

Statement of Dr. Anne Layne-Farrar

U.S. Senate Committee on Health, Education, Labor, and Pensions Hearing on Rebuilding Economic Security: Empowering Workers to Restore the Middle Class

March 10, 2009

Thank you for the opportunity to present the findings of my empirical analysis of the Employee Free Choice Act. In this statement I will summarize the findings presented in detail in my study entitled “An Empirical Assessment of the Employee Free Choice Act: The Economic Implications” (referred to hereinafter as “Economic Implications”).¹

Before turning to the empirical findings in “Economic Implications”, consider first the provisions contained in Employee Free Choice Act (EFCA). Renowned law and economics scholar, Professor Richard A. Epstein,² describes in detail the two primary provisions of EFCA in his manuscript entitled “The Case Against the Employee Free Choice Act,” which is due to be published soon by the Hoover Institution of Stanford University. Specifically, Epstein explains the majority sign-up, or “card check” provision in EFCA as follows:

The first proposal would allow either party the option to substitute a card-check system for the current electoral system. To be sure, the EFCA leaves in place the present NLR provisions that allow unions to proceed by filing a representation petition supported by 30 percent or more of employees in an appropriate bargaining unit and then holding elections. Nonetheless, it seems clear that in virtually all cases the card check will displace the secret ballot. As a matter of current practice, virtually all major unions choose to file representation petitions only after they have accumulated signed authorization cards from well over 50 percent of unit members. They need that cushion because they know from experience that worker defections will take place during the course of any election campaign in which management can present its own case of the tradeoffs, costs and disadvantages of representation. It follows therefore that no rational union would risk the election if they have in their possession authorization cards from just over 50 percent of the members of the unit they seek to represent. As a practical matter however, the EFCA would wholly displace union elections with the new “card check” procedure. No union is likely to file for an election with over 30 but under 50 percent of signed authorization cards in the hopes of improving its position during a campaign. The conversion to the card check system is likely to prove well-nigh complete.

¹ A copy of the study is attached to this statement for your reference.

² Richard A. Epstein is the James Parker Hall Distinguished Professor of Law, The University of Chicago; the Peter and Kirsten Bedford Senior Fellow, The Hoover Institution, and a visiting professor a New York University Law School.

In regards to the second major provision of EFCA, Epstein writes:

EFCA's second major provision would introduce a system of compulsory interest arbitration that leads to a first "contract" of two years duration. The term contract is put in quotation marks because an actual agreement that obtains the assent of both parties is not required during the initial period in question. This mandatory first contract, moreover, is not limited to wage matters, but must cover all the issues that are typically hammered out by agreement under the current system.

Although Epstein does not quantify his findings as I have done in my own study of EFCA, based on his analysis he concludes that:

The legislative adoption of these provisions taken together, would radically alter the balance of power between management and labor. Its impact would extend to virtually all businesses, except for some small businesses that fall below the "interstate commerce" thresholds that the NLRB applies in exercise of its own jurisdiction. But even those exemptions have little relevance to any new firm that hopes to grow over time. The bottom line therefore is that the passage of the EFCA will create huge dislocations in established ways of doing business that will in turn lead to large losses in productivity.

My findings in "Economic Implications" are consistent with Professor Epstein's conclusion. "Economic Implications" presents an empirical assessment of how the two primary provisions of ECFA can be expected to affect important economic outcomes in the United States. The study finds that while card checks could be expected to increase union membership as hoped by EFCA proponents, EFCA is unlikely to achieve its primary goal of improving social welfare, which should take into account possible consequences not only for union members but for all individuals. In particular, the statistical analysis quantifies the likely impact of card checks and mandatory contract arbitration on the US unemployment and employment rates.

In terms of US unemployment, the quantitative analysis in "Economic Implications" predicts that if EFCA were passed today, then for every 3 percentage points that EFCA raised union membership this year, we could expect unemployment to increase by roughly one percentage point by the following year. Thus, if EFCA were to produce the kinds of results that some of its proponents have claimed, it could be expected to increase union membership by 5 - 10 percentage points within a year of passing.³ According to the

³ For example, Sheldon Friedman, research coordinator for the AFL-CIO, stated that EFCA "could spur an increase in U.S. union density of nearly 5 percentage points and perhaps much more." (See Sheldon Friedman, *The Limits of NLRB Certification and its Alternatives*, Labor and Employment Relations Association: Proceedings of the 58th Annual Meeting 2006, at 190. Available at <http://www.press.uillinois.edu/journals/lera/proceedings2006/friedman.html>.) Carter and Lotke, in a 2007 paper, estimated that EFCA would increase union density by approximately 10 percent. (See Alex Carter

calculations in the study, then this would result in an increase in the US unemployment rate of around 1.5 to 3 percentage points.

These are sizable effects for the US economy. To put the potential impact into context, consider this January's labor force of 153 million people, with an unemployment rate of 7.6%. From this base, a 1.5 to 3 percentage point increase in the unemployment rate would mean a new higher rate of 9.1% to 10.6%, which translates into 1.5 to 3.5 million jobs lost by January 2010, not counting any other job losses due to other factors including the current recession.

"Economic Implications" also presents estimates of EFCA's likely impact on the employment rate. The employment rate is measured as the ratio of employed people to the total population. Because some people do not count themselves in the labor force – such as those persons who are retired or are stay-at-home parents, for example – the unemployment rate and employment rate can differ from one another. It can therefore be instructive to consider both rates to obtain a more complete picture of the likely impact on the economy.

The statistical analysis in "Economic Implications" suggests that if EFCA were to increase union membership by the amounts its proponents predict, that is by 5 to 10 percentage points within a year of enactment, then we can expect the employment rate to fall by around 0.9 to 2.3 percentage points in the following year. Again, to put these figures into perspective, start from January's labor statistics. From this base, US employment would drop by 550,000 to 2.6 million jobs by 2010, not counting any losses due to the recession or other factors.

It is quite difficult to predict the economic consequences of most legislative proposals before they are enacted, let alone to quantify them as I have done in the above figures. However, with EFCA we have the benefit of observing the experience in Canada, which has experimented with both secret ballot elections and card checks. Canada is very close in both culture and industrial composition to the US, as the table below demonstrates.

Table 1: Full-Time Employment by Industry, 2007

	United States	Canada	Absolute Difference
Services	81.8%	76.3%	5.5
<i>Trade</i>	15.2%	15.9%	0.7
<i>Transportation and warehousing</i>	3.3%	4.9%	1.6
<i>Financial activities and leasing</i>	6.1%	6.3%	0.2
<i>Professional, scientific and technical</i>	5.8%	6.7%	0.9
<i>Business, building and other support</i>	7.4%	4.2%	3.2
<i>Educational services</i>	2.1%	7.0%	4.9
<i>Health care and social assistance</i>	11.0%	10.9%	0.1
<i>Information, culture and recreation</i>	3.5%	4.6%	1.1
<i>Accommodation and food services</i>	7.2%	6.3%	0.9
<i>Public admin. and Gov. enterprises</i>	15.5%	5.1%	10.4
<i>Other services</i>	4.6%	4.3%	0.3
Manufacturing	10.5%	12.1%	1.6
Construction	5.8%	6.7%	0.9
Agriculture, Forestry, Fishing, Mining, Utilities	1.9%	4.8%	2.9

With the exception of public administration and government enterprises, Canada and the US exhibit a very similar composition of labor. Public administration and government enterprises, accounting for 15.5% in the US and 5.1% in Canada, include homeland security expenditures in the US, which rose dramatically in the wake of 9-11, and is the likely driver of the one meaningful discrepancy.

The other key difference between the US and Canada is a beneficial one that can be used in statistical analysis. For most industries in Canada, union organizational rules are set at the provincial level, not at the federal level, as they are in the US. Throughout the early 1970s, all Canadian provinces employed systems of card checks. Starting in 1976, however, several Canadian provinces began to experiment with regimes that required unions to win secret ballot elections, as is commonly practiced today in the US. The new union rules coincided with provincial elections and were driven largely by changes in the political party in power in a given province rather than by economic factors. British Columbia alone changed its union certification procedure three times in the period 1976-2008: beginning with card checks from 1976-1984, moving to mandatory elections in 1984-1993, then back to card checks from 1993-2001, and finally settling on a private ballot voting system in 2001. As of 2006, half of the Canadian provinces rely on mandatory voting regimes, accounting for roughly 68% of the Canadian labor force, while the remaining half of the provinces covering 32% of the labor force continue to rely on card check systems. During this same time period, many of the provinces also introduced mandatory first contract arbitration. Thus, a number of Canadian provinces have experimented with the very changes to union organizing that are proposed in EFCA.

As a result of the provincial level changes made over time, Canada offers a natural experiment for studying and quantifying the effects of the changes proposed in EFCA. By assessing the actual experience in Canada over a 22-year time span as unionization rules changed in a number of provinces, the regression analysis in “Economic Implications”

provides a reliable prediction of what would likely happen in the US if EFCA were to become law. The regressions that provide those predictions were tested extensively, both with different estimation procedures (i.e., Ordinary Least Squares, Fixed Effects, and Random Effects) and with different model specifications (i.e., changing the variables included in the data set). The estimates are remarkably stable and consistently statically significant across the different estimations and specifications.

In addition to being robust, the results presented in “Economic Implications” are also consistent with the broader empirical academic literature. In particular, other statistical studies have found that higher unemployment is associated with higher rates of unionization.

These effects also make sense within a larger framework of economic theory. As the proponents of EFCA have pointed out, unions typically increase their members’ wages and benefits. But as union labor becomes more expensive for firms, it is natural that these firms will make changes in their production, just as they would for any other increase in costs.

First consider firms with market power. If a firm in a newly unionized industry is earning a supra-competitive level of profits, as typically would be the case with a monopoly or an oligopoly firm, then the firm may pay for the higher labor costs stemming from unionization out of company profits, without jeopardizing its return on investment. In this case, labor and management will share the profits. This appears to be the scenario that EFCA proponents have in mind.

However, because most US firms face competition from both home and across the globe, and are earning no more than a competitive return on their investments, then any increased labor costs that may come with passage of legislation such as EFCA cannot be paid for by reducing profits; doing so would likely lead to those firms failing to earn an adequate return on their investments. Instead, in a competitive setting, firms facing higher labor costs will need to make adjustments elsewhere to compensate, just as any entity operating under a budget.

Firms facing higher costs have several options. One is to reduce the use of the now more expensive input. Thus, firms will likely use less union labor as its cost increases. This effect is not to be confused with the illegal firing of union employees. Rather, it is a straight forward matter of economics: as prices go up, demand tends to go down. Thus, firms may choose not to fill empty positions, not to replace workers resigning or retiring, and/or not to create new positions or expand production.

Another alternative is to raise prices. In competitive markets, well established economic theory dictates that price (P) equals marginal cost (MC). Wages are clearly a marginal cost. Thus, as marginal production costs go up because union labor is more expensive, firms in competitive industries will likely raise prices to consumers.

Higher consumer prices would bring other consequences. Most importantly, consumers can be expected to react to the higher prices, just as the firms did before them. While

union members may be earning higher wages, price increases would act to erode union members' pay increases. Moreover, non-union workers are unlikely to be earning higher wages. When faced with higher prices for the goods and services they purchase, many consumers may simply buy less. Goods and services are more expensive, so to stay within their budget constraints consumers may reduce their overall buying. Or, consumers may choose to buy cheaper alternatives offered by firms that do not face increased labor costs, in particular international firms.

To the extent that consumers reduce their purchases of US goods, that reduction will likely reinforce any unemployment effects. Non-union firms, particularly international firms, will likely gain larger shares in the marketplace at the expense of domestic firms facing higher union labor costs. In the face of shrinking sales, domestic firms can be expected to make further cuts in their headcounts, again increasing unemployment and reducing job creation.

In light of my quantitative analysis and how it fits within the broader context of economic incentives, the costs entailed in the provisions of EFCA appear to be substantial. In considering whether to pass EFCA, I would urge that Congress's analysis not stop with potential benefits to some workers in the form of higher wages and increased benefits promised by unions. As with all legislation, but especially for such an important area as labor relations and management, it is essential that both the potential benefits *and* costs be considered. A bill that touches so many aspects of the economy is sure to have far-reaching repercussions. There is no coherent theoretical argument that explains how higher costs, greater legal uncertainty and expanded government intervention entailed in EFCA would improve social welfare for *all* workers. The analysis presented in "Economic Implications" suggests that the costs of passing the Employee Free Choice Act could very well outweigh the benefits.