Congressional Testimony

To the House Subcommittee on Health, Employment, Labor, and Pensions

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Chairman Roe, Ranking Member Andrews, and Distinguished Members of the Congress,

Thank you for this opportunity to testify today on the vital issue of worker rights, jobs, and the U.S. economy. I will share an analysis I have done of the RAISE Act, sponsored by Congressman Rokita of Indiana, which would allow employers to lift the "seniority ceiling" on workers' wages by allowing employers to pay individual workers more—but not less—than a Collective Bargaining Agreement (CBA) specifies. The views expressed in this testimony are mine alone and do not necessarily represent those of the Hudson Institute.

As the grandson of an elected Democrat, Edward Kane, who was inspired by President Franklin Delano Roosevelt to run for office in the city of Wyandotte, Michigan during the Great Depression, won, and served for decades in Michigan, I can promise you that I represent a family that has long put the American working man first and foremost. Also as the son of the president of a small manufacturing company, I can promise you that I bring the perspective of someone who appreciates how jobs are truly created. I've spent my career studying the U.S. economy, but have also founded and run a few software companies, so I am honored to share my perspective as an economist and entrepreneur.

I'd like to thank all of the Members here for your tireless efforts to pull the U.S. economy out of the recession. I know you share with me some frustration that the recession may have technically ended years ago, but job market remains mired in recession. We need to face the truth that the policies put in place since 2009 have been an abject failure in terms creating a recovery in U.S. employment, despite the promises of the Obama administration's leading economists.

Recent calculations I did show that the **employment-to-population** ratio collapsed by a staggering 4 percent during the recession, and it has not recovered at all in the last three years. Other measures of labor utilization such as the unemployment rate or payroll jobs created are not demographically neutral, masking elements such as worker discouragement and population change. The employment-population ratio averaged 63 percent for two decades before the current recession, but crashed to a modern low level of 58.2 percent in late 2009. In the most recent report from the Labor Department, it remains stuck 58.6 percent, where it has held steady for two and a half years, representing a permanent loss of 12 million jobs under this policy regime.

My analysis of employment-to-population shows a complete recovery after 54 months in 4 of the last 5 recessions going back to 1970. There was a 50% recovery after 2001 and a zero percent recovery today. The status quo is a powerful reminder that the policies in place today have *prevented* what should be by now a recovery of all 12 million jobs.

WORKER RIGHTS

If I may turn the clock back in time to 1934 when my Grandfather ran for tax assessor in Wyandotte, the labor movement then was fighting to promote workers' rights against the abuses of some corporations. The abuses were real and the eventual victory of workers' rights represented what I believe was true progress.

What are workers' rights? Some say that workers have a right to bargain collectively, and I agree. Some say this is the limit of workers' rights, and I disagree. There is no economic or logical reason to require workers to surrender their individual rights when they bargain collectively, or merely consents to a collective agreement. **A collective agreement should be understood to establish minimum standards for all, not the maximum potential for everyone.**

Unfortunately, U.S. labor law has regressed over the decades such that the existence of collective bargaining rights now means the suppression of individual bargaining rights. To be honest, I am an economist, not a specialist in labor law, so I had no idea that giving *higher* pay to union workers is illegal under the National Labor Relations Act of 1935. The Supreme Court has actually upheld the law in extreme cases, and the NLRB routinely blocks companies that attempt to give individual raises. In 2009, for example, the NLRB ordered the Brooklyn Hospital Center to stop giving $100 gift cards to its top nurses. This fails the common sense test, and I believe it fails the economic test as well.

ECONOMIC ANALYSIS

I've conducted an analysis of the RAISE Act on the U.S. economy and would like to share the results briefly here. The RAISE Act – remarkable in its brevity – would allow companies with unionized workforces to offer bonuses and higher wages to some or all its workers than the current baselines contract. That is the whole matter at hand.

To predict the economic effect of the RAISE Act, the key variable is what will happen to **labor productivity**. The economic literature on unionization and productivity is mixed. A widely respected 1984 book by Freeman and Medoff (*What Do Unions Do?*) asserted a positive effect of unions on productivity in the U.S., but the claim has not held up well to more sophisticated statistical analysis in more recent studies, and has not been substantiated by any other broad-based studies. Barry Hirsch revisited the question in a 2004 paper published by the Journal of Labor Research and cited numerous other papers, notably Clark (1984) which find a negative relationship. For example, a 2003 study by Metcalf found that a unionized firm's labor productivity was 14 percentage points more likely to be below the industry average.

In theory, a unionized workforce will have positive and negative effects on productivity, which is why disentangling them across multiple industries and legal-market contexts is muddled. All economists agree and empirical data show that unions hurt firm profitability. That effect also is known to limit productivity *growth*, if not initial levels, which may be why the private sector industries with high unionization rates have declined so dramatically since the 1980s. Metcalf outlines four negative channels and five positive channels. On the negative side:

> First, unions may be associated with restrictive work practices. Second, industrial action may have an adverse impact. Third, union firms may invest less than non-union firms. Fourth, if unions are associated with an adversarial style of industrial relations the consequent low trust and lack of cooperation between the parties may lower productivity.

On the positive side:

> First, firms' responses to union relative wage effects may result in higher labor productivity, but this should not be interpreted as raising the welfare of society. Second, unions may play a monitoring role on behalf of the employer. Third, the familiar collective voice arguments may have favorable consequences. Fourth, it is sometimes held that a union presence may make managers less lethargic. Finally, unions should stop exploitation of labor, resulting in improved productivity.

It is important to understand that none of the positive effects of unionization would be diminished by the Act. Indeed, the worst-case outcome of passing RAISE is a completely neutral effect on the economy. However, the Act has potential to remove some of the negative effects of unions on productivity. The most important negative effect this Act will remove is the ban on performance incentives. Metcalf discusses incentives, but I believe this merits consideration as one of the main productivity inhibitors of unionization. Seniority, rather than work effort and competence, is the dominant consideration for promotion and raises under most union rules.

Economic research shows that workers respond to incentives, with estimates of the increase in worker earnings ranging from 6 to 10 percent when pay is performance-based. The productivity gain is at least that high, but possibly much higher. We can imagine the effect will be even larger in firms which have never had merit-based pay. One study found that only 20 percent of workers employed through CBAs, which includes 7.6 million private sector union employees, operate under contracts that allow performance-based pay. That means 80 percent (6.1 million) of union workers have a wage ceiling enforced by U.S. law that makes individual performance bonuses and raises illegal, but would be legal after passage of the RAISE Act. **I think it is safe to assume a 10 percent productivity increase across the board for all 7.6**

million union workers affected by the RAISE Act, most which would be given directly to workers in the form of higher pay. The typical union worker will get a 5-10 percent raise in take-home pay.

Other economic effects that the Act will make possible include higher firm revenues. Because the marginal product of labor will increase, affected firms will soon move to hire more workers in two waves. The first wave will be to hire workers rather than expand capital investment because of labor's increased relative productive impact, but the second wave will be in response to higher profit potential as the firm expands. A conservative estimate is that each wave will increase employment by 1-2 percent above current levels, or roughly 200,000 new jobs over the next few years. Union jobs. The effects could be much higher. Again, let me emphasize the legislation has no potential to hurt jobs or wages.

CONCLUSION

Currently, the National Labor Relations Act allows collective bargaining agreements (CBAs) that suppress individual bargaining rights. Specifically, CBAs can set wage floors and wage ceilings, barring merit-pay, even barring across the board raises by the employer to all workers. A better approach would not put collective rights at odds with individual rights, but to allow both to be realized.

The RAISE Act – less than 200 words of legislation – will restore the upside of individual worker rights and allow firms to give individual bonuses and raises.

Lifting the pay cap on union workers across America would provide a much needed boost to our economy. I estimate the RAISE Act will generate an average raise of 10 percent to union workers in response to new productivity gains based on new incentives. The follow-on effects will lead to increased firm revenues and the creation of an additional 200,000 union jobs in the United States.

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