprising attorneys have, for example, filed suits against third parties other than employers. For example, considerable litigation surrounded manufacturers of asbestos products to which employees were exposed while at work. However, both sides - injured worker and employer/insurance carrier - can resort to litigation. Especially in the occupational disease area, where the causal link to the workplace can be questioned, claims by workers are often contested by the employer or carrier. Indeed, one study questions the use of the term "no fault" as applied to such claims, since contesting them is the norm, not the exception.[12]

Box A

High (Blood) Pressure Workplaces

The stereotypical view of the kind of employee subject to job-related heart problems is the high pressure executive. Medical research have related high blood pressure to job stress. However, they have found that the kind of employee most likely to suffer from such stress is one with little control of the workplace situation, not a high-level executive. Jobs where demands are high and control is low are most likely to produce elevated blood pressure.

Source: Malcolm Gladwell, "Environmental Stress Linked to Chronic Hypertension," Los Angeles Times, April 11, 1990, p. A18.

Box B

Elements of Workers' Compensation Reform

The State of California, concerned about rising workers' compensation costs and their impact on the "business climate", adopted important changes in its program in 1993. Highlights include:

*Limits on claims filed after layoff.

*Higher standards of proof for stress claims.

*Limits on the number of medical/legal evaluations a worker can receive.

*Fines for bad faith, frivolous, or delaying tactics.

*Deregulation of insurance premiums charged by carriers which write workers' compensation policies for employers.

In exchange for these cost-containment measures, the new system provided higher basic benefits for successful claimants. For example, after the first year, total disability benefits were scheduled to rise more than 20%.

Source: Carl Ingram, "Wilson Signs Workers' Compensation Reform," Los Angeles Times, July 17, 1993, pp. A1, A18, and related articles.

Safety Incentives.

Since workers' compensation premiums for many employers vary depending on claims experience, some incentives may be present to reduce employee exposure to risk of injury or disease.[13] However, if there are compensating wage differentials for risk, i.e., if risky jobs pay more than others (other things equal), provision of workers' compensation benefits would lead to somewhat lower wages, diluting the incentive effect.[14] Still, the growth in interest by employers in establishing "Employee Assistance Plans" (EAPs) - discussed in an earlier chapter - seems associated with concerns about workers' compensation costs. In addition, students of occupational stress have suggested approaches to job design that can improve working conditions. These suggestions run from making jobs more predictable to reducing physical stressors such as loud noise and bright light.[15]

However, the fact that workers' compensation limits claims liability to state-specified benefit schedules may reduce employer incentives to invest in safety, relative to the old common-law system of litigation. In addition, since only the employer is liable under workers' compensation, there may be a misallocation of responsibility between employer and employee in situations when it would have been cheaper for the worker to undertake precautions.[16] Since employees cannot sue for damages resulting from job-related injuries and illnesses through the regular court system, there is no way to know what costs of such a system would be, nor how employers would react to it in terms of expenditures for risk mitigation.[17] Employers have not pressed, however, for a return to the common law system of court litigation, suggesting they view the current workers' compensation approach - whatever its defects - as the cheaper alternative. It is known that claims incidence rises with the benefit levels provided across states, suggesting that higher recoveries attract more filings; the duration of reported injuries also rises suggesting a similar effect.[18]

Still, premiums for workers' compensation accounted for only 2.2% of total private-sector labor compensation in 1992, although there was a definite upward trend in this proportion.[19] Some of the long-term upward trend seems to have resulted from state implementation of improved benefits recommended by a federal commission.[20] However, benefits for workers and costs to employers vary substantially between state systems, as do administrative procedures. The general upward pressure on health care costs is also reflected in workers' compensation expenses.

In some states rising costs of workers' compensation provoked strong cost-containment movements. During the late 1980s, Oregon added stringent controls resulting in more claim denials but also notable cost reductions. Public disclosures of doctor/lawyer "stress mills" and of solicitors for potential workers' compensation claimants outside state offices where workers go after layoff to collect unemployment insurance led to calls for substantial reform in California, which enacted cost controls in 1993. These examples are likely to spread to other states.[21]

ii. Unemployment Insurance.

Most paid employees are covered by unemployment insurance (UI), a state operated, but federally-induced program which originated with the Social Security Act of 1935.[22] Under the various state UI programs, workers who are laid off and meet certain standards of eligibility are entitled to weekly benefits for a specified maximum period, generally 26 weeks. These benefits are based on prior earnings of the claimant, but are subject to a cap. UI benefits are financed by payroll taxes which are experience rated. However, caps and floors on the tax rates facing employers mean that taxes paid by some employers effectively subsidize high rates of layoffs by others.[23] Use of layoffs by employers as a strategy for adjusting to demand fluctuations is encouraged by UI.[24] Because this aspect of UI was discussed in an earlier chapter, only brief highlights regarding other human resource management implications of UI are provided here.

Box C on varieties of UI here

Box D on private UI here

Box C

The Varieties of Unemployment Insurance

Because each state operates its own unemployment insurance system subject to certain federal guidelines, the programs vary significantly between states.

*In 1993, for example, four different systems of experience rating were in use. The most popular - the reserve ratio system - geared the employer's tax rate to the net balance of contributions paid and benefits withdrawn divided by average payroll. Thirty-two states used this system but the rest followed other basic formulas.

*New employers do not have experience against which they can be judged. States establish qualifying periods for new employers ranging from 12 to 36 months. Until they qualify, new employers pay a standard rate which varies from state to state.

*States vary in exclusions from coverage. Some common exclusions are newspaper distributors, casual labor, real estate and insurance agents on commission, and interns and student nurses.

*Maximum weekly benefit amounts varied from $116 to $468 in 1993 depending - in some states - on the number of dependents. In many cases, the maximum benefit was determined as a percentage of state average weekly wages with the percentages between 50% and 70%.

*The most common maximum duration of benefits was 26 weeks but some states had formula triggers which extended the maximum duration during periods of high unemployment.

*Seventeen states had varying provisions for worksharing to encourage reduced workweeks spread among with workforce rather than complete layoffs.

Source: National Foundation for Unemployment Compensation and Workers' Compensation, Highlights of State Unemployment Compensation Laws, January 1993 (Washington: NFUCWC, 1993).

Box D

Private Unemployment Insurance?

It has usually been assumed that private unemployment insurance would be difficult to provide because of adverse selection (persons knowing they were to be laid off would take out policies) and moral hazard (persons laid off might not search diligently for work). A few labor unions had informal unemployment benefits for members in the 1920s, as did certain employers, but private insurance companies never got into the market. The only contemporary private unemployment insurance examples until recently were the Supplemental Unemployment Benefits (SUB) under certain union contracts.

During the recession of the early 1990s and its aftermath, however, some real estate lenders offered a limited form of unemployment insurance to attract mortgage borrowers. Employees considering buying a house might be fearful of doing so if they faced a layoff risk which would render them unable to meet their monthly house payments. So lenders offered policies that would cover house payments for a limited duration in the event of layoff.

Source: Denise Gellene, "Consumer Affairs," Los Angeles Times, November 6, 1992, p. D3.

Typical human resource management concerns with UI involve monitoring claims of laid off or terminated employees. It may be to the employer's advantage - depending on its experience rating - to challenge such claims. If, for example, the claims involve a worker discharged for misconduct, state law may restrict benefit eligibility, providing that the employer asserts that misconduct occurred and is prepared to prove it.

UI may also have an influence on employer strategy in collective bargaining, since two states pay benefits to strikers and some states will pay benefits to workers deemed to be unemployed due to an employer lockout.[25] Where benefits for strikers are paid, strike durations may be increased and the union's position in negotiations is strengthened. If benefits are payable for lockouts - but not strikes - employers may try to tailor their dispute strategies so that if work stoppages occur, it is the union - not the management - which initiates the action.

Box E on lockouts here

As in the case of workers' compensation, the precise administrative procedures, employer costs, and employee benefits under UI vary from state to state, and can be complex.[26] Unlike

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Box E

Lockouts and Unemployment Insurance Legislation

Most states do not pay unemployment insurance benefits to strikers. However, they vary in their treatment of workers affected by lockouts during labor disputes. In one case, a lockout triggered a change in state law to allow benefits to locked out workers. In 1993, a bitter dispute occurred at Boston Gas Company over the Company's demand for certain health care cost containment measures such as employee co-payments. The resulting lockout continued for 17 weeks until a settlement was reached on a six-year contract involving some co-payments. During the dispute, the union involved used various tactics including petitioning the legislature to allow unemployment benefits for locked out workers.

Following the settlement, the Massachusetts legislature amended its unemployment insurance law - over a veto by the governor - to permit unemployment benefits to locked out workers who are willing to work under the expired labor agreement.

Source: "Massachusetts Approves UI in Lockouts," Daily Labor Report, June 21, 1993, p. D17, and other related articles.

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workers' compensation, which attracted substantial public attention because of its rising costs, UI has not had similar scrutiny. This neglect is paradoxical since job security and unemployment were of public concern, especially after the recession of the early 1990s. There have been some experiments in adding incentives for workers receiving UI to find work (see box F) but these have yet to spark a major change in public policy.

Box F on experiments with UI and Figure 2 here

There has been public policy discussion, however, about the seeming decline in usage of UI by the eligible unemployed. Figure 2 shows that the proportion of the unemployed who are UI recipients - while cyclically sensitive - has shown some decline since the 1960s and 1970s. However, many unemployed individuals are not among the job losers who would be eligible for UI. Instead they may be new entrants or re-entrants to the labor force. Nonetheless, job losers as a percent of the unemployed have risen over the period shown on Figure 2. When the ratio of UI recipients to job losers is plotted (the upper line on the figure), the downward trend in UI claim rates is more evident.[27]

Studies of the downward trend have not revealed an obvious cause. Some of the drop is "explained" by a shift in the unemployed toward states which historically had lower claimant

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Box F

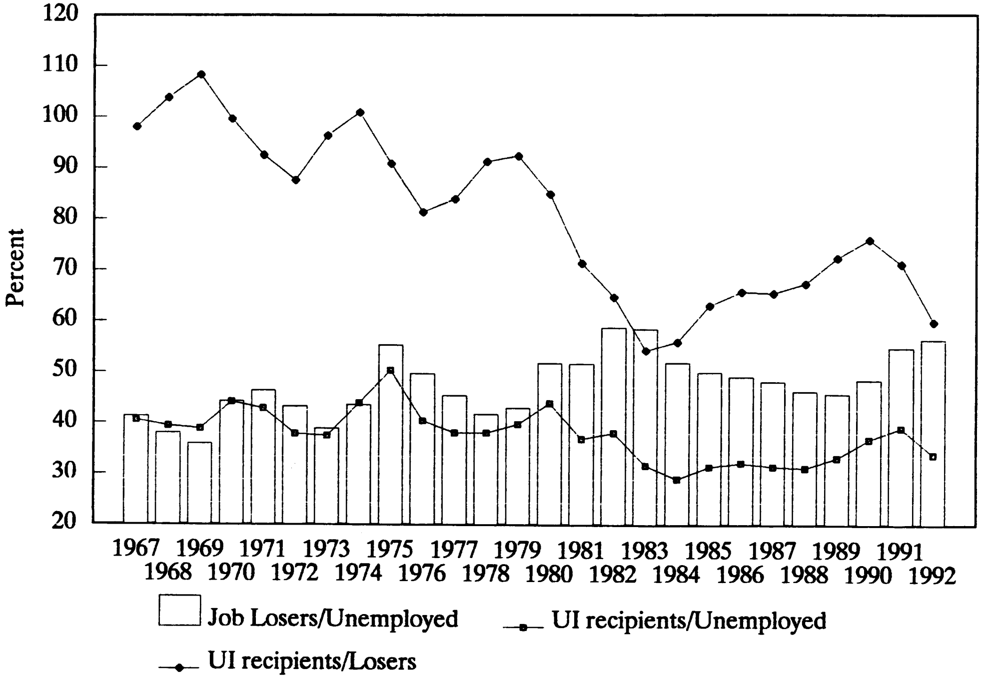
Experiments in Subsidized Job Finding

Although unemployment insurance may subsidize longer job searches, there have been experiments with alternative approaches which provide financial encouragement to job finding. On the supply side, workers have been offered bonuses if they find a job and these do seem to speed up re-employment. Another approach - on the demand side - is to provide workers with a voucher which entitles an employer which hires them to a wage subsidy. This approach also seems to encourage re-employment although it may entail a negative "signaling" effect in some cases. Employers may view presentation of a voucher as a sign that there is a problem with the job candidate, and therefore become reluctant to hire.

Source: Patricia M. Anderson, "The Effect of a Reemployment Bonus with the Possibility of Recall: Experimental Evidence from New Jersey," working paper no. 263, Industrial Relations Section, Princeton University, March 1990; Jeffrey A. Dubin and Douglas Rivers, "Experimental Estimates of the Impact of Wage Subsidies," Social Science working paper no. 778, Division of the Humanities and Social Sciences, California Institute of Technology, October 1991.

Figure 2

Trends in UI Recipients, Job Losers, and the Unemployed
1967–1992



Source: U.S. Bureau of Labor Statistics, Employment and Training Administration

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rates than others. Generally, job losers are more likely to claim benefits if they are union members - perhaps because unions inform members of eligibility and where benefits are higher. Unionization rates and benefit levels vary considerably across states. But even such factors leave much of the decline unexplained.[28] It may be that the conservative political climate in the 1980s discouraged workers in complex ways from claiming benefits from a government program.

iii. Social Security.

Social Security is known primarily as a government-run pension system for workers and their survivors. It is indeed the most important element in the nation's retirement system. But there are also two other key components of Social Security: disability insurance and health insurance. With the exception of certain public sector employees, almost all American workers are covered by these three programs. (Table 1). As can be seen on Table 2, in the early 1990s, average monthly Social Security benefits stood at 40% of the income level of the average private-sector nonsupervisory worker.[29] The increase in relative benefits over the period shown, and the widening coverage of older individuals by Social Security, produced a significant decrease in poverty among the elderly.[30]

Social Security retirement payments are similar in form to those under private defined-benefit plans. Benefits are based on

Table 1

Coverage of Social Insurance Programs: 1990

Program	Population Covered by Program (millions)	Ratio: Covered Population to Paid Civilian Population (%)
Workers' Compensation	96.7	83%
Unemployment Insurance	110.8	95
Social Security	109.8	94

Source: U.S. Bureau of the Census, Statistical Abstract of the United States: 1992 (Washington: GPO, 1992), p. 358.

Table 2

Social Security Benefits Relative to Monthly Earnings, 1970-90

Year	Average Benefit for Retiree	Average Benefit for Disabled Worker	Average Benefit as Percent of Average Monthly Earning(a)	
			Retiree	Disabled Worker
1970	$118	$131	23	25
1980	341	371	33	36
1990	603	587	40	39

(a) Average monthly earnings are calculated by multiplying average weekly earnings for production and nonsupervisory workers in the private nonagricultural economy by (365/12)/7.

Note: In years in which different averages applied for different months, monthly averages were weighted by the proportion of months in the year.

Source: U.S. Bureau of the Census, Statistical Abstract of the United States: 1992 (Washington: GPO, 1992), p. 361; U.S. President, Economic Report of the President, January 1993 (Washington: GPO, 1993), p. 396.

past earnings history, time in the workforce, and age, and become vested after a specified period. But unlike most private pension arrangements, Social Security is completely portable from job to job; it is not a hindrance to job mobility. This feature is a significant advantage if pressures for job mobility, both voluntary and involuntary, increase. Also, unlike most private pensions, Social Security pension benefits are indexed to price inflation.

Since it is a public social welfare system, the financing of Social Security also differs from a private defined-benefit pension. It is financed by payroll taxes levied as a proportion of pay up to a ceiling on both employer and employee. Having an employee contribution component and modeling the benefit formula after private defined-benefit schemes reflected the desire of Social Security's inventors to differentiate it from general relief payments under "welfare."[31] However, increases in benefits relative to average pay (see Table 2) without commensurate payroll tax increases led to a financial crisis in the early 1980s. The Social Security "trust" funds, rather than acting as set-asides for future liabilities had become petty cash funds, with tax inflows not even covering expenditure outflows. In 1983, after a study by a bipartisan commission, a variety of tax increases and benefit restrictions (for example, a scheduled rise in the normal retirement age from 65 to 67 years) were put in place and the funds began accumulating assets in anticipation of the baby booms retirement in the early twenty-first century.

Because the amounts that will build up in the trust will be large, there have been periodic proposals to cut Social Security taxes and to divert the tax inflow to some other use. In late 1991, the Advisory Council on Social Security - a panel of outside consultants - concluded that the system was in financial balance for the next 50 years and that no further adjustments in taxes were needed.[32] Yet controversy has continued in Congress over whether the asset build up should "count" in the calculation of the federal budget deficit. Not surprisingly, representatives of the elderly push to separate Social Security from other components of the federal budget so that benefit entitlement reductions will not be considered to reduce the overall federal deficit.

Saving, Deficits, and Human Resource Management Policy.

It has been argued by some economists that Social Security promises of future benefits substitute for private retirement saving that would otherwise occur. Due to the pay-as-you-go approach to funding until the 1980s, and to Congressional generosity, workers (and their employers) have historically been required to pay less in taxes (actuarially adjusted) than they have received in benefits. The gap between lifetime taxes and eventual benefits was funded by increased tax rates and by a widening labor force base which paid into the system. But although there have been empirical attempts to pin down the effect of Social Security on national saving, the results have not been at all conclusive.[33]

A major difficulty in trying to estimate the saving effect is establishing what workers would be saving if Social Security had not been created. Would there be an intergenerational "understanding," whereby children would support their aging parents? Such arrangements exist in traditional societies and functioned, albeit imperfectly, prior to the creation of Social Security in the U.S. If Social Security has simply "nationalized" a within-family pay-as-you-go understanding, no net saving effect should be expected. If not - if each person would otherwise be putting aside funding for retirement personally or through private pensions - then Social Security could be lowering saving.

There is unlikely to be any resolution of this issue in the near future. And from the viewpoint of firm-level human resource management, the effect of Social Security on overall saving it is only of marginal significance. Its main impact on the firm's human resource function comes only if Congress - in the hope of either fostering saving generally or simply trimming the federal budget deficit - restricts Social Security benefits and/or encourages the creation or expansion of "offsetting" private work-related savings plans. Although there have been proposals that it should do so, Congress is unlikely to require establishment of private pension plans.[34] Hence, its main means of encouraging such arrangements is the traditional one of providing favored tax treatment for them. But such tax incentives lead to government revenue losses. Thus, the same budgetary constraint that affects Social Security is likely to restrict additional tax-based encouragement of private savings and pensions. Indeed, changes in the tax code in the 1980s restricted use of 401(k) savings plans and Individual Retirement Accounts (IRAs).[35]

Indexation.

As noted, Social Security retirement benefits - unlike those of private pension plans - are formally adjusted to reflect changes in the Consumer Price Index.[36] Indeed for a period ending in the mid 1970s, an "error" in the escalation formula resulted in "over-indexing," i.e., a systematic rise of benefits faster than that warranted by CPI-measured inflation. As Table 2 shows, the result was that the economic welfare of retirees rose faster than that of the active working population. And the importance of Social Security as a source of retirement income relative to private pensions and other sources was enhanced.

The fact that Social Security benefits are indexed to inflation has the effect of lessening pressure on employers to place escalators in their own pension plans. Legally-mandated funding rules make it extremely difficult to index a private pension plan. Employers, however, sometimes make ad hoc adjustments for retirees during inflationary periods. Since retirees generally receive a significant fraction of their retirement income from Social Security, employers know that their former workers and dependents have automatically received some inflation-linked benefit increases. For example, if a retiree receives three fourths of his/her retirement income from Social Security - which is 100% indexed - and one fourth from a private pension plan with no indexation, the combination of the two plans is 75% indexed against inflation.

Portability.

As noted, from the employee viewpoint, belonging to Social Security has an advantage not found in other defined-benefit pension plans. The benefits are portable from employer to employer, and even carry over into self employment. Although private defined benefit plans become quasi-portable once the employee has met the vesting requirements, there are typically substantial losses in net pension wealth entailed in job changing for long-service workers.[37] And, of course, employees who change jobs after short spells of employment may never vest in plans under which they are nominally covered at all.

However, from the employer perspective, the portability of Social Security may be a disadvantage when compared with alternative private retirement systems. Lack of portability and limited vesting help reduce turnover costs for employers. The presence of Social Security thus reduces the degree to which pensions can be used for turnover control. And its portability lessens the degree to which pensions can be used for the "efficiency wage" incentive purposes discussed in an earlier chapter.[38]

Labor Supply.

Social Security may reduce the supply of labor in various ways.[39] For older workers, the availability of retirement benefits makes withdrawal from the workforce more feasible than it otherwise would be. In addition, Social Security has a feature which discourages work for benefit recipients. Until the attainment of age 70, earnings above a specified floor result in partially offsetting benefit reductions. These reductions constitute a de facto heavy marginal "tax" on wages and work, which may discourage substantial employment. Finally, the disability provisions of Social Security make it more possible for workers with illnesses or injuries to withdraw more readily from labor force participation.

"Normal" retirement age under Social Security has been 65 years. An early retirement option - with reduced monthly benefits - is available between ages 62 and 65. Table 3 shows that participation of males aged 65 and over has dropped dramatically since the early 1950s. Early retirement for males was introduced in the early 1960s. Thereafter, participation in the 55-64 year old group also began to decline.

Table 3

Civilian Labor Force Participation Rates of Older Persons, 1950-92

Year	Males		Females	
	55-64 Years	65 Years and Older	55-64 Years	65 Years and Older
1950	87%	46%	27%	10%
1960	87	33	37	11
1970	83	27	43	10
1980	72	19	41	8
1990	68	16	45	9
1992	67	16	47	8

Source: U.S. Bureau of Labor Statistics, Handbook of Labor Statistics, bulletin 2217 (Washington: GPO, 1985), pp. 18-19; Employment and Earnings, vol. 38 (January 1991), p. 164; vol. 40 (January 1992), p. 174.

Of course, retirement and labor force withdrawal of older men was influenced by forces other than the presence of Social Security. And there was some evidence in the 1980s of a bottoming out of the effect.[40] Yet, retiring workers cluster around ages 62 and 65, the Social Security early and normal retirement ages.[41] It is hard to believe, therefore, that the Social Security system did not play an important role in the decisions of these workers to leave the labor market.

For women, the story is more complex, since there has been a rising trend in general female labor force participation. But older women, caught between the increased propensity to participate and the availability of Social Security (which has the opposite effect) have exhibited declining participation since 1960. The availability of early retirement for women has produced participation stagnation for the 55-64 year old group in the 1970s and 1980s.

Workers can qualify for disability benefits under Social Security, even if the illness or injury is not job related (unlike workers' compensation). The qualifying disability can be mental as well as physical. To be eligible, recipients must have met prior work tests and must be medically precluded by their disability from "substantial gainful work." The degree of generosity or restrictiveness in administering this standard has varied.

In the early to mid 1970s, the number of disability recipients increased rapidly, and appeared to reduce labor force participation for groups below normal or early retirement ages. More restrictive standards, especially during the initial years of the Reagan administration, reduced the number of recipients. However, litigation and pressure from Congress led to a subsequent increase in disability recipients.

The Social Security incentives for labor force withdrawal at certain ages change the demographic structure within firms. Despite an end to mandatory retirement, Social Security limits the workforce accretion of older workers. As noted in an earlier chapter, if the employer-employee relationship is viewed as an ongoing implicit contract, with low pay at the beginning and higher pay at the end, some means of ending the relationship is needed. In the absence of mandatory retirement, the incentives from Social Security and private pensions may be that means.

A related issue is the demographic bulge caused by the "baby boom" generation born in the late 1940s through the early 1960s. There will be a larger-than-steady-state fraction of middle aged workers pressing for advancement opportunities by the mid 1990s. The labor force withdrawal incentives from Social Security - even though they have been reduced by a budget-minded Congress - will dovetail with the needs of this middle-aged group by opening opportunities as still-older workers retire.[42]

However, despite pressures from younger cohorts in the firm, employers will not necessarily want to shed all of their older workers, or - at least - not shed them at the ages that they choose to retire, given the Social Security incentives. To retain older workers, some accommodations to these incentives need to be made in human resource management policy. For example, the earnings test for workers under age 70 means that firms who wish to retain their older workers may need to arrange for part-time employment options.

Integration of Private Benefits.

The presence of Social Security needs to be considered by employers in benefit administration and design. Human resource professionals in firms which offer disability insurance, for example, must consider what their disabled workers will receive from Social Security in formulating their firms' own plans. In general, it can be assumed that if Social Security offers a benefit, employees will place lower value on increments of that benefit from the employer.[43] Thus, Social Security tends to replace benefits employers might otherwise offer.

Congress also takes account of the presence of similar benefits from private employers and Social Security. For example, firms typically provided for reductions in private health insurance for older workers who became eligible for health insurance

("Medicare") from Social Security. However, in an effort to reduce budgetary outlays, Congress effectively required employers to provide the first-dollar of protection for older workers under Medicare, a reversal of past practice.[44] Even so, firms may continue to provide Medicare supplements to their pensioners. For retirees and dependents, Medicare - not the supplement - pays for the first dollar of coverage.

The most dramatic cases of integration of private benefits with Social Security involve pension plans.[45] There are three chief methods by which private pension designs take account of Social Security. First, there are plans which do not officially include any recognition of Social Security in their formulas, but nevertheless contain benefit levels established in the knowledge that retirees would also draw Social Security benefits. Defined contribution plans typically fall into this category. But among full-time workers under defined benefit plans in medium and large establishments in 1991, only 46% were under plans with no formal tie to Social Security.[46]

Second, there are "excess plans" which provide benefits based on earnings above a specified level (or which provide a higher rate of benefits for earnings above the level). Such plans effectively recognize that Social Security benefits will be paid for those with lower earnings. In some of these plans, the specified level is the Social Security tax ceiling, since workers earning more than the ceiling effectively do not get credit from Social Security for their above-ceiling earnings. In 1991, excess plans covered 36% of full-time workers under defined-benefit pensions in medium to large establishments.

Third, "offset plans" reduce plan benefits by an amount related to Social Security benefits received by the retiree. The reduction is less than dollar-per-dollar under these plans, and the precise formula may also involve years of service. Once the offset is calculated upon retirement, it is not changed to reflect changes in Social Security benefits.[47] The remaining one fifth of full-time workers under defined-benefit plans were covered by the offset method.

Nonunion pensions are substantially more likely than union plans to contain formal Social Security integration provisions. Part of the reason may be that nonunion plans will contain higher paid white collar, professional, and managerial workers for whom the ceilings on Social Security are important. Also a factor in the lower propensity of the union sector to integrate with Social Security may be the median voter political process within unions.[48] This process may reduce the influence of the minority of high paid union workers in union decision making.

iv. Income Redistribution and Social Insurance.

Although the term "insurance" connotes reduction of risk, social insurance often involves more than simply dealing with economic uncertainty. Also involved is income redistribution. A longstanding theme in American economic policy - reflected, for example, in the sixteenth amendment to the Constitution permitting a progressive income tax - is a notion that government should foster economic "equality." Not surprisingly, however, given the political processes which enact economic policy, the social programs that result from this theme are often aimed more at benefits for the middle class rather than at benefits for those at the very bottom of the income scale. The same "median voter" model used to describe the political process in union decision making can also be applied to the larger polity as well. Median voters will be interested in benefits aimed at mid-range incomes.

Despite the interest in the idea of equality, American public opinion has never favored outright confiscation and transfer of wealth. Robin Hood - taking from the rich and giving to the poor - is a more popular figure among children than among voting adults. While a simple economic theory of democracy might suggest that coalitions of 51% of the electorate should form and vote themselves the wealth of the remaining 49%, such bald economic transfers have not been seriously attempted.

Generally, when transfers do occur, e.g., through the progressive income tax, the rationale is couched in terms of fairness and equality of burden sharing.[49] The rich "should" pay more in taxes, it is argued, because the money they pay in taxes is "worth less" to them since they have more of it than the average taxpayer. According to this view, income is subject to diminishing marginal utility. Pure theorists have long had problems with such arguments - it is not really possible to make interpersonal utility comparisons and demonstrate what incremental income is actually "worth."[50] But the general public has not been bothered by such fine points of reasoning.

Similar to the notion that taxpayers should pay what they can "afford" is the idea that employers ought to ensure and provide - or be compelled to ensure and provide - certain minimum standards for their employees. "They" (employers) can afford to do so, it is argued, in comparison to the average employee who is likely to be more vulnerable to life's vicissitudes. No one will win a prize in pure economic theory for these propositions, but politicians are not competing for such prizes.

v. The Incidence of Social Insurance Costs.

In any case, even though the public - probably including most employers - may feel that job-related social insurance is being paid partially or fully by firms rather than workers, the standard method of social insurance finance raises questions about this popular perception. Presumably, the idea that the "firm" pays for something must really be understood to mean that the firm's <u>owners</u> ultimately have their profits reduced by the cost of the insurance. But social insurance is generally financed by payroll taxes or premiums related to employment. Profit or income taxes are not the method of choice. Hence, there is reason to suspect that the "incidence" or burden of the cost of social insurance falls on employees, not owners.

It is true that when payroll taxes are increased, the official total compensation-per-hour numbers issued by the U.S. Bureau of Labor Statistics tend to "blip" up. This tendency suggests that in the very short run, the tax is simply added to (not subtracted from) the wage. Such an observation is in keeping with the implicit contract/sticky wage model of pay setting developed in earlier chapters.[51] But the basic issue is what occurs in the long run. What is the long run tax incidence?

The answer depends heavily on the elasticity of labor supply, which is often assumed to be relatively inelastic with respect to the wage.[52] And in the face of relatively inelastic labor supply curves, economic theory predicts, and empirical evidence suggests, that the incidence of payroll tax and similar mandated payments will fall largely on wages over the long haul.[53] That is, real wages will ultimately be reduced to "pay for" the costs of social insurance programs. While this notion is often the working assumption of economists regarding taxes and mandated employee benefits, it is not at all obvious to business representatives nor the general public.[54] So it is worth examining the point further.

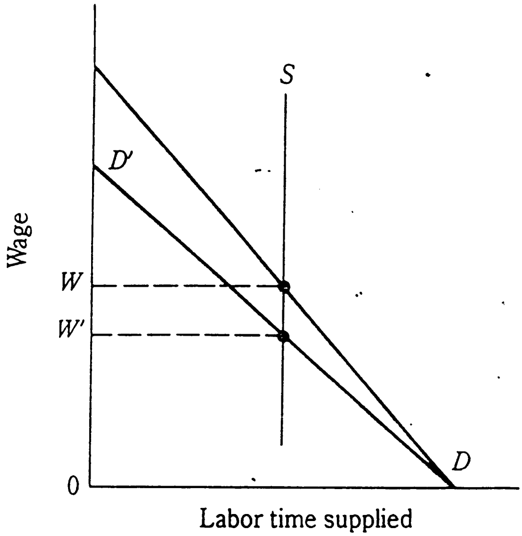
Consider Figure 3. A payroll tax proportional to pay is levied on employers in a labor market characterized by demand curve D and (perfectly) inelastic supply curve S. The tax shifts the effective demand curve down to D', where D' = D/(1+t), and t is the tax rate, e.g., .1 or 10%. As a result, the wage falls from W to W'.[55] Effectively, labor "pays" all of the tax on Figure 3, even though it is officially levied on the employer. Apart from this tax analysis, there are two other reasons to suspect that labor ends up paying indirectly for its own social insurance.

Figure 3 here

First, the payroll tax payment entitles the employee to benefits which are of some value, even if the employee might prefer the cash to the benefits. Just as payments for voluntary benefits, such as pensions, can be viewed as part of the total wage - and, hence, deductions from the take-home wage - social insurance benefits can also be so regarded.[56] Second, to the extent that social insurance does raise net costs to the employer, these costs may be passed into product prices, cutting into real wages.

Figure 3

Effect of a Payroll Tax on Wages



Note: $W = W'(1 + t)$
$D = D'(1 + t)$

Thus, while there is an income redistribution aspect to social insurance, it is more a matter of transfers between groups of employees rather than rich-to-poor transfers per se. Younger workers contribute to the support of retired persons. Employed persons contribute to the support of the unemployed. Able-bodied employees help support the disabled.

There is some deliberate tilting of the benefits of social insurance to the lower-paid. Retirement benefits under Social Security, workers' compensation benefits, and unemployment insurance benefits replace a larger fraction of the incomes of low-wage workers than high wage. And UI and Social Security benefits are subject to personal income taxation when received by higher income persons, but not when received by those with lower incomes.

Nevertheless, U.S. social insurance programs cannot be characterized as "soak the rich" schemes. Perhaps the best evidence of this proposition is that unemployment insurance and Social Security are financed by regressive taxation schedules. Both are funded by payroll taxes up to an annual wage ceiling. Thus, higher wage workers (or their employers) pay no tax above the ceiling, making the tax collected a lower proportion of their wage than for lower wage workers.

As in other tax/transfer programs, social insurance will have behavioral effects that go beyond simple income redistribution.

There are incentives to undertake steps which minimize taxation and maximize benefits. Since payroll taxes are collected on the basis of wages, not total compensation, there is added incentive for workers to be paid in the form of nonwage benefits rather than cash.[57] On the benefit side, examples can also be found. For example, as already noted, certain employers have an incentive to rely more heavily on layoffs than on other means to adapt to fluctuations in demand, since their laid-off workers receive an unemployment compensation subsidy.

Because of the behavioral effects induced, social insurance may engender various "inefficiencies." Hence, apart from the use of administrative resources, these programs entail a variety of economic costs. The late economist Arthur M. Okun once referred to public policies involving income redistribution as "leaky buckets." A dollar transferred produces less than a dollar's worth of benefits for the recipient.[58] The inefficiency leakage is not necessarily an argument that the programs should not be undertaken. Rather it simply says that "society," through the political process, must make a collective decision about whether the social benefits from the programs are worth the costs.

vi. Employer Resistance to Social Insurance Costs.

Particularly in the 1930s, as the various New Deal social insurance programs were being adopted, there was resistance within the management community to these newly-imposed arrangements. However, there is today little management objection to the basic social insurance arrangements in principle. But there is resistance to <u>increases</u> in taxes and mandated premiums. If, as economic theory suggests, workers ultimately pay for their own benefits, why should management be concerned with these matters?

<u>Variable Cost Burdens</u>.

Several reasons may be given. First, certain kinds of social insurance impose variable cost burdens across employers. Specifically, workers' compensation and unemployment insurance are "experience rated." Thus, the more claims there are against the employer, the higher the cost. Even if the average cost of these programs is shifted to employees over time in the form of lower wages, particular employers with above-average (below-average) claims and costs will bear extra costs (or benefit from lower costs) relative to competitors.

It pays for employers - subject to the rules of the programs - to "administer" the workers' compensation and unemployment insurance aspects of their human resource management system. Holding down costs will benefit the firm. Proposed legislative changes in these programs which make such administration more difficult from the employer perspective will be opposed by management organizations. On the other hand, it might be expected that the management community would be less concerned about Social Security taxes - which are not experience rated, and which are assessed on all employers uniformly - than about other forms of social insurance. And, indeed, there has been far less ongoing concern expressed by employers about the Social Security program than about unemployment insurance and workers' compensation.

The behavioral responses induced by changes in social insurance programs - especially by changes which make them more generous - can also be costly to employers. And the costs may not be evenly spread across all employers. For example, workers' compensation benefits are relatively low, compared to the wages earned by higher paid workers. Firms employing a high-paid workforce may be little troubled by claims for benefits based on assertions of "occupational stress." But firms with lower paid workforces might find that a loosening of standards for occupational stress claims would have a more important impact on their costs of operation.

Short-Run Effects.

A second reason for management opposition to social insurance cost increases may relate to short run effects. As noted above, in the short run, when payroll taxes increase, total compensation figures tend to blip up, indicating that the tax is initially added to the wage. Wages are not reduced in the short term to cover the added tax burden, even if the costs are later absorbed by labor. Thus, in the short run, increased payroll taxes may cut into profits, creating obvious management incentives for opposition.[59]

Tax Illusion?

Finally, there is a third possible reason for management concern about social insurance cost increases, even if the costs are absorbed by employees. A "tax-illusion" effect may be present; employers are legally obligated to pay the tax, even if its burdens are ultimately shifted completely or partially to employees by the workings of the labor market. The situation depicted on Figure 3 involved labor market demand and supply curves, not demand curves of individual firms or workers. An individual employer would "see" only a wage of W′ prevailing in the labor market plus the tax rate t. The total labor cost to the employer would be W′(1+t).

Such an employer might reason (incorrectly) that if t were lower, total compensation would fall accordingly. While it is true that if the tax rate were reduced just for that employer, its profits would be higher, the profit gain will not occur if the tax rate is reduced for all employers in the labor market. As drawn on Figure 3, each dollar "saved" by employers through a tax reduction would eventually be "lost" to them due to resultant wage increases. With a somewhat more elastic supply curve for labor, reducing taxes would reduce total compensation, but each tax reduction of $1 would produce less than a $1 net cost saving. There is a potential for a "fallacy of composition" effect; each employer erroneously assumes that what is true for one taken alone is true for all taken together.

The idea of tax illusion will bother theorists who insist that actors in the economic system have perfect insight. But as already noted in the case of unions, union members - and employees generally - often reason on a personal basis with regard to wages. They reason that if <u>their</u> wages were higher, they would be better off, and have trouble appreciating the side effects that might ensue if wages in their firm <u>all</u> rose. Employers, in thinking about taxes, may well reason in the same manner. But informed human resource managers, who are aware of the subtle points discussed above, can help focus the firm's energy on legislative objectives which are truly in its interest.

IV. Health Care As Social Insurance.

Before the 1940s and 1950s, the health care market was largely an individual concern with little government influence.[60] Individuals either bought care out of pocket when needed or purchased insurance on their own. Some employers offered embryonic health plans - often employ<u>ee</u>-paid - as a convenience to workers who wanted them. Insurance companies found they could achieve economies of scale in marketing their products - more often life insurance than health insurance - by selling through employers. Tax considerations were not particularly important since before World War II, ordinary employees had little or no income tax liabilities.

After World War II, however, a system of employer-paid health insurance, fostered by the tax code and prodded by major union contracts containing health care, evolved. More and more workers came to depend on job-related health insurance during their active years. Beginning in the 1960s, the Medicare component of Social Security covered the elderly (mainly 65 and over), sometimes along with retiree health insurance from employers as a supplement or in the form of individually-purchased Medicare wrap-around policies from private carriers.

By 1990, 75.6% of the population was covered by private health insurance (sometimes in conjunction with government-provided insurance), 13.0% had no coverage at all, and the remainder had government insurance only (mainly Medicare and Medicaid). Of those persons with private health insurance, over 8 out of 10 had this insurance in connection with a job, either as an employee, former employee, or dependent. Thus, over 60% of the American population was covered by job-related health insurance policies.[61] For that reason, much of the discussion of health care reform has revolved around employer-paid programs.

Several factors have given rise to dissatisfaction over the workings of the employment/employer-based health insurance system in the U.S. First, the price of medical goods and services has tended to rise faster than the general price level. Second, there seems to be a growth in the utilization of real medical goods and services faster than the general growth of population. These two factors have given rise to an ever-increasing health expenditure-to-GDP ratio. From 1960 to 1980, for example, the ratio rose from 5% to 9%. By 1990, it had reached 12% despite intensive efforts at health care cost containment.

Third, this ratio seems out of line with other countries. Among major industrial countries, Canada was the next highest in 1990 with a 9% ratio. Japan's ratio was about 6½% and showed no upward trend in the 1980s. Fourth, general indicators such as life expectancy do not suggest that the U.S. is getting more for its higher expenditure share going to health. Greek life expectancy exceeded American, yet Greece's 1990 health expenditure to GDP ratio was only 5% and its absolute level of expenditure per capita on health was less than a sixth of the U.S. level.[62]

Fourth, because of the common connection between job and health insurance, workers who change jobs - voluntarily or involuntarily - may lose coverage, especially if they (or their dependents) have health problems. Many plans exclude or delay coverage of pre-existing illnesses for new enrollees (newly-hired employees).

Several factors are often cited for the problem of health care inflation and the upward creep in health expenditures. First, use of insurance to pay for health services means that the ultimate consumer (the patient) is shielded from the price of providing those services. Only about a fifth of American health expenditures in the U.S. came in the form of consumer out-of-pocket expenses in 1990. The drop was particularly dramatic in the 1970s when the out-of-pocket expense ratio dropped from 37% at the beginning of the decade to 25% at the end.[63] Consumers, in short, do not have strong price incentives to retard their health care consumption since they do not pay marginal costs.

Second, consumers are at a disadvantage in the health care market. It is the suppliers (mainly doctors) who tell consumers what they "need." When this feature of the market is combined with insurance insulation, the potential for over-expenditure is evident. Because consumers cannot judge quality or need, the mechanism for quality control is after-the-fact litigation (malpractice suits). However, juries may not be better evaluators of quality than patients and may feel impelled to tap the deep pockets of hospitals and insurance companies out of sympathy for plaintiffs, regardless of "fault." Malpractice is an imperfect and costly mechanism of control which may induce "defensive medicine" (performing tests and procedures which may not be needed as a legal defense).

Third, since health insurance coverage is provided on a decentralized basis, considerable paperwork is expended on cost shifting. If an employee is ill, his/her employer's insurance company will want to know if the employee's costs might be picked up on someone else's plan, perhaps as a dependent. Or possibly the illness or injury might be covered by Medicare or workers' compensation. Such shifting is rational from the viewpoint of each plan, but in the context of the overall national system, it is a negative-sum game because of the administrative costs.

Fourth, there is no reason to believe that employers are especially expert at administering health insurance plans. A manufacturer of automobiles, computers, or textiles presumably has expertise in the production of those goods. But why should it be assumed that they also would be particularly adept at health care? Are the skills needed to produce and sell automobiles, computers, and textiles inherently complementary to those needed to run a health insurance plan? The same question can be asked about operators of supermarkets, banks, or advertising agencies. Yet the system which evolved after World War II implicitly assumed that employers are good at health care cost containment and administration.

Various options for health care reform have been suggested, some based on foreign examples.[64] At one extreme is the British system of socialized medicine under which all persons are covered and the providers of health services are agencies or employees of the state. Britons can use private services outside the national system if they can afford to do so. Some British firms do offer private health insurance, especially to higher paid employees such as executives (although without any particular tax advantage). But the bulk of the British population is under the national plan which combines insurance and provision, often under conditions of overt rationing.

More typical of developed countries are national or regional health insurance funds combined with private providers. The funds negotiate prices and contracts with private hospitals and doctors' associations. Such funds may be supported in significant part by payroll taxes from employers but those employers have little other connection with plan administration (just as American employers are not involved in the administration of Social Security). Health care cost containment is left to the fund authorities. Such "single payer" systems eliminate private insurance companies from most of the market (although they may provide supplementary programs for uncovered services). In Canada, for example, each province operates a single payer program.

The Clinton administration rejected the single payer option in its proposals regarding a national health insurance plan. Instead the proposed plan would mandate employer coverage, thus bringing more (mainly small) employers into the pool. Other mechanisms would provide coverage for those not employed. Because of the retention of the employer base, the system still would leave a considerable role for insurance carriers. In general terms, large employers could retain their individual programs but others would be grouped into regional alliances which would negotiate with health providers. No one could be refused coverage based on pre-existing illness. Hence, job loss or job change would not entail loss of health insurance.

Considerable effort is made under the Clinton plan to make a decentralized system work as if it were a single payer program. Whether such a system can truly restrain health care costs is uncertain. Clearly, adding coverage for those now without health insurance will add to costs and put upward pressure on prices. And there are many "details" to work out. Will employers pay the same absolute amount for full and part time workers? If so, the program will discourage use of the latter. Will there be different employer premiums for employees with dependents relative to single employees? If so, employment of the latter will be encouraged. What may be enacted could be quite different from what is proposed. And even when in effect, the plan will be subject to change.

Apart from coordination problems, plan operators will have to walk the fine line between obvious rationing (bound to be unpopular) and price and usage controls. Because the health service market involves expenditures of hundreds of billions of dollars, there will be considerable interest group pressure entailed in creating the "final" plan and operating it. If the plan proves unable to retard costs in a politically-acceptable manner, the issue of designing a national system will again re-open.

To the extent that the administrative burden for administering national health care is shifted away from employers, human resource administrators should be happy. They will have time for performing services more closely aligned to their firm's market performance. However, it must be recognized that there are many human resource administrators who have made careers in health care operations; they may not be delighted to see their function eliminated. General managers must keep this orientation in mind in evaluating responses from their human resource departments.

Finally, the reader is again reminded that the long run incidence of a mandated health program is likely to fall heavily on labor. Employers may write the checks but employees will bear much of the costs.

V. Other Minimum Standards Regulation.

Social insurance can be regarded as part of a national program of minimum workplace labor standards. Employers must offer at least those benefits contained in federal/state social insurance arrangements. For example, employers must be part of Social Security's retirement income and disability programs. But they can - if they choose - offer private supplements, such as pensions or more generous permanent and temporary disability plans. Employers must be part of the unemployment insurance system of the state in which they operate. But they can choose to offer Supplement Unemployment Benefit plans, as some unionized firms do.

There are other forms of minimum standards regulation which do not involve a government-run or sponsored program. At the federal level, some of these regulations involve wages and hours. State-level regulation may involve higher-than-federal standards regarding wages and hours, or more specialized regulation dealing with such matters as the minimum frequency of pay, e.g., California requires that most workers must be paid at least every other week. Apart from social insurance and wages and hours, the other major form of minimum standards regulation involves occupational safety and health.

i. FLSA Wage and Hour Standards.

Earlier chapters have discussed the establishment of a minimum wage and "time-and-a-half" for weekly overtime above 40 hours under the federal Fair Labor Standards Act (FLSA) of 1938 as amended. Like federal social insurance, the FLSA was a product of the New Deal economic policies of the Great Depression era. The enactment of the FLSA came three years after a much more elaborate New Deal attempt to regulate wages and hours on an industry-by-industry basis was declared unconstitutional by the U.S. Supreme Court.[65]

The Minimum Wage.

Because the economic analysis of the minimum wage was discussed in a previous chapter, only a brief review will be presented here. Table 4 shows the federal minimum wage standards in place during 1967-91. As can be seen, the minimum wage was moved up from time to time during that period, pursuant to various legislative amendments to the FLSA.

Apart from minimum wage increases, minimum wage coverage of new groups of workers was expanded. Although the law contains many specialized exemptions, over 87% of nonsupervisory, private sector wage and salary earners were covered in 1990.[66] (Managers and professionals - who would earn more than the minimum anyway - are not covered). Public sector employees are also subject to FLSA standards.[67] Generally, until 1981, the basic federal minimum approximated about half the level of average hourly earnings for nonsupervisory workers in the private, nonfarm sector. No change was made in the minimum wage under the Reagan administration,

Table 4

Federal Minimum Wage Rates as Percent of Average Hourly Earnings, 1967-91

Effective Date of Minimum Wage Imposition	Basic Minimum		Minimum for Workers Covered since 1966	
	Wage Rate	Percent of Average Hourly Earnings(a)	Wage Rate	Percent of Average Hourly Earnings(a)
Feb. 1967	$1.40	53%	$1.00	38%
Feb. 1968	1.60	58	1.15	41
Feb. 1969	1.60	54	1.30	44
Feb. 1970	1.60	51	1.45	46
Feb. 1971	1.60	48	1.60	48
May 1974	2.00	48	1.90	45
Jan. 1975	2.10	48	2.00	45
Jan. 1976	2.30	49	2.20	47
Jan. 1977	2.30	45	2.30	45
Jan. 1978	2.65	48	2.65	48
Jan. 1979	2.90	49	2.90	49
Jan. 1980	3.10	48	3.10	48
Jan. 1981	3.35	48	3.35	48
Apr. 1990	3.80	40	3.80	40
Apr. 1991	4.25	41	4.25	41

(a) Average hourly earnings data apply to nonsupervisory workers in the private, nonagricultural sector.

Note: Lower minimum wage rates applied to farm workers during 1970-77.

Source: U.S. Bureau of the Census, <u>Statistical Abstract of the United States: 1992</u> (Washington: GPO, 1992), p. 415; U.S. Bureau of Labor Statistics, <u>Employment, Hours, and Earnings, United States, 1909-84</u>, bulletin 1312-12, vol. 1 (Washington: GPO, 1985), pp. 5-6; U.S. Bureau of Economic Analysis, <u>Business Statistics, 1963-91</u> (Washington: GPO, 1992), p. 54.

resulting in a gradual decline in its real and relative value. Two increases during the Bush administration pushed it up to 41% in 1991.

The minimum wage has never enjoyed the favor of economists as a group; economic theory suggests that raising a relative wage will diminish the demand for the labor affected, resulting in employment displacement.[68] A queue of job seekers for minimum wage jobs can be expected to result.[69] There may be persons displaced by the minimum wage who may not officially appear in the national statistics as unemployed; some may drop out of the labor market and not be counted. Nevertheless, the income losses of the displaced - even if small - need to be offset against the gains of those who remain employed at the higher wage. In addition, to the extent that they have the latitude to do so, employers may reduce nonwage conditions - such as the provision of training - for those minimum wage workers who retain their jobs.[70]

There is a tendency for opponents of the minimum wage to seize on such arguments, and overstate them. For example, the high black, teenage unemployment rates which are often cited in connection with minimum wages seem more closely linked to the shift in the black population to urban areas and away from the agricultural pursuits which once absorbed black teens.[71] Child labor laws, as applied to teenagers, remove certain job opportunities in manufacturing and construction which might otherwise absorb relatively unskilled young workers.[72] These laws also contribute to reduced teen job possibilities.

In addition, the low level of the minimum wage during the 1980s and early 1990s reduced the number of minimum wage workers. About 9% of workers paid on an hourly basis reported being paid at or below the minimum wage in 1992 (less than 6% of all wage and salary earners). Thus, relative few workers are affected by changes in the minimum wage. That may be part of the reason that some studies have failed to detect a disemployment impact.[73]

Issues of potential employment displacement by the minimum wage - even if overstated - are compounded by the teenage vs. adult division of the low-paid workforce. In the mid 1980s, about 22% of all hourly paid workers who earned the (then) minimum wage of $3.35 or less fell under the government's official "poverty line" on the basis of their total family income. But for teenagers, the rate was under 13%, mainly because teenagers are likely to be in families with one or more adult workers.[74] Although comparable estimates are not available for the 1990s, over half of all minimum wage workers in 1992 (those earning $4.25 or less) were under 25 years old and 29% were under 20.[75] Thus, the minimum wage seems to be a blunt anti-poverty instrument; most workers at or near the minimum wage are not below the poverty line. And the minimum may hurt some of those who are below the poverty line while benefiting others.

From the human resource management viewpoint, however, these arguments over the basic premise of the minimum wage are of little import. The concept of the minimum has been part of American public policy for so long that it can be safely assumed to remain in effect. Indeed, in many respects, the basic argument is really non-economic. There are other examples of private labor-market contracts which are forbidden, even if voluntarily arranged. The law forbids slavery, even in hypothetical cases in which persons were willing to sell themselves.[76] And prostitution is generally outlawed. It appears that much the same attitude has formed about working below some minimum wage. Very low wages are a symptom the public would rather not observe.

Thus, human resource management professionals must assume that minimum wage legislation will remain on the books, both at the federal and state levels. The magnitude of the wage, and the frequency of its adjustment, however, will be of special concern to employers in low paying industries such as fast-food restaurants, car washes, and certain retailers. But any firm with some minimum wage workers will have an interest in minimum wage developments. And one of the issues in the 1990s may be indexing the minimum wage to inflation or general wage levels.

One issue for human resource management professionals in situations where there is a mix of minimum wage workers and higher paid workers is the impact of a minimum wage increase on the pay of the latter group. Given the norms of equitable treatment which influence pay setting, a hike at the bottom of the pay scale will compress the wage gap between those at the bottom and those higher up, and lead to pressure on employers to restore the previous differential. Firms are unlikely simply to boost the entire pay scale up with the minimum; if they did, the federal minimum wage would effectively set pay for the entire workforce. But employers may grant some pay increases - in order to lessen, not eliminate, compression - to workers whose wages are above the new minimum.[77]

Concern over adverse employment effects of the minimum wage has resulted in special arrangements for sub-minimum wages for such groups as full-time students, student-learners, and the handicapped.[78] A perennial issue - raised whenever the minimum wage is hiked - is the possibility of adding a provision permitting a general subminimum wage for teenagers.[79] Still another proposal is the suggestion to index the minimum wage to average hourly earnings, thus avoiding periods - such as the 1980s - of relative minimum wage erosion. It is over these incremental issues, rather than over the basic principle of having a minimum wage, that human resource professionals in affected industries must be concerned.

Hours Regulation.

As an earlier chapter noted, the FLSA has a much more pervasive effect on American employers through its overtime provisions than through its minimum wage requirements. Yet, these provisions are virtually never debated, in Congress or anywhere else, in striking comparison to the continuous debate over the minimum wage. The overtime provision was originally a product of the Great Depression and the problem of widespread unemployment the depression created. It was thought that by encouraging employers to add shifts, rather than pay their current workers for overtime at a stiff premium, existing work could be "spread around" to more employees. Since passage of the FLSA in 1938, the U.S. economy has experienced booms and busts. But the notion of a 40 hour standard workweek, with overtime thereafter, seems to have become an immovable norm in the labor market.[80]

The overtime provisions have important implications for employment practices. There is an incentive - as the framers of the FLSA planned - to add workers rather than hours, once the 40 hour hurdle is reached. But this incentive is not sufficiently strong to end the use of overtime hours completely. Empirical evidence suggests that the premium does reduce the incidence of overtime work.[81]

Adding a shift is a lumpy decision with fixed costs, both in terms of obligations to the new employees and the need for rearranging schedules. In addition, there may be premiums to be paid for night work or weekend work - not because of federal law, but because of worker time preferences. Estimates of overtime hours per employee in manufacturing suggest that once aggregate average overtime/worker reaches about 3½ hours, further demand for labor is channeled mainly into the hiring of more employees.[82]

Despite the dormancy of the overtime issue, publicized successes in reducing the workweek below 40 hours in some European industries in the 1980s may re-ignite interest in the working-week standard in the U.S. Much depends on the course and trend of unemployment. Overtime as a work spreading device is an issue that is more potent in a slack economy with high, persistent unemployment, than in a tight one.

ii. Labor Standards for Federal Contractors.

The federal government is a major consumer of goods and services from the private sector. As a consumer, it can require its private suppliers to meet the minimum labor standards of the FLSA. Under the Walsh-Healey Act, for example, suppliers of goods to the federal government can lose their contracts, and even be blacklisted from future contracts, for labor standards violations.[83]

As a consumer, the federal government can also require minimum labor standards which are <u>higher</u> than those of the FLSA for private federal contractors. Of course, to the extent that such standards raise the cost of producing for the government, the government will have to pay more for its contracts. Two pieces of legislation, the Davis-Bacon Act of 1931 - applicable to federal construction contractors - and the Service Contract Act of 1965 (for services such as equipment repair, building maintenance, food preparation, etc.) require the payment to employees hired under federal contracts of wages "prevailing" in the local area. The level of prevailing wages is determined by U.S. Department of Labor surveys.[84]

Generally, public debate about such requirements has focused mainly on the cost issue and secondarily on administrative practice. Proponents of prevailing wage standards (chiefly affected unions) argue that federal contracts should not be won by competitive wage cutting. They argue that federal costs are not actually raised by the prevailing wage requirement because more productive workers are employed by higher-wage contractors.[85] These two arguments, however, are potentially in conflict; if the productivity effect offset the wage effect, low-wage contractors would not be able to underbid high-wage contractors.

A more sophisticated, theoretically-based economic argument is sometimes made that the federal government might act as a monopsonist in the absence of a legal constraint on such behavior. That is, the government would be tempted to "take advantage" of its dominance in certain markets for goods and services, push down prices of the goods and services it buys, and thus depress wages. Opponents of prevailing wage standards - most notably the U.S. General Accounting Office - have cited higher costs to the federal government and tendencies by the Labor Department to select upward biased wage samples in determining what wage was prevailing.[86]

Administration of such laws is influenced by political shifts. Often the battles are fought outside the public spotlight on arcane issues such as formulas to calculate the prevailing wage or the use of helpers in construction.[87] For industries and unions affected, however, the battles loom large.

iii. Occupational Safety and Health.

The federal government imposes minimum workplace occupational safety and health standards primarily through mechanisms established by the Occupational Safety and Health Act of 1970 (OSHA).[88] Prior to OSHA, such regulation was mainly in the hands of the states, pursuant to laws dating back to the 1870s. The new law created the Occupational Safety and Health Administration in the U.S. Department of Labor to administer the Act and conduct worksite inspections, the Occupational Safety and Health Review Commission to hear appeals of citations and fines from employers, and the National Institute for Occupational Safety and Health

(NIOSH) to conduct research and recommend safety and health standards.

Under OSHA, state governments have the option of having their own enforcement programs, so long as state standards are at least as strict as the federal rules. States which meet the requirements of OSHA can receive a federal subsidy for their administrative costs. Of course, from the employer perspective, higher state standards means the potential of inconsistent requirements for worksites in different regions of the country.

The Union Role.

Unions played a key role in obtaining Congressional enactment of OSHA. It is not surprising that unions would have a special interest in occupational safety and health, since their members are more likely to be in hazardous jobs than nonunion workers.[89] But why would unions have wanted a special statute?

The answer might seem obvious; with a statute unions could bargain as they traditionally had for wages and benefits, and then let OSHA provide the safety umbrella "on top of" what had been negotiated. But this answer is not entirely satisfactory. To the extent that providing safety and health is costly, and to the extent that workers value safety and health, OSHA-induced costs may be shifted back to workers by employers, like other fringe benefits. Just as more pension can be expected to mean less wages, other things equal, so more safety could also mean less wages. Why wouldn't unions prefer to make the trade-off themselves through bargaining, rather than have the federal government impose it?

There could be several answers. First, it may have appeared to unions that OSHA-imposed safety standards would have been added, like gravy, on top of their traditional wage and benefit packages.[90] That is, they may not have perceived the possibility of a backward shift in costs, even if economic theory suggests its potential. After all, unions could see that employers opposed a federal statute; if the backward shift had been assured, employers presumably would have been indifferent towards the law's passage. As in other areas of public policy in the labor market, the parties involved often focus on the direct effects and play down (or do not perceive) possible indirect consequences.

A second reason why unions may have pushed for OSHA is that bargaining intelligently for health and safety involves costly technical expertise. Proposing safety standards requires knowledge of industrial engineering and chemistry; proposing health standards requires knowledge of industrial medicine. Moreover, as technology changes, new equipment appears at the workplace with new hazards. New chemicals are developed with potential dangers of exposure. A heavy investment in expertise is involved in simply keeping up with new processes and their consequences, let alone conducting a research program. Under OSHA, these costs are federally-borne and centralized.

A third possibility is that OSHA standards, as typically applied, have the effect of increasing employment. The "engineering" controls needed to reduce noise or chemical exposure may act as a "tax" on capital (not labor), thus raising the demand for employees. A net increase in employment is possible if the substitution effect of higher effective capital costs outweighs the negative effect of higher costs on output. There is limited evidence that OSHA standards have an employment-raising effect.[91]

Finally, the existence of OSHA standards has sometimes proved to be a useful tool for unions in recognition or negotiating disputes with employers. Charges of unsafe working conditions are of obvious concern to workers, and can rally their support. Moreover, as part of the general environmental movement which developed in the 1970s, the public is sympathetic to workers who are exposed to health hazards.

Box G on unions and OSHA here

<u>Compensating Wage Differentials</u>.

Box G

Unions and OSHA Enforcement

One study suggests that where unions are present, OSHA enforcement is more stringent. Where unions are present there are more inspections and higher penalties for violations. Employees in unionized situations are also more likely to utilize their right to walk around with OSHA inspectors. These effects, however, were concentrated at larger establishments.

Source: David Weil, "Enforcing OSHA: The Role of Labor Unions," Industrial Relations, vol. 30 (Winter 1991), pp. 20-36.

Economic theory predicts that wages would adjust to known differential risk. Other things equal, high risk jobs should pay more than low risk jobs. As noted earlier, these hypothetical wage premiums are termed "compensating wage differentials" by economists. However, demonstrating the existence of such differentials empirically is made difficult by the observed gross negative correlation between wage level and occupational risk. Within blue collar occupations, for example, (low-wage) laborers face greater hazards than (middle-wage) semi-skilled operatives, who - on average - face greater risk than (high-wage) skilled trades.[92]

The negative gross correlation does not mean that the theoretical proposition is necessarily wrong. It may simply be that worker preferences for safety, like other fringes, rise with income levels. Or it may indicate that employers tend to shift dangerous work toward low-paid occupations in order to reduce the differentials that must be paid.[93] Some studies have used statistical controls in examining job-related risks, and found evidence of positive compensating differentials for work hazards. However, the evidence has sometimes been ambiguous and, to the extent that positive differentials are found, they seem to be concentrated in the union sector.[94] A complicating factor is that the existence of workers' compensation, by offering injured employees financial compensation, can be expected to weaken the link between riskiness and pay.[95]

As noted at the outset of this section, for job risk to affect wages, there must be worker knowledge of the hazards involved. Evidence exists that workers - if given accurate information on employment hazards - will respond appropriately; risk averse individuals will exit risky jobs.[96] Undoubtedly, firefighters and roofers are aware that they are in risky occupations. But their risks involve injuries which are readily observed, and which are easily connected with the job. Occupational diseases, however, often have long incubation period and their connection with the job may not be at all obvious, even to health professionals. Thus, there is evidence to suggest that to the extent that compensating wage differentials exist, they relate to injury risk, not to disease risk.[97]

Box H on right to know here

The complex nature of the employer-employee relationship also suggests difficulties with complete reliance on the labor market to deal with safety and health issues. Employees may come to the job with expectations about "reasonable" levels of workplace safety. Yet, like other aspects of the relationship, the exact nature of reasonable behavior on the part of the employer is not clearly defined. OSHA is a case in which public policy has been called in to define that behavior more precisely.

Box H

"Right to Know" Approaches

General environmental concerns often overlap with workplace health issues. For example, the State of California, by ballot initiative, enacted "Proposition 65" in 1986 which required businesses to notify the general public of the presence of toxic or carcinogenic materials, initially was not applied to the workplace. However, subsequent court decisions have applied Proposition 65 to employers and required them to notify workers of hazardous substances to which they might be exposed.

Source: James C. Robinson, "Policy Alternatives for Occupational Health," CPS Brief (publication of the California Policy Seminar), vol. 4 (April 1992), pp. 1-4.

Regulations vs. Incentives.

Although a case can be made for public policy in the job safety and health area, the particular regulatory system created by OSHA is not necessarily ideal. OSHA standards tend to be specific, i.e., indicating precisely what steps, equipment, etc, should be undertaken or installed to mitigate a particular hazard. On the other hand, the resources available for OSHA safety inspections are small, as are the fines typically imposed. Economists have long criticized this approach to regulation.[98] Two basic issues are raised.

First, there may be more than one way to mitigate a hazard, and it may be more efficient to leave the method chosen to the employer. But if the employer is allowed discretion, there must be assurance that the method picked is effective. So the second issue is the need for expected financial penalties - tied to the occurrence of injuries or illness - which are large enough to provide deterrence. A mix of more elaborate inspection resources - but to check on occurrences rather than equipment - and larger fines would be needed.

Unfortunately, the disease aspect of occupational safety and health poses hurdles for such an incentive-based system. Just as workers may have difficulty recognizing the disease risk, so would inspectors assessing fines on the basis of occurrences. The occurrence might take place 20 or more years after exposure to the job hazard. Would the employer be assessed retroactively? What if the employer no longer existed? If the employee had worked for more than one employer at which the disease might have been contracted, how would the fine be allocated between them? What kind of appeals mechanism could be provided to examine events of the distant past while providing due process?

A Bargaining Alternative?

It has been suggested that the federal government should supplant the OSHA model of regulation with private bargaining. Although, as noted above, unions favored the creation of OSHA, the argument has been made that they could be induced to bargain on safety matters and, effectively, replace OSHA by doing so. What would be needed, according to this view, is a sufficient subsidy to be given to unions to develop the necessary health and safety expertise. Additionally, some kind of a limit on union liability to injured workers would be required.[99]

In fact, OSHA has distributed some funds for training of union officials in safety matters. And unions do engage in safety bargaining, even in the absence of a subsidy. But they do not have typically have the kind of expertise that the enforcement and research arms of OSHA can provide. At any rate, unions represent a minority of workers, even in high-hazard sectors such as manufacturing and construction. How would bargaining be applied in nonunion situations?

Cost/Benefit Analysis?

Even within the basic OSHA model of rulemaking, it has been suggested that economic analysis should play a larger role. For example, one possibility would be to subject new rules to some kind of cost/benefit analysis. While courts have not demanded complete avoidance of economic considerations in the standard-setting process, they have not accepted a strict cost/benefit approach either, since the statute does not call for it. Costs of regulation enter in court review of proposed OSHA standards indirectly through general judicial insistence that some benefits of the rules must be demonstrated and through judicial acknowledgment that achieving zero risk is not a feasible goal.[100]

Box I on cost/benefit here

At any rate, it is easier to call for cost/benefit analyses than to implement a procedure for conducting them. The cost side is more readily handled than the benefit side. And even the cost side has ambiguities, since - as noted earlier - some of the costs to the employer may be shifted back to workers.

Box I

Weighing Costs and Benefits of OSHA Rules

Although economists generally think about public policies in terms of costs and benefits, the legal framework of OSHA does not formally recognize such an approach. From time to time, attempts to assess OSHA standards in this manner have sparked controversy. In a Supreme Court case in 1981 - American Textile Manufacturers Institute v. Secretary of Labor - OSHA was prohibited from using a cost-benefit approach and was instead directed to look only at technological and economic feasibility.

In 1992, the Office of Management and Budget proposed that the government should consider whether its OSHA rules save more lives than they cost. The costs would include the possibility of lowered wages due to the expense of employer compliance which might - in turn - reduce worker health. OMB argued that the Department of Labor should at least consider the argument and perhaps sponsor empirical research. However, the proposal met with angry opposition from Democratic lawmakers and disappeared.

Source: "OMB Defends Cost-Benefit Theory in Testimony Before Senate Committee," Daily Labor Report, March 20, 1992, pp. A8-A9.

To value the benefits of a proposed rule, the likely reduction in injuries or illness must be calculated. For occupational diseases, this step is difficult because of long incubation periods and lack of knowledge about the functional relationships involved. As an example, it is often not known whether disease reduction related to chemical exposure is proportionate to exposure reduction, or whether there is a hurdle level of safe exposure, below which no hazard is involved.

Given these difficulties of implementation, suggestions have been made for relying on costs alone. The OSHA authorities might be given an annual "budget" of costs they could impose on employers. Within that budget, presumably, the regulations felt to be most beneficial would be implemented, although precise calculations of benefit would not be needed.[101]

Box J on OSHA inspectors here

The Safety and Health Record.

The Bureau of Labor Statistics began to collect information on occupational safety beginning in the early 1970s. There may be some reporting biases in these data since they rely on employer reports.[102] Nonetheless, they are the best we have. As Figure 4

Box J

OSHA Effectiveness as Seen by Its Inspectors

A poll of OSHA compliance officers undertaken by the U.S. General Accounting Office taken in 1989 revealed the following views:

1) 40% of the inspectors characterized the overall OSHA program as "effective", 19% as ineffective, and the remainder (41%) took a neutral position.

2) Inspectors regarded standards relating to health as more difficult to understand than those related to safety.

3) Inspectors emphasized lack of knowledge by employers and employees as being significant contributors to health and safety hazards. They viewed OSHA's efforts at education as moderately effective for employers and less so for workers.

4) Inspectors thought that employers should be required to develop and implement workplace safety and health programs. Workers should more often accompany inspectors during inspections and participate in settlement discussions. However, inspectors believe that workers are not knowledgeable about their rights under OSHA and often fear that employers will retaliate if they report violations.

Source: U.S. General Accounting Office, Occupational Safety & Health: Inspectors' Opinions on Improving OSHA Effectiveness, GAO/HRD-91-9FS (Washington: GAO, 1990).

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illustrates, reported injury and illness fell after the early 1970s. However, the decline was centered in minor injuries; as Figure 5 shows, so-called lost-workday cases, i.e., occurrences that led to absence from work (on average over 20 days), show no trend.[103] On the other hand, death rates do appear to have fallen although the monitoring of death rates has not been consistent over the period since OSHA became effective.[104]

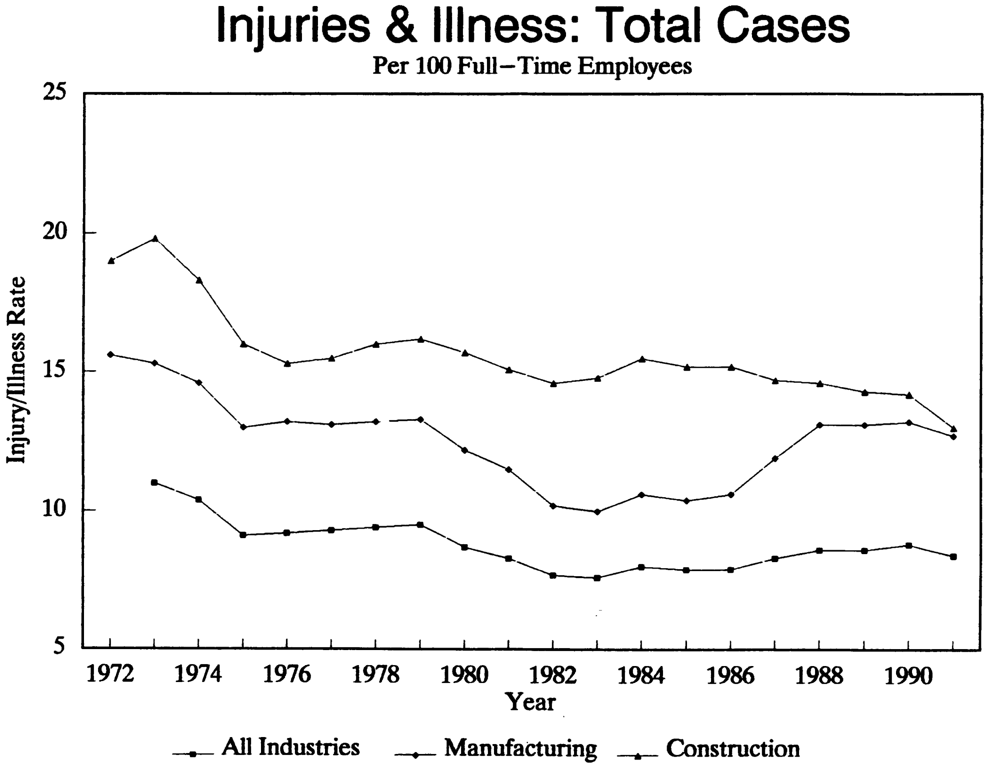
Figures 4 and 5 here

Box K on getting their attention here

Establishing cause and effect relationships from these data is difficult. Some detailed studies have suggested that OSHA regulations do reduce certain types of injuries.[105] Others find, however, that the cost of noncompliance is not sufficiently high to have had a significant effect on injury rates.[106] It has been noted that there is a procyclical effect in injuries; when the business cycle picks up new hires are often inexperienced and more accident-prone.[107]

Apart from the injury-deterrence question is the issue of occupational disease. Data problems related to occupational disease make study of that facet of the OSHA program especially

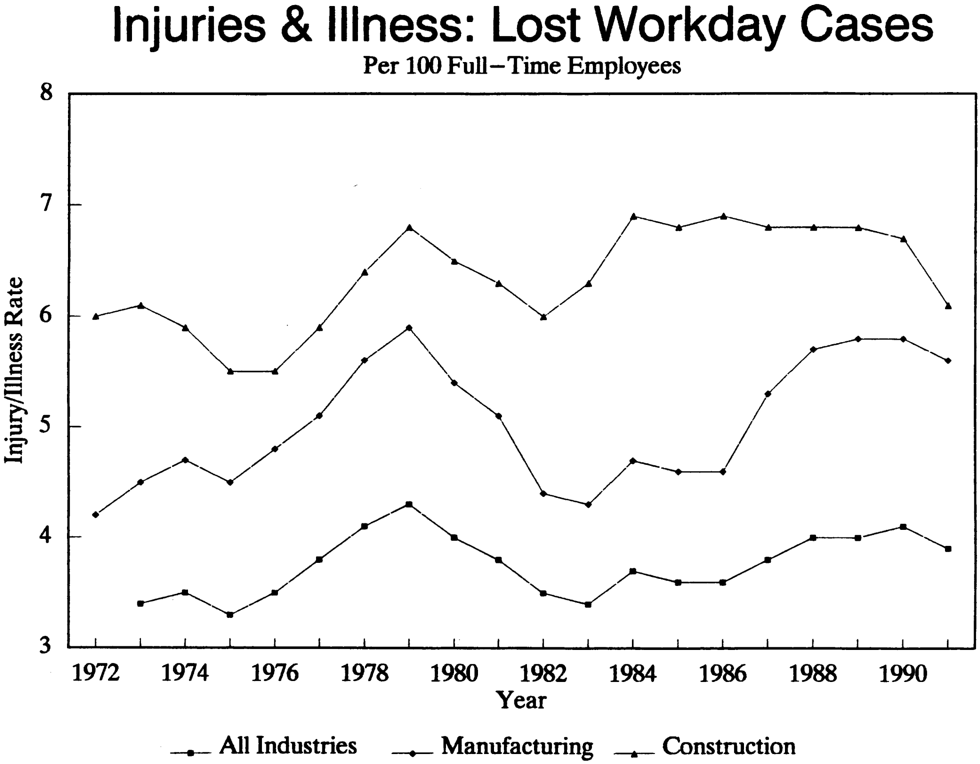
Figure 4



Source: U.S. Bureau of Labor Statistics.

occtotal.pic
occ.wk1

Figure 5



Source: U.S. Bureau of Labor Statistics.

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Box K

Getting Their Attention

What circumstances will shift management attention toward occupational safety issues? Not surprisingly, the occurrence of an accident seems to induce management to take corrective actions. Similarly, a safer-than-normal record may divert management attention from safety.

Analysis of accident histories at specific plants indicates that deviations of accident rates from industry means are corrected over a period of time. The process seems to be more than the expected "regression-to-the-mean" phenomena.

Analysis of the data also suggested that a 10% increase in OSHA inspections with penalties reduced accidents by 2%.

Source: Wayne B. Gray and John T. Scholz, "A Behavioral Approach to Compliance: OSHA's Enforcement's Impact on Workplace Accidents," working paper no. 2813, National Bureau of Economic Research, January 1989.

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complicated. Employees who contract a disease long after exposure to the workplace hazard may not even be recorded as suffering from a work-related illness. And even if good data were readily available, the full effect of OSHA might not be felt for many years.

Box L on a favorable verdict here

Box M on an unfavorable verdict here

The OSHA Outlook.

OSHA's effectiveness is difficult to assess, a fact which paradoxically has insulated the program from criticism. And the proposed alternatives to OSHA founder on practical difficulties of implementation. Thus, human resource specialists would not be well advised to anticipate fundamental changes in the OSHA approach to job safety and health. There may well be experimentation within the basic model. For example, OSHA has developed approaches which target high risk industries and employers, in order to economize on limited inspection resources. The absence of an effective alternative suggests the OSHA model will be retained.

Box L

A Favorable Verdict on OSHA Inspections

Although the OSHA system of workplace inspection and enforcement is often criticized as ineffective, two researchers find a positive impact on safety and health. Based on internal OSHA management data they concluded that OSHA inspections reduce violations (measured by citations for such violations) by employers. The initial inspection seems to have the greatest impact.

Source: Wayne B. Gray and Carol Adaire Jones, "Longitudinal Patterns of Compliance with OSHA Health and Safety Regulations in the Manufacturing Sector," working paper no. 3213, National Bureau of Economic Research, December 1989; and "Are OSHA Health Inspections Effective? A Longitudinal Study in the Manufacturing Sector," working paper no. 3233, January 1990.

Box M

An Unfavorable Verdict on OSHA Results

After reviewing the empirical evidence on injury reduction through the 1980s, one expert in the field concludes that evidence that OSHA has had a positive effect on safety is "minimal." One problem is that studies are based mainly on employer-reported data and incentives to report accurately may be influenced by OSHA itself. Financial incentives to reduce injuries, rather than the specific engineering standards approach are recommended. But analysis of workers' compensation, which in principle should have some such incentives, do not reveal a strong impact. Perhaps, this disappointing result is due to incomplete experience rating under workers' compensation insurance policies. Therefore, self insurance and high deductibles for workers' compensation are therefore recommended to strengthen the financial incentive effect.

Source: Robert S. Smith, "Have OSHA and Workers' Compensation Made the Workplace Safer?" in David Lewin, Olivia S. Mitchell, and Peter D. Sherer, eds., Research Frontiers in Industrial Relations and Human Resources (Madison, Wisc.: IRRA, 1992), pp. 557-586.

One impact of OSHA has been to thrust human resource management policy into an area in which it had previously had little influence: engineering and the application of technology. Human resource managers of the future will have to acquaint themselves with this unfamiliar territory. The very design of equipment has assumed importance in the employment relationship.

Safety and health issues also interact with other public policies. Most prominent have been conflicts between equal employment opportunity policy - discussed in the next chapter - and safety standards. In some cases - the most notable of which is excerpted in the appendix to this chapter - firms have forbidden women of child-bearing age from assuming jobs where exposure could occur to substances which might adversely affect the female reproductive system or unborn fetuses. Is this sex discrimination or responsible risk management? Look at the appendix yourself and make your own evaluation.

VI. Conclusions.

Public policies which affect the labor market consist of two types: those which are primarily aimed at other objectives - but which have labor market consequences - and those which are deliberately focused on labor-market goals. This chapter reviewed macroeconomic policy and product-market regulation and deregulation as examples of the former type of policy. It then turned to a variety of public policies aimed directly at the labor market.

Labor market policies contain both "do's" and "don'ts" for employers. Those policies reviewed in this chapter have been primarily of the affirmative nature, i.e., thou shalt participate in and provide social insurance. Thou shalt pay at least the minimum wage. Thou shalt follow minimum safety and health standards. But other policies in the labor market focus more heavily on negatives. In the next chapter there will be examination of two public policies intended primarily to forbid certain employer behaviors, namely the hiring of illegal immigrants and the discrimination in employment decisions against women and minorities.

EXERCISE FOR THE STUDENT

Although public policies tend to cover employers across the board, certain industries will be more affected by particular policies than others. For example, minimum wage laws tend to affect industries with substantial fractions of their workforces in low-paid jobs. Using available industry data, see if you can identify industries which you think would be especially concerned with minimum wage legislation, with workers' compensation and OSHA standards, and with unemployment insurance. (Different industries, of course, may fall into different categories). See if you can determine how firms falling into the especially concerned industries in your area or state have reacted to proposed changes in these public policies.

Hint: To the extent that policy decisions are decided at the state level (state minimum wage, workers' compensation, unemployment insurance, safety and health if your state operates its own mini-OSHA program), it may be easier to pinpoint the employer reaction in your area.

QUESTIONS AND KEY PHRASES AND CONCEPTS

1. How does macroeconomic policy impinge on human resource management concerns?

2. What impact might you expect product market deregulation to have on an industry's human resource policies and practices? If the industry was heavily unionized prior to deregulation, what special impacts might you anticipate?

3. In what way might workers' compensation induce a safer workplace?

4. How might unemployment insurance procedures affect the course of a union-management dispute?

5. In what ways should designers of a firm's pension policy take account of Social Security?

6. Who pays for programs supported by payroll taxes such as Social Security?

7. Are OSHA standards subject to cost/benefit analysis?

Phrases:

compensating wage differential, Davis-Bacon Act, disability benefits, employee assistance plans (EAPs), experience rating and unemployment insurance, experience rating and workers' compensation, Fair Labor Standards Act, funding of Social Security, integration of Social Security with private pensions, Occupational Safety and Health Review Commission, overtime pay, payroll tax incidence, portability of Social Security vs. private pensions

FOOTNOTES

1. Shirley J. Smith, "Revised Worklife Tables Reflect 1979-80 Experience," Monthly Labor Review, vol. 108 (August 1985), p. 27.

2. For a review, see the symposium on "Keynesian Economics Today" in Journal of Economic Perspectives, vol. 7 (Winter 1993), pp. 3-82.

3. There is dispute in the empirical macroeconomic literature as to whether wage inflation is best explained through a price-wage or a wage-wage model. Some economists have argued that the empirical evidence suggests that wage and price setting are largely independent. The difficulty with this view is apparent, since taken to an extreme, it would suggest massive profit fluctuations as costs and prices moved without relation to one another. For discussion, see Robert J. Gordon, "The Role of Wages in the Inflation Process," American Economic Review, vol. 78 (May 1982), pp. 276-283.

4. During periods of high inflation, it is not unusual for retirees to receive ad hoc benefit adjustments. Union workers appear to be more likely to receive such adjustments than nonunion. See Steven G. Allen, Robert L. Clark, and Daniel A. Sumner, "A Comparison of Pension Benefit Increases and Inflation, 1973-79," Monthly Labor Review, vol. 107 (May 1984), pp. 42-46. During the relatively low inflation period 1986-90, only 11% of private full-time workers were under defined-benefit pension plans which provided some kind of benefit adjustment. Source: U.S. Bureau of Labor Statistics, Employee Benefits in Medium and Large Private Establishments, 1991, bulletin 2422 (Washington: GPO, 1993), p. 84.

5. Many economists would want to qualify the statements in the text. Some would argue that deviations in the product market from the auction model are just as important as those of the labor market, e.g., Olivier Jean Blanchard, "Aggregate and Individual Price Adjustment," Brookings Papers on Economic Activity (1:1987), pp. 57-109. Others might question the dynamic implications of freely-adjustable wages. And, regarding inflation, still others would note that unanticipated inflation (or deflation) could cause income redistribution between debtors and creditors, even if real wages were unaffected.

6. For example, in 1988, unions in dispute with Texas Air Corporation succeeded in prompting a widely publicized federal safety investigation against two carriers owned by the firm: Continental and Eastern. For more on the effects of deregulation on the airline industry, see Herbert R. Northrup, "The New Employee-Relations Climate in Airlines," Industrial and Labor Relations Review, vol. 36 (January 1983), pp. 167-181.

7. There are special programs which can be classified as social insurance applicable to particular sectors. Worthy of mention are Railroad Retirement - a sort of Social Security system for railroad employees - and black lung compensation, an occupational disease program for coal miners. These programs are not discussed below because of their limited applicability.

8. For an historical background, see Irving Bernstein, A Caring Society: The New Deal, the Worker, and the Great Depression (Boston: Houghton Mifflin Co., 1985), chapter 2.

9. Programs exist for the District of Columbia, American territories, and federal employees. There is also a federally-operated program for maritime workers.

10. States have various special funds which provide certain kinds of supplementary benefits. The most common is a "second injury" fund for workers who have been previously injured and whose earlier injury is aggravated by a subsequent injury. Such funds are designed to avoid disincentives to employers to the hiring of injured workers on the grounds that their previous injuries will increase employer exposure to the risk of additional claims. Apart from supplements to workers' compensation, a few states have temporary disability funds. Under these programs, workers are able to collect benefits for injuries not covered by workers' compensation (not caused at work) which prevent them from working. There is some evidence that workers' compensation costs are higher - other things equal - in states which operate insurance funds directly competitive with private insurance. See Alan B. Krueger and John F. Burton, Jr., "The Employers' Costs of Workers' Compensation Insurance: Magnitudes, Determinants, and Public Policy," working paper no. 3029, National Bureau of Economic Research, July 1989.

11. Nicholas Askounes Ashford, Crisis in the Workplace: Occupational Disease and Injury (Cambridge, Mass.: MIT Press, 1976), pp. 388-389.

12. Peter S. Barth and H. Allan Hunt, Workers' Compensation and Work-Related Illnesses and Diseases (Cambridge, Mass.: MIT Press, 1980), p. 187.

13. A self-insured employer obviously bears the risk of claims on a dollar-for-dollar basis. Employers covered through insurance carriers face more complex situations. Very small employers may not be experience rated, since their claims are too few for a carrier to evaluate their riskiness. Instead, they pay state-designated rates based on their industry. Larger firms can arrange for experience rated coverage. However, the formulas used seem to provide more than a dollar's premium reduction for each dollar of claims saved by accident avoidance. In a competitive insurance market, the cross subsidy from high risk to low risk employers

would not occur. High risk firms would be quoted lower rates than under the current system, and therefore the cross subsidy would be eliminated. However, the cross subsidy prevails because the insurance is sold under detailed state regulation. See Richard B. Victor, Workers' Compensation and Workplace Safety: The Nature of Employer Financial Incentives, report R-2979-ICJ (Santa Monica, Calif.: Rand Corporation, 1982).

14. Richard B. Victor, Linda R. Cohen, and Charles E. Phelps, Workers' Compensation and Workplace Safety, report R2918-ICJ (Santa Monica, Calif.: Rand Corporation, 1982).

15. Robert L. Kahn, "Work, Stress, and Health" in Barbara D. Dennis, ed., Proceedings of the Thirty-Third Annual Meeting, Industrial Relations Research Association, September 5-7, 1980 (Madison, Wisc.: IRRA, 1981), pp. 257-267.

16. Daniel M. Kasper, "An Alternative to Workmen's Compensation," Industrial and Labor Relations Review, vol. 28 (July 1975), pp. 535-548. Kasper argues for a system under which both the employer and employee carry insurance and fault is determined by courts.

17. For example, under workers' compensation, there are no damages for "pain and suffering."

18. Ronald G. Ehrenberg, "Workers' Compensation, Wages, and the Risk of Injury" in John F. Burton, Jr., New Perspectives in Workers' Compensation (Ithaca, N.Y.: ILR Press, 1988), pp. 71-96; Alan B. Krueger, "Incentive Effects of Workers' Compensation Insurance," working paper no. 3089, National Bureau of Economic Research, August 1989; Alan B. Krueger, "Workers' Compensation Insurance and the Duration of Injuries," working paper no. 3253, National Bureau of Economic Research, February 1990.

19. U.S. Bureau of Labor Statistics, Employment Cost Indexes and Levels, 1975-92, bulletin 2413 (Washington: GPO, 1992), p. 91.

20. Martin W. Elson and John F. Burton, Jr., "Workers' Compensation Insurance: Recent Trends in Employer Costs," Monthly Labor Review, vol. 104 (March 1981), pp. 45-50.

21.Detailed information about the various state systems can be found in Analysis of Workers' Compensation Laws, an annual publication of the U.S. Chamber of Commerce. Updates on state programs are also reported annually in the Monthly Labor Review.

22. The State of Wisconsin had initiated, but had not implemented, an unemployment insurance plan prior to 1935. Some unions had informal unemployment benefit plans for members prior to the 1930s. And a few companies had initiated plans for their employees. The joint federal-state nature of unemployment insurance means that the system's taxes and benefits are part of the federal budget, despite

the major role played by states in administering the programs. Proponents of the UI system have called for its removal from the federal budget because its inclusion allegedly causes Congress to restrict the program out of concern with the overall federal deficit. See National Commission on Unemployment Compensation, Unemployment Compensation: Final Report (Washington: GPO, 1980), pp. 103-104.

23. Denton Marks, "Incomplete Experience Rating in State Unemployment Insurance," Monthly Labor Review, vol. 107 (November 1984), pp. 45-49. The net subsidy goes to industries such as construction and agriculture with strong seasonal unemployment patterns. See Clair Vickery, "Unemployment Insurance: A Positive Appraisal," Industrial Relations, vol. 18 (Winter 1979), pp. 1-17, especially pp. 6-8.

24. A study of UI claims in Pennsylvania and Missouri found that over 30% of the weeks of unemployment of UI recipients ended in recall from layoff. Some workers expected to be recalled when they initially became unemployed, but were subsequently disappointed. Because they expected recall, their search for alternative work was attenuated. See Lawrence F. Katz and Bruce D. Meyer, "Unemployment Insurance, Recall Expectations and Unemployment Outcomes," working paper no. 2594, National Bureau of Economic Research, 1988.

25. Although only two states explicitly pay benefits to strikers, some others have rules under which workers laid off because of a strike may receive benefits if they are not directly involved in the dispute. It has been argued that such arrangements may increase strike frequency. See Robert Hutchens, David Lipsky, and Robert Stern, "Unemployment Insurance and Strikes," Journal of Labor Research, vol. 13 (Fall 1992), pp. 337-351.

26. Annual summaries of the state programs can be found in Highlights of State Unemployment Compensation Laws, a publication of the National Foundation for Unemployment Compensation and Workers' Compensation. Other sources of data include the Social Security Bulletin and Unemployment Insurance Statistics. Updates of state UI programs are reported annually in the Monthly Labor Review.

27. Not all job losers are eligible for UI; that depends on their work histories. Thus, the ratio of UI recipients to job losers exceeds 100% in some years.

28. Rebecca Blank and David Card, "Recent Trends in Insured and Uninsured Unemployment: Is There an Explanation?, working paper no. 2871, National Bureau of Economic Research, March 1989.

29. Because Social Security benefits are nontaxable for low income recipients and only partially taxable for higher income recipients, the after-tax ratios of benefits to active wages would be higher.

In addition, married couples receive two payments, typically based on the husband as retiree and the wife as spouse. The average husband-plus-wife benefit was about half of active worker monthly earnings.

30. Sar A. Levitan, Peter E. Carlson, and Isaac Shapiro, Protecting American Workers (Washington: Bureau of National Affairs, 1986), pp. 192-193; Laurence J. Kotlikoff, Avia Spivak, and Lawrence H. Summers, "The Adequacy of Savings," American Economic Review, vol. 72 (December 1982), pp. 1056-1069.

31. Daniel J.B. Mitchell, "Social Insurance and Welfare" in David Lewin, Olivia S. Mitchell, and Peter D. Sherer, Research Frontiers in Industrial Relations and Human Resources (Madison, Wisc.: IRRA, 1992), pp. 596-597.

32. U.S. Advisory Council on Social Security, Commitment to Change: Foundation for Reform (Washington: Advisory Council on Social Security, 1991), p. 21.

33. Henry J. Aaron, Economic Effects of Social Security (Washington: Brookings Institution, 1982), chapter 4.

34. A Presidential commission appointed by the Carter administration recommended a system of mandatory minimum pensions. Under this proposal, employers would have either set up their own pension plans or contributed to a federally-operated supplement to Social Security. See President's Commission on Pension Policy, Coming of Age: Toward a National Retirement Income Policy, February 1981, pp. 42-45.

35. Under 401(k) plans, employees voluntarily reduce their take-home pay and the resulting monies go into a savings plan, thus avoiding current taxation. Changes in the tax code lowered the ceiling on amounts that could be diverted into tax-sheltered savings. IRA accounts were individually established, rather than employer based (although some employers offered IRA arrangements). Payments to IRAs, subject to various limitations, are made in pre-tax dollars. Tax code changes made higher paid employees who were covered by pensions at their job ineligible for most of the benefits of IRAs.

36. Because of the indexing feature of Social Security, the popular image of a retired person living on a "fixed income" is misleading. Social Security is likely to be an important part of a retiree's income, and it is not fixed in nominal dollars.

37. Alan L. Gustman and Thomas L. Steinmeier, "An Analysis of Pension Benefit Formulas, Pension Wealth and Incentives from Pensions," working paper no. 2535, March 1988.

38. Under the efficiency wage model, the firm pays a lower-than-productivity wage early in a worker's career, compensated by a higher-than-productivity wage at the end. The higher pay later in the career functions as a reward for loyal and satisfactory service, and as a "bond" which the worker can lose (through dismissal for unsatisfactory performance). Defined benefit pension plans could function as efficiency wages, since their value to the worker increases with service. It is difficult to confirm the presence of efficiency wages directly, since employee marginal productivity must be measured. One study finds a lack of evidence for the efficiency wage model, in terms of cash wages, but raises the possibility that benefits (such as pensions) could be the efficiency wage/bond. See Katharine G. Abraham and Henry S. Farber, "Job Duration, Seniority, and Earnings," American Economic Review, vol. 77 (June 1987), pp. 278-297, especially p. 295. See also Laurence J. Kotlikoff and David A. Wise, The Wage Carrot and the Pension Stick: Retirement Benefits and Labor Force Participation (Kalamazoo, Mich.: Upjohn Institute, 1989).

39. A review of this issue can be found in Aaron, Economic Effects of Social Security, op. cit., chapter 5.

40. Jon R. Moen, "Past and Current Trends in Retirement: American Men from 1860 to 1980," Economic Review, Federal Reserve Bank of Atlanta, vol. 73 (August 1988), pp. 16-27.

41. Gary Burtless, "Social Security, Unanticipated Benefit Increases, and the Timing of Retirement," Review of Economic Studies, vol. 53 (October 1986), pp. 781-805.

42. Malcolm H. Morrison, "The Aging of the U.S. Population: Human Resource Implications," Monthly Labor Review, vol. 106 (May 1983), pp. 13-19.

43. A qualification to this statement is that workers may not have a clear idea of exactly what their pension benefits are. See Olivia S. Mitchell, "Worker Knowledge of Pension Provisions," working paper no. 2414, National Bureau of Economic Research, October 1987.

44. Under federal regulations, providing less than first-dollar coverage to older, Medicare-covered workers is considered to be illegal age discrimination, if the firm offers health insurance to younger workers.

45. Material in this section is drawn from Donald Bell and Diane Hill, "How Social Security Payments Affect Private Pensions," Monthly Labor Review, vol. 107 (May 1984), pp. 15-20.

46. U.S. Bureau of Labor Statistics, Employee Benefits in Medium and Large Establishments, 1991, bulletin 2422 (Washington: GPO, 1993), p. 91.

47. The complex integration formulas partially reflect tax code restrictions. To qualify for tax-favored treatment, pensions are not supposed to be biased towards higher paid workers. Social Security, however, tilts its benefits toward the lower paid. Formulas used for integration effectively reverse some of this tilt, but are designed not to do so in a manner offensive to the tax code.

48. The median voter model was discussed in an earlier chapter.

49. A progressive tax is one under which higher income individuals pay a greater proportion of their income in taxes. A "regressive" tax is the opposite; higher income individuals pay a lower proportion of their income in taxes. As will be noted below in the text, the payroll taxes supporting UI and Social Security are regressive.

50. Walter J. Blum and Harry Kalven, Jr., The Uneasy Case for Progressive Taxation (Chicago: University of Chicago Press, 1953).

51. Wages are set relatively infrequently - yearly or longer - and, hence, do not immediately shift in response to a payroll tax increase. In a long-duration model of wage setting, however, the employer can recoup the tax in some future round of pay setting by simply slowing the rate of nominal wage increase.

52. There can be various explanations of a low elasticity of labor supply with respect to the wage. It could be that employees see little substitution between wages and "leisure," i.e., hours not supplied to the labor market. If the income effect of the tax imposed is low, the lack of substitution and income reactions will produce a low supply elasticity. However, it is also possible to have a high level of substitutability between wages and leisure whose effect is offset by a large positive income effect. When the payroll tax is imposed, the leisure effect tends to reduce hours supplied to the labor market, but the income effect (less leisure demanded as income falls) works in the opposite direction. One study concludes that the inelasticity of labor supply is the result of just such an offset. See Jerry A. Hausman, "Labor Supply" in Henry J. Aaron and Joseph A. Pechman, eds., How Taxes Affect Economic Behavior (Washington: Brookings Institution, 1981), pp. 27-83.

53. John A. Brittain, The Payroll Tax for Social Security (Washington: Brookings Institution, 1972); Richard F. Dye, "Payroll Tax Effects on Wage Growth," Eastern Economic Journal, vol. 11 (April-June 1985), pp. 89-100; Jonathan Gruber and Alan B. Krueger, "The Incidence of Mandated Employer-Provided Insurance: Lessons from Workers' Compensation Insurance," working paper no. 3557, National Bureau of Economic Research, December 1990.

54. For example, when the Congressional Budget Office was called upon to estimate costs of competing plans for health insurance, it assumed the cost incidence would fall on labor. See Congressional Budget Office, "Estimates of Health Care Proposals from the 102nd Congress," CBO papers, July 1993, p. 3.

55. The tax rate is calculated on the after-tax wage which lies along the demand curve D'. Hence, the old demand curve D can be expressed as D' + D't or D'(1+t). And, therefore, D' = D/(1+t). Thus, if in the absence of the tax, the wage would be $10 per hour, a tax rate of 10% would lead to a take-home wage of $10/1.1 = $9.09.

56. One empirical study asserts that workers' compensation premiums reduce nonunion wages on a dollar-for-dollar basis, but found no such tradeoff for union workers. The argument made was that for nonunion workers, the presence of (value of) workers' compensation payments offsets the job hazard premiums that employers would otherwise have had to pay. See Stuart Dorsey and Norman Walzer, "Workers' Compensation, Job Hazards, and Wages," <u>Industrial and Labor Relations Review</u>, vol. 36 (July 1983), pp. 642-654.

57. There is an offsetting effect, namely that lower Social Security earnings will eventually produce lower benefits for the employee, upon retirement or disability.

58. Arthur M. Okun, <u>Equality and Efficiency: The Big Tradeoff</u> (Washington: Brookings Institution, 1975), pp. 91-95.

59. There is an issue of whether employers - in the context of implicit contracting and infrequently adjusted wages - anticipate payroll tax increases in setting pay. If they do, even though compensation may blip up when the tax is first imposed, the tax burden may still fall on wages. Suppose, for example, a firm sets its wage each July 1 for the next 12 months. Suppose further that it knows that on the next January 1, payroll taxes will be increased by 1%. It might set its July-to-June wage 0.5% lower than otherwise, e.g., grant a 3.5% increase rather than a 4% increase, to "cover" the tax burden. (One percent over 6 months is equivalent to 0.5% over 12 months). On January 1, the firm's compensation would still blip up when the added tax was imposed, but the firm is not absorbing the tax.

60. Daniel J.B. Mitchell, "Social Insurance and Benefits" in David Lewin, Olivia S. Mitchell, and Peter D. Sherer, eds., <u>Research Frontiers in Industrial Relations and Human Resources</u> (Madison, Wisc.: IRRA, 1992), pp. 595-596, 604-609.

61. U.S. Bureau of the Census, <u>Statistical Abstract of the United States: 1992</u> (Washington: GPO, 1992), p. 105.

62. U.S. Buréau of the Census, Statistical Abstract of the United States: 1992 (Washington: GPO, 1992), pp. 97, 825, 829.

63. U.S. Bureau of the Census, Statistical Abstract of the United States: 1992 (Washington: GPO, 1992), p. 100.

64. Daniel J.B. Mitchell and Jacques Rojot, "Employee Benefits and the Single Market" in Lloyd Ulman, Barry Eichengreen, and William T. Dickens, eds., Labor and an Integrated Europe (Washington: Brookings Institution, 1993), pp. 128-166.

65. The National Industrial Recovery Act of 1933 (NIRA) organized firms into industrial groupings which worked out "codes" of conduct with governmental approval. These NIRA codes contained minimum wage and hour standards, pursuant to an economic theory prevalent at the time that pushing up nominal wages would raise consumption and speed recovery from the depression. The wage-consumption theory was controversial among economists of the time and would not be widely accepted today, although for different reasons. For discussion, see Daniel J.B. Mitchell, "Wages and Keynes: Lessons from the Past," Eastern Economic Journal, vol. 12 (July-September 1986), pp. 199-208.

66. U.S. Bureau of the Census, Statistical Abstract of the United States: 1992 (Washington: GPO, 1992), p. 415.

67. Congress covered certain state and local workers in the 1966 FLSA amendments. The bulk of the others were covered in 1974. However, a U.S. Supreme Court decision prevented coverage of state and local employees until the Court reversed itself in 1985.

68. Reviews of the economic literature can be found in Charles Brown, Curtis Gilroy, and Andrew Cohen, "The Effect of the Minimum Wage on Employment and Unemployment," Journal of Economic Literature, vol. 20 (June 1982), pp. 487-528; Finis Welch, Minimum Wages: Issues and Evidence (Washington: American Enterprise Institute, 1978); Donald O. Parsons, Poverty and the Minimum Wage (Washington: American Enterprise Institute, 1980); U.S. General Accounting Office, Minimum Wage Policy Questions Persist, GAO/PAD-83-7 (Washington, GAO, 1983).

69. There is empirical evidence of such a queue. See Harry J. Holzer, Lawrence F. Katz, and Alan B. Krueger, "Job Queues and Wages: New Evidence on the Minimum Wage and Inter-Industry Wage Structure," working paper no. 2561, April 1988.

70. Masanori Hashimoto, "Minimum Wage Effects on Training on the Job," American Economic Review, vol. 72 (December 1982), pp. 1070-1087.

71. John F. Cogan, "The Decline in Black Teenage Employment: 1950-1970," American Economic Review, vol. 72 (September 1982), pp. 621-638. Cogan emphasizes the decline in agriculture but does indicate that the minimum wage interfered with finding alternative (nonfarm) employment.

72. Teenagers are barred from designated occupations involving potential work hazards. Some states, however, have special school-supervised programs approved by the U.S. Department of Labor permitting such work for 14-15 year olds identified as potential dropouts. More information on child labor laws can be found in Daniel J.B. Mitchell and John Clapp, Legal Constraints on Teenage Employment: A New Look at Child Labor and School Leaving Laws (Los Angeles: UCLA Institute of Industrial Relations, 1979).

73. See the symposium on "New Minimum Wage Research" in Industrial and Labor Relations Review, vol. 46 (October 1992), pp. 3-88.

74. Ralph E. Smith and Bruce Vavrichek, "The Minimum Wage: Its Relation to Incomes and Poverty," Monthly Labor Review, vol. 110 (June 1987), pp. 24-30.

75. U.S. Bureau of the Census, Statistical Abstract of the United States: 1992 (Washington: GPO, 1992), p. 415.

76. It may seem that practically no one would sell themselves into slavery, and, hence, that the prohibition has no human resource management implications. However, in some cases, the slavery prohibition prevents enforcement of certain kinds of labor contracts. Individuals who contract to perform a service, and then refuse to do so, cannot be compelled by law to perform the service. But they can be sued for damages resulting from nonperformance. Although strict slavery is a lifetime arrangement, even short-term contracts involving performance of work will not be enforced.

77. Jean Baldwin Grossman, "The Impact of the Minimum Wage on Other Wages," Journal of Human Resources, vol. 18 (Summer 1983), pp. 359-378.

78. Employers must obtain certificates from the U.S. Department of Labor to pay sub-minimum wages to such groups.

79. The U.S. Chamber of Commerce has supported a youth differential. However, a difficulty - from the public policy viewpoint - is that such a differential would encourage substitution of teenagers for low-wage adults, although - as noted in the text - the latter group has a much higher poverty rate. In a book sponsored by a Chamber-affiliated foundation, economist Belton M. Fleisher disagreed with the Chamber's view on this issue. See Belton M. Fleisher, Minimum Wage Regulation in the United States (Washington: National Chamber Foundation, 1983), p. 4.

80. State and local workers can be paid in "comp time," rather than cash, at a rate of time-and-a-half for overtime. Comp time means time off for personal leave. Thus, a state and local worker with two hours of overtime in a given week can take off 3 hours at a later date.

81. Stephen J. Trejo, "Does the Statutory Overtime Premium Discourage Long Workweeks?," paper dated April 1992 given to the Public Finance-Labor-Econometrics Workshop, UCLA Department of Economics, May 12, 1992.

82. Of course, the aggregate average overtime/worker figure includes some firms which make extensive use of overtime and others which do not use it at all.

83. Until 1985, federal contractors under Walsh-Healey had to pay overtime after 8 hours per day, rather than the looser FLSA standard of 40 hours per week. Legislation passed in late 1985 ended the requirement.

84. Some state governments have similar laws for their contractors.

85. Steven G. Allen and David Reich, Prevailing Wage Laws Are Not Inflationary: A Case Study of Public School Construction Costs (Washington: Center to Protect Workers' Rights, 1980); The GAO on Davis-Bacon: A Fatally Flawed Study (Washington: Center to Protect Workers' Rights, 1979).

86. U.S. General Accounting Office, The Davis-Bacon Act Should Be Repealed, HRD-79-18 (Washington: GAO, 1979); U.S. General Accounting Office, The Congress Should Consider Repeal of the Service Contract Act, GAO/HRD-83-4 (Washington: GAO, 1983). Relatively few research studies of such laws have been completed. Among them are Armand J. Thieblot Jr., The Davis-Bacon Act, Industrial Research Unit, Wharton School (Philadelphia: University of Pennsylvania Press, 1975); John P. Gould and George Bittlingmayer, The Economics of the Davis-Bacon Act: An Analysis of Prevailing-Wage Laws (Washington: American Enterprise Institute, 1980); Armand J. Thieblot Jr., Prevailing Wage Legislation: The Davis-Bacon Act, State "Little Davis-Bacon" Acts, and the Service Contract Act (Philadelphia: Industrial Research Unit, Wharton School, University of Pennsylvania, 1986).

87. Herbert R. Northrup, "The 'Helper' Controversy in the Construction Industry," Journal of Labor Research, vol. 13 (Fall 1992), pp. 421-435.

88. For a history of the enactment of OSHA, see Judson MacLaury, "The Job Safety Law of 1970: Its Passage Was Perilous," Monthly Labor Review, vol. 104 (March 1981), pp. 18-24.

89. John D. Worrall and Richard J. Butler, "Health Conditions and Job Hazards: Union and Nonunion Jobs," Journal of Labor Research, vol. 4 (Fall 1983), pp. 339-347.

90. This notion has been called the "ratcheting" approach. See James C. Miller III, "Is Organized Labor Rational in Supporting OSHA?," Southern Economic Journal, vol. 50 (January 1984), pp. 881-885.

91. Miller, "Is Organized Labor Rational in Supporting OSHA?," op. cit., pp. 881-885. Miller notes that unions share OSHA's preference for engineering controls (modifications to equipment) rather than personal protective devices (such as earplugs). The latter would act as a "tax" on labor, rather than capital, thus reducing the demand for labor through both the substitution and output effects. (Usually, the preference for equipment modification is defended on the grounds that workers may fail to wear the protective devices given to them).

92. Norman Root and Deborah Sebastian, "BLS Develops Measure of Job Risk by Occupation," Monthly Labor Review, vol. 104 (October 1981), pp. 26-30.

93. James C. Robinson, "Hazardous Occupations Within the Job Hierarchy," Industrial Relations, vol. 27 (Summer 1988), pp. 241-250. Robinson finds evidence of such a downshifting of risk. But note that the argument assumes that low-paid workers will receive absolutely smaller risk premiums than high-paid workers.

94. Various empirical studies are reviewed in William T. Dickens, "Differences Between Risk Premiums in Union and Nonunion Wages and the Case for Occupational Safety Regulation," American Economic Review, vol. 74 (May 1984), pp. 320-323.

95. Stuart Dorsey and Norman Walzer, "Workers' Compensation, Job Hazard, and Wages," Industrial and Labor Relations Review, vol. 36 (July 1983), pp. 642-654.

96. W. Kip Viscusi and Charles J. O'Connor, "Adaptive Responses to Chemical Labeling: Are Workers Bayesian Decision Makers?," American Economic Review, vol. 74 (December 1984), pp. 942-956.

97. J. Paul Leigh, "Compensating Wages for Occupational Injuries and Diseases," Social Science Quarterly, vol. 62 (December 1981), pp. 772-778.

98. Charles L. Schultze, The Public Use of Private Interest (Washington: Brookings Institution, 1977), pp. 55-57; John Mendeloff, Regulating Safety: An Economic and Political Analysis of Occupational Safety and Health Policy (Cambridge, Mass.: MIT Press, 1979).

99. Lawrence S. Bacow, "Private Bargaining and Public Regulation" in Eugene Bardach and Robert A. Kagan, eds., Social Regulation: Strategies for Reform (San Francisco: Institute for Contemporary Studies, 1982), pp. 201-220.

100. Lester B. Lave, The Strategy of Social Regulation: Decision Frameworks for Policy (Washington: Brookings Institution, 1981), pp. 99-101.

101. Suggestions along these lines can be found in John Mendeloff, "Regulatory Reform and OSHA Policy," Journal of Policy Analysis and Management, vol. 5 (Spring 1986), pp. 440-468.

102. These data are kept confidential and are not available to OSHA enforcement officials. Employers are also required to keep logs of injuries which are available for inspection.

103. Information on average duration of lost workday injuries can be found in Martin E. Personick and Ethel C. Jackson, "Recuperation Time for Work Injuries, 1987-91," Monthly Labor Review, vol. 116 (April 1993), pp. 33-35.

104. Levitan, Carlson, and Shapiro, Protecting American Workers, op. cit., pp. 119-123. Estimates of workplace fatalities from various sources vary widely. As a result, the Bureau of Labor Statistics has begun collecting data from various sources in participating states such as OSHA records, workers' compensation reports, death certificates, etc. A typical death victim seems to be a white male, aged 25-44, in a blue collar occupation. About a fourth of all fatalities resulted from transportation accidents, varying from highway collisions to accidents involving within-plant vehicles. It is hoped that reports will become available for all states during the 1990s. Source: Guy Toscano and Janice Windau, "Fatal Work Injuries: Census for 31 States," Monthly Labor Review, vol. 115 (September 1992), pp. 3-8.

105. William P. Curington, "Safety Regulations and Workplace Injuries," Southern Economic Journal, vol. 53 (July 1986), pp. 51-72.

106. Michael L. Marlow, "The Economics of Enforcement: The Case of OSHA," Journal of Economics and Business, vol. 34 (2:1982), pp. 165-171.

107. Robert S. Smith, "Have OSHA and Workers' Compensation Made the Workplace Safer?" in David Lewin, Olivia S. Mitchell, and Peter D. Sherer, eds., Research Frontiers in Industrial Relations and Human Resources (Madison, Wisc.: IRRA, 1992), p. 564.

Appendix

Occupational Safety, Fetal Protection, and EEO

In 1991, the U.S. Supreme Court heard the Johnson Controls case involving a potential conflict between safety at work and EEO protections.[1] Specifically, a battery manufacturing company had adopted rules forbidding women of childbearing potential to work in jobs which involved significant lead exposure. The company cited possible harm to fetuses of fertile women who might take such work. Lead is an important component of batteries and the denial of the right to work with lead meant that certain higher-paying jobs were off-limits to many women. A fertile woman would have to undergo sterilization under these rules in order to obtain such jobs.

Since the ban did not apply to men, the company rules appeared to be a type of sex discrimination barred by Title VII of the Civil Rights Act of 1964. (See the next chapter for more details.) On the other hand, job safety is also a public policy under OSHA. But whose safety is protected by OSHA, an employee's or the unborn child of an employee? And is the decision to risk the health of an unborn child properly made by its mother or her employer? Obviously, this was a case raising a variety of larger social and ethical questions.

When the employer's policies were challenged as sex discrimination, it was successful in defending those policies at the federal district court and court of appeals levels. Yet the Supreme Court did not agree with the lower court decisions and reversed them, finding the Johnson Controls' fetal protection policies were indeed a form of illegal sex discrimination.

Below is an edited version of the majority opinion of the Supreme Court. Read the opinion and consider:

1) The appropriate trade off that you would make in this difficult case.

2) The implications of the Supreme Court's decision for employers and female employees in matters related to pregnancy.

Edited Majority Decision:[2]

In this case we are concerned with an employer's gender-based fetal-protection policy. May an employer exclude a fertile female

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[1] UAW v. Johnson Controls, Inc., 111 S. Ct. 1196 (1991).

[2] The reader is cautioned that the text below has been heavily edited to highlight certain issues and omit legal details. Deletions and changes in wording are not indicated. Those interested in the exact wording should consult the original decision.

employee from certain jobs because of its concern for the health of the fetus the woman might conceive?

Johnson Controls, Inc., manufactures batteries. In the manufacturing process, the element lead is a primary ingredient. Occupational exposure to lead entails health risks, including the risk of harm to any fetus carried by a female employee. Before the Civil Rights Act of 1964 became law, Johnson Controls did not employ any woman in a battery-manufacturing job. In June 1977, however, it announced its first official policy concerning its employment of women in lead-exposure work: "Protection of the health of the unborn child is the immediate and direct responsibility of the prospective parents. While the medical profession and the company can support them in the exercise of this responsibility, it cannot assume it for them without simultaneously infringing their rights as persons.

Consistent with that view, Johnson Controls stopped short of excluding women capable of bearing children from lead exposure, but emphasized that a woman who expected to have a child should not choose a job in which she would have such exposure. The company also required a woman who wished to be considered for employment to sign a statement that she had been advised of the risk of having a child while she was exposed to lead. The statement informed the woman that although there was evidence "that women exposed to lead have a higher rate of abortion," this evidence was "not as clear... as the relationship between cigarette smoking and cancer," but that it was, "medically speaking, just good sense not to run that risk if you want children and do not want to expose the unborn child to risk, however small..."

Five years later, in 1982, Johnson Controls shifted from a policy of warning to a policy of exclusion. Between 1979 and 1983, eight employees became pregnant while maintaining blood lead levels in excess of 30 micrograms per deciliter. This appeared to be the critical level noted by the Occupational Health and Safety Administration (OSHA) for a worker who was planning to have a family. The company responded by announcing a broad exclusion of women from jobs that exposed them to lead:

"...It is [Johnson Controls'] policy that women who are pregnant or who are capable of bearing children will not be placed into jobs involving lead exposure or which could expose them to lead through the exercise of job bidding, bumping, transfer or promotion rights."

The policy defined "women... capable of bearing children" as "all women except those whose inability to bear children is medically documented." It further stated that an unacceptable work station was one where, "over the past year," an employee had recorded a blood lead level of more than 30 micrograms per deciliter or the work site had yielded an air sample containing a lead level in excess of 30 micrograms per cubic meter.

In April 1984, petitioners filed in the United States District

Court for the Eastern District of Wisconsin a class action challenging Johnson Controls' fetal-protection policy as sex discrimination that violated Title VII of the Civil Rights Act of 1964, as amended. Among the individual plaintiffs were petitioners Mary Craig, who had chosen to be sterilized in order to avoid losing her job, Elsie Nason, a 50-year-old divorcee, who had suffered a loss in compensation when she was transferred out of a job where she was exposed to lead, and Donald Penney, who had been denied a request for a leave of absence for the purpose of lowering his lead level because he intended to become a father.

The District Court granted summary judgment for Johnson Controls. It concluded that while "there is a disagreement among the experts regarding the effect of lead on the fetus," the hazard to the fetus through exposure to lead was established by "a considerable body of opinion"; that although "expert opinion has been provided which holds that lead also affects the reproductive abilities of men and women... [and] that these effects are as great as the effects of exposure of the fetus... a great body of experts are of the opinion that the fetus is more vulnerable to levels of lead that would not affect adults"; and that petitioners had "failed to establish that there is an acceptable alternative policy which would protect the fetus." The Court of Appeals for the Seventh Circuit affirmed the District Court's judgment.

Specifically, the Court of Appeals concluded that there was no genuine issue of material fact about the substantial health-risk factor because the parties agreed that there was a substantial risk to a fetus from lead exposure. The Court of Appeals also concluded that, unlike the evidence of risk to the fetus from the mother's exposure, the evidence of risk from the father's exposure, which petitioners presented, "is, at best, speculative and unconvincing."

The bias in Johnson Controls' policy is obvious. Fertile men, but not fertile women, are given a choice as to whether they wish to risk their reproductive health for a particular job. The Civil Rights Act of 1964, prohibits sex-based classifications in terms and conditions of employment, in hiring and discharging decisions, and in other employment decisions that adversely affect an employee's status.

Johnson Controls' policy classifies on the basis of gender and childbearing capacity, rather than fertility alone. Respondent does not seek to protect the unconceived children of all its employees. Despite evidence in the record about the debilitating effect of lead exposure on the male reproductive system, Johnson Controls is concerned only with the harms that may befall the unborn offspring of its female employees. We hold that Johnson Controls' fetal-protection policy is sex discrimination forbidden under Title VII unless respondent can establish that sex is a "bona fide occupational qualification (BFOQ)." Therefore, we turn to the question whether Johnson Controls' fetal-protection policy is one of those "certain instances" that come within the BFOQ exception.

BFOQs are limited to certain special instances where sex discrimination is reasonably necessary to the normal operation of the particular business. But the most telling term is "occupational"; this indicates that these objective, verifiable requirements must concern job-related skills and aptitudes. Johnson Controls argues that its fetal-protection policy falls within the so-called safety exception to the BFOQ. But the unconceived fetuses of Johnson Controls' female employees are neither customers nor third parties whose safety is essential to the business of battery manufacturing. No one can disregard the possibility of injury to future children; the BFOQ, however, is not so broad that it transforms this deep social concern into an essential aspect of battery making. Women as capable of doing their jobs as their male counterparts may not be forced to choose between having a child and having a job.

We have no difficulty concluding that Johnson Controls cannot establish a BFOQ. Fertile women, as far as appears in the record, participate in the manufacture of batteries as efficiently as anyone else. Johnson Controls' professed moral and ethical concerns about the welfare of the next generation do not suffice to establish a BFOQ of female sterility. Decisions about the welfare of future children must be left to the parents who conceive, bear, support, and raise them rather than to the employers who hire those parents. Congress has mandated this choice.

A word about tort liability (in the event of a job-related birth defect) and the increased cost of fertile women in the workplace is perhaps necessary. More than 40 States currently recognize a right to recover for a prenatal injury based either on negligence or on wrongful death. According to Johnson Controls, however, the company complies with the lead standard developed by OSHA and warns its female employees about the damaging effects of lead. It is worth noting that OSHA gave the problem of lead lengthy consideration and concluded that "there is no basis whatsoever for the claim that women of childbearing age should be excluded from the workplace in order to protect the fetus or the course of pregnancy." Instead, OSHA established a series of mandatory protections which, taken together, "should effectively minimize any risk to the fetus and newborn child." Without negligence, it would be difficult for a court to find liability on the part of the employer. If, under general tort principles, Title VII bans sex-specific fetal-protection policies, the employer fully informs the woman of the risk, and the employer has not acted negligently, the basis for holding an employer liable seems remote at best.

Our holding today that Title VII forbids sex-specific fetal-protection policies is neither remarkable nor unprecedented. Concern for a woman's existing or potential offspring historically has been the excuse for denying women equal employment opportunities. It is no more appropriate for the courts than it is for individual employers to decide whether a woman's reproductive role is more important to herself and her family than her economic role. Congress has left this choice to the woman as hers to make. The judgment of the Court of Appeals is reversed.