

A POLICY DILEMMA - A STRONG SOCIAL DIMENSION FOR THE EUROPEAN UNION OR A COMMITMENT TO FREE TRADE

Frank McDonald, International Business Unit, Manchester Metropolitan University

Manchester, UK

Tel: 00 44 161 247 3901 Fax: 00 44 161 247 6313 e-mail: F.McDonald@mmu.ac.uk

Paper presented at the ECSA Conference, Seattle, 29 May - 1 June 1997

INTRODUCTION

The social policy of the EU is very different from the social policies of the member states. The EU has few powers in the areas such as social security payments, housing, health and social welfare systems because this is largely the responsibility of the governments of the member states. Furthermore, the EU does not have a large budget available for social policy programmes. Therefore, the EU can not become significantly involved in large scale social policy expenditures. However, the EU does have significant powers to issue legislation in the area of employment rights and working conditions. Issuing legislation in these areas effectively passes the cost of attaining social objectives from taxpayers to companies, because employers have to comply with the requirements of legislation. The significant expansion of the *social dimension* of the integration process that the Commission was able to achieve in the late 1980s and the early 1990s led to a considerable expansion of legislation to enhance labour standards in the EU. The consequent increase in the cost of employing labour has significant implications for companies and for the future development of the *social dimension*. Companies that will find it difficult to compete with imports from countries with lower labour standards are likely to press for more protection from the instruments of the Common Commercial Policy. Therefore, the EU may find that it must abandon its commitment to the pursuit of open and competitive markets in the international trading system. In other words, the development of the *social dimension* has potentially very significant implications for the attitude and the policy stance that the EU adopts towards free trade.

BACKGROUND

The role of the 'social dimension' in the integration process of the European Union (EU) was given a considerable boost as a result of the programme to complete the Internal Market. The expected restructuring of the European economy, following from the creation of the Internal Market, was considered to lead to a problem of *social dumping* that would result in a downward spiral in employment rights and working conditions as companies sought to compete by adopting policies to reduce labour costs. The plans to move towards European monetary union also led to concerns about the possible impact of monetary integration on *social cohesion*. The Delors report on European monetary union advocated the development of the *social dimension* as an important component for successful monetary union (European Commission, 1989a)

In response to these concerns the President of the Commission, Jacques Delors, advocated the adoption of a Social Charter at the Stockholm Congress of the European Trade Union Confederation (ETUC) in May 1988. The Commission developed this momentum by issuing a working document on the *social dimension* of the Internal Market and a proposal for a Social Charter (European Commission, 1988b and 1989b). The Commission constructed an Action Programme to provide a framework for implementing the Social Charter (European Commission, 1989c). The Social Charter was approved by the Council of Ministers in October 1989 and it was subsequently adopted by all member states, except for the UK, at the European Council in Strasbourg in December 1989.

Most of the legislation connected to the Social Charter Action Programme has been approved, but a few proposals have yet to gain approval (see Annex I). To further develop the *social dimension* the Commission issued a Green Paper and a White Paper on Social Policy (European Commission, 1993a and 1994a). In the early 1990s the EU launched a large number of legislative developments in the areas of employment rights and working conditions. The scene appeared to be set for an ever expanding *social dimension* to the integration process and legislation on enhancing labour standards was at the heart of these developments.

However, the momentum to develop stronger and more wide ranging legislation in the area of employment rights and working conditions was hampered by concerns about the implications of such legislation for the competitiveness of companies. Labour market regulations that increase the cost of employing labour and that hinder the development of flexibility was identified as important factors in the relatively poor competitiveness of European companies (OECD, 1994, 1995a and 1995b). Even the Commission advocated a measure of deregulation of labour markets as a means of reducing unemployment and of improving the competitiveness of European companies (European Commission, 1993b, 1994b and 1994c). Moreover, concerns were expressed, among the main trading partners of the EU, about the dangers of the creation of a 'fortress Europe' to protect European companies from the competitive disadvantages that may arise from granting high minimum employment rights and working conditions (Dornbusch, 1990).

Nevertheless, the Commission, particularly DG V (responsible for Employment and Social Affairs), remained convinced that the *social dimension* was a crucial component in the process of European integration. *"The achievement of the single market and of economic and monetary union will be at risk if the general population, and notably the working population does not take part in the venture. The issue of social dumping is often invoked in this context. Although it is a fact that due to fierce competition enterprises need flexibility and that high unemployment reduces the bargaining power of workers, competition within the Community on the basis of unacceptably low social standards, rather than the productivity of enterprises, will undermine the economic objectives of the Union."* (European Commission, 1993b, p59-60)

ECONOMIC RATIONALES FOR LEGISLATION

Five economic reasons can be put forward to support the case for legislation in the area of labour standards:

- i) to encourage companies to adopt policies that enhance the productivity of labour;
- ii) to correct for market failure;

- iii) to reduce the pool of alienated labour;
- iv) to improve institutional frameworks;
- v) to enhance labour mobility.

Productivity Arguments

Legislation in the areas of employment rights and working conditions may encourage companies to adopt policies that increase the involvement of their employees in the management process and thereby encourage greater commitment by workers. In these circumstances workers will be more likely to acquire company specific training and to increase their work effort to fulfil the goals of the company. A work-force with these characteristics will provide a flexible and adaptable method of adjusting to the demands of increasing competition and to fast technological change. On the other hand legislation will discourage attempts by companies to attain competitiveness by cutting the cost of employing labour by reducing employment rights and working conditions. This type of argument is supportive of the views of the *empowerment* management gurus (Kanter, 1989, Senge, 1990) and is opposed to those who advocate the creation of *lean machines* based on *reengineering* the development of *core competencies* and the creation of *lean organisational structures* (Hammer and Champy, 1993, Prahalad and Hamel, 1994, Womack, 1996).

There is evidence that the UK has met with more difficulties than countries such as France and Germany in securing suitable skilled labour. This has hampered many UK companies in their attempts to attain the productivity levels that are reached in other countries (Mason, van Ark and Wagner, 1994). Moreover, although UK companies, in the manufacturing sector, have experienced considerable increases in productivity levels in recent years, on average, they are still lower than French and German levels (Oulton, 1994). However, there is no clear evidence that the failure of UK companies to match the productivity levels of those in the most successful European countries is connected to poor employment and working conditions. These problems are more closely connected to low skills levels in the UK labour force arising from failures in the education and training policies of the UK (Steedman, Mason and Wagner, 1991, Mason and Wagner, 1995).

There is no convincing evidence that low skill levels in the UK is due to an unwillingness by British workers to engage in education and training activities because they feel alienated from the goals and aspirations of the companies that employ them. The main problem seems to be that UK education and training system is incapable of supplying appropriately trained labour. Therefore, EU legislation in the areas of employment and working conditions is unlikely to significantly alleviate the problems of low skills that affect companies in some of the member states.

Moreover, it is not clear why legislation is needed to encourage companies to undertake actions that are in their interests. In cases where empowering the work-force increases the productivity of workers, companies will presumably adopt such policies: especially if reducing employment rights and working conditions is not an effective method of attaining competitiveness. Moreover, if the *lean machine* management gurus are correct, legislation that prevents the use of lean and flexible operations will undermine the competitiveness of companies.

It is possible, because of the nature of the markets and conditions in which companies operate, that some companies must attain competitiveness by creating 'lean machines' while others can become competitive by use of softer, more empowering, systems of management. Furthermore, competitiveness may be best attained by granting high standards to a core group of employees whilst the peripheral employees are offered lower standards (Atkinson and Meager, 1986, Handy, 1989). Consequently, legislation that is applied across all sectors may be harmful to some companies, whilst having little effect, either good or bad, on those companies who must seek to attain competitiveness by use of high labour standards. Moreover, even in cases where empowerment policies help companies to boost their competitiveness, legislation may lead to the imposition of inappropriate employee-employer relations.

It is difficult to sustain the case that legislation that seeks to encourage companies to adopt policies to enhance the productivity of labour can help them to create or maintain competitiveness. A case maybe put for legislation to protect especially vulnerable workers in particular sectors in some member states or regions. However, in these cases the subsidiarity principle would indicate that EU legislation was not required. Furthermore, such legislation would be for equity reasons and could not be justified by reference to claims that it would help to boost competitiveness.

Market Failure Arguments

Market failure can arise if problems of adverse selection are widespread. Adverse selection problems may arise from the wide-spread use of *lean machine* management systems. Companies that offer high remuneration and good employment conditions, backed by tough hire and fire policies to create strong incentives to perform at high level, will attract *star performers*. Companies that adopt a more empowering and participate forms of management will generally have fewer differences in remuneration and employment conditions across their work-forces. In these circumstances companies that adopt participative approaches may face an adverse selection problem, that is, they will be left with those employees that have lower levels of skills and who have a weak work ethic. This outcome will arise because most of the *star performers* will be located in the *lean machine* companies. Therefore, adverse selection may lead to lower productivity in companies who adopt a participative approach. A solution to this problem would be to encourage the spread of star performers across companies thereby boosting the average level of productivity of companies because spreading the 'star performers' across companies will boost the productivity of all, or most, workers. Legislation could be used to encourage the spreading of *star performers* by forcing all companies to adopt a participative and empowering management system (Levine and Tyson, 1990).

However, this analysis assumes that *star performers* will continue to perform at high level even if their differentials, in remuneration and employment conditions, are close to those of average, or even poor, performers. Human capital theory suggests that *star performers* have higher skills or have experience or

attributes that are in short supply (Becker, 1975). Consequently, legislation that compresses differentials may lead to a decline in the number of *star performers* because they may emigrate, refuse to acquire relevant skills or choose to become average performers (Addison and Siebert, 1992). Such human capital theory assumes that labour and product markets are competitive. Problems of market failure can arise if employees are able to obtain excessive remuneration and employment packages by use of monopoly power. To counter such problems legislation may be required to correct such cases of market failure. However, the necessary legislation would be to counter monopoly power, not to force companies to adopt participative management systems.

Health and safety issues may also lead to problems of market failure. If companies fail to provide adequate health and safety conditions, their workers will be subject to excessive risk. This problem should not arise if markets are competitive and if all parties have access to the same information. In these circumstances employers and employees should reach agreement on what constitutes acceptable levels of risk. However, markets are often not competitive and employers normally have better information than employees about the level of risk associated with work activities. Legislation can help to overcome this problem if it reduces monopoly power and if it requires employers to provide good information about the risks that are connected to work activities. Nevertheless, legislation can be a very blunt weapon to tackle this problem if it concentrates on specific safety measures because the legislators may have even poorer information than the employees about risk factors. Moreover, legislation may not take into account the specific factors that affect particular industries or companies. Effective legislation in the area of health and safety, if it is to correct for market failure, should concentrate on ensuring that all parties to agreements should have access to good information about risk factors and employers should be required to reach agreement with their workers on acceptable levels of risk. The Health and Safety framework Directive (see Annex I) concentrated on this issue. However, the Directives on specific health and safety issues were more concerned to specify concrete rules for health and safety. This approach may not be a good response to problems of market failure because

the specific measures may be inappropriate given the levels of risk and the attitude of the parties involved to such risk

Pool of Alienated Labour Arguments

The use of *lean machine* approaches to management may lead to job insecurity and to the alienation of workers. A pool of such alienated people is created who have poor skills levels, low incomes and who lack commitment to the societies in which they live. In these circumstances the overall productive capacity of countries is undermined and a large-scale waste of resources arises because high unemployment and poverty lead to large economic and social costs that reduce the productive capacity of countries.

This problem is considered to be most likely to arise in Anglo-Saxon systems of capitalism because in these systems investment is thought to be biased towards those projects that yield high profits in the short-term, but which do not enhance the long-term productive capacity of economies. Therefore, investments are geared towards low productivity projects that are often in the service sector and that generate low skilled and low productivity jobs. Thus a low productivity economy is created and sustained, leading to economies with a large, low productivity, service sector that generates a substantial part of the employment opportunities. It has been argued that long-term investment planning could provide the basis for a more productive system. However, if companies base their competitiveness strategies on short-run profitability considerations they will seek to cut labour costs by adopting *lean machine* management systems that will undermine their ability to boost productivity by encouraging their work forces to acquire skills and to commit themselves to the goals of the company. This type of argument has been put forward as an explanation for the low growth in the UK in the post-war period (Hutton, 1995). It is argued that legislation that requires high labour standards will reduce the ability of companies to engage in such short-sighted policies and will therefore force them to make better use of their labour resources. Some left wing economists have argued that such legislation is crucial if Europe is to avoid significant economic and social costs (Coates and Holland, 1995, Holland, 1993).

However, the Anglo-Saxon economies, particularly the USA, have been considerably more successful in creating new private sector jobs than the economies of continental Europe. However, the Anglo-Saxon economies have experienced an increase in the levels of relative poverty. In the UK, between 1970-92, the proportion of the population that maybe classified as being relatively poor, as measured by income levels, has grown. Nevertheless, if poverty levels are measured in terms of expenditure, rather than by income, relative poverty in the UK does no appear to be significantly different from most of the rest of Europe (Blundell and Preston, 1995). Capitalist systems create a problem for those who cannot succeed in the harsh competitive environment. This problem leads to a need to make a choice on how to deal with the losers - high unemployment (with relatively low living standards) financed by state expenditures or low living standards financed by low paid employment. Legislation that seeks to boost employment and working conditions is unlikely to help these losers to improve their position because this will tend to increase the costs of employing marginal players in the labour market. In this context, legislation may worsen the problems of losers (Addison and Siebert, 1993).

It is difficult to understand why companies should voluntarily select low productivity activities because such operations tend to have low value-added characteristics that will, in a competitive system, generate low profits. Consequently, this argument appears to depend on long-term collective myopia by companies. Moreover, companies are deemed to be incapable of learning that they are continually choosing to adopt policies that will generate low value-added and therefore low profitability projects.

The Schumpeterian concept of *creative destruction* provides another possible argument for legislation. Capitalism tends to create new profitable opportunities by making existing production systems obsolete and by replacing traditional products with new or improved products (Schumpeter, 1934). However, this *creative destruction* may come at the cost of creating a large pool of alienated people. This pool of people is denied access to high productivity jobs and the overall productive potential of the country is thereby undermined.

The essence of this analysis is that what is beneficial for individual companies can lead to harmful results for society as a whole. This problem arises because the pursuit of profitable opportunities by companies creates a pool of workers, that lose their jobs and then find it very difficult to re-enter the work-force. The pool of people in this position may be unable or unwilling to acquire new skills and they may also develop poor attitudes to work. The subsequent lack of appropriately skilled workers undermines the ability of companies to attain competitiveness. In such a world legislation that limited the destructive aspects of capitalism may lead to benefits by increasing the skill levels and by encouraging a more appropriate work ethic across a larger proportion of the population.

The case for a *social dimension* to alleviate the harmful aspects of *creative destruction* rests on the view that social policy could reduce the pool of alienated people, or that legislation could hinder the process of competition in order to prevent the destruction of jobs. The first reason is in accord with the objectives of the treaties, that is, to promote open and competitive markets. However, the EU has only a limited role in alleviating the problems caused by a pool of alienated and low skilled people. Moreover, the concept of subsidiarity would suggest that this role may be more effectively performed by national governments. The second reason is directly opposed to the promotion of open and competitive markets and could be regarded as a type of protectionism. The pursuit of such a policy would have implications for the common commercial policy of the EU because it is difficult to ameliorate the forces of *creative destruction* and to simultaneously promote open and competitive markets.

Institutional Frameworks Arguments

The new institutional economics suggests that the ability of market systems to deliver beneficial transactions is closely linked to the institutional frameworks of countries. Institutional frameworks determine the rules of human interactions (North, 1990). These frameworks have formal characteristics, for example, constitutions, bills of rights and informal, for example, social convention and codes of behaviour. Therefore, institutional frameworks - the political, legal and cultural determined rules and conventions of a society - provide the arena

in which organisations and individuals interact with each other. In North's analysis institutional frameworks provide a vital role in reducing the transaction costs and uncertainties that beset all human interaction. Effective institutional frameworks are those that provide low transaction costs and low risk interactions between economic actors

A version of the new institutional economics provides an argument for the need for appropriate institutional reform to counter the harmful effects, on disadvantaged workers, of unfettered capitalism (Humphries, 1995). Such reform could reduce the inefficiencies associated with high turnover, under investment in training for disadvantaged groups and high levels of absenteeism by certain groups of workers (Bruegel and Perrons, 1995). Therefore, institutional frameworks that encourage companies to provide incentives for their workers to acquire appropriate skills and attitudes to work would avoid some of the harmful social and economic consequences that are connected to capitalism

Institutional reform requires changes to constitutional procedures, social conventions and legal and judicial structures. The development of institutional frameworks is normally considered to be path determined - that is, influenced by the historical, political, legal, economic and cultural backgrounds of countries. Therefore, attempts to alter institutional frameworks have to take into account the path of development that led to the current characteristics of institutional frameworks and the underlying forces that are influencing the evolution of these frameworks. Consequently, legislative changes are only one part of a more complex set of forces that drive institutional change. In the context of the EU, the path dependency character of institutional development may mean that the existing diversity in the member states could make attempts to alter the basic structure of institutional frameworks very difficult. The *social dimension* is an attempt to graft minimum standards onto existing the legal systems, it is not directly concerned with reforming institutional frameworks. However, if the underlying problem is connected to failings in institutional frameworks, such legislation is

unlikely to achieve its objectives. Nevertheless, the legislation may add to the costs of employing labour without curing the underlying problem.

Furthermore, North's historical analysis of the importance of institutional structures indicates that Anglo-Saxon systems have often provided effective systems for generating the conditions under which individuals and organisations can engage in profitable opportunities. Such profitable opportunities often lead to the growth of disadvantaged groups - losers in the competitive game. Finding institutional solutions to the problem of *creative destruction* in capitalist systems is an important question, but the *social dimension* of the EU is not a well-developed response to this problem. However, the Commission has begun to consider the need to develop new institutional frameworks to ease the transition to more flexible working patterns. The Commission considers that new arrangements need to be developed between national governments, the Social Partners and the institutions of the EU (European Commission, 1997a, European Industrial Relations Review, 1997). However, these developments are at a very early stage and they do not yet appear to have diverted the Commission from its standard approach to problems - that is, to legislate on a pan-EU basis.

Labour Mobility Arguments

The economic case for enhancing labour mobility in the EU is strong. The integration of markets that is being encouraged by the development of the Internal Market and the moves towards monetary union requires a greater integration of labour markets if the economies of the EU are to effectively adjust to the new market environment that is being created. Social policy has a role in this process of promoting greater labour mobility. Problems connected to the transnational transfer of social security and pension rights and the recognition of qualifications and relevant work experience are a major source of legal barriers to labour mobility. However, the EU has made little progress in dealing with the problems with social security and pensions and the attempts to use mutual recognition of qualifications does not appear to have removed barriers created by difference in qualifications.

It might be expected that the Commission would have emphasised the need to remove these legal barriers in the second Social Action Programme. However, this Programme contained very little on this issue (European Industrial Relations Review, 1995). The significant differences in the qualifications systems in the member states and the reluctance of the member states to tackle problems connected to social security and pensions provision has hampered the ability of the Commission to secure effective legislation to overcome these problems.

Assessment of the Economic Rationales

From an economic perspective the EU clearly has good grounds to legislate to remove the legal barriers to labour mobility. However, the EU is not engaged in vigorously legislative activity in this area. The argument that legislation will encourage companies to take actions that will improve the productivity of their workers is weak. The case for legislative action by the EU to correct for market failure may be strong if adverse selection is a widespread and if legislation can alleviate this problem. However, the extent and scope of the legislation that has emerged from the EU is greater than would be necessary to deal with adverse selection problems. Similarly, the action taken by the EU in the area of health and safety also suggests that the legislation arises from motives other than to correct for market failure. Legislative programmes, or the development of new institutional frameworks, to curb the harmful aspects of *creative destruction* may be a valid policy objective. However, it may not be possible to curtail the process of 'creative destruction' without significantly undermining the benefits that arise from this process.

The EU is engaged in a process of unleashing the forces of 'creative destruction' by creating the Internal Market and by seeking to liberalise market access in areas such as air travel, energy and telecommunications. The establishment of monetary union will also contribute to enhancing the competitive environment in the EU. The EU is also party to the attempts by the World Trade Organisation (WTO) to improve market access in the service sector and to implement the liberalisation measures contained in the Uruguay Round. Therefore, if the *social dimension* leads to legislation that seeks to alleviate the forces of *creative destruction*

it is possible that the Commission will have to decide which policy should take precedence - the pursuit of open and competitive markets or the preservation of social stability. The main policy area that is affected by this dilemma is the common commercial policy. It is possible to use the common commercial policy to protect certain industries while remaining committed, in principle if not in practice, to the idea of open and competitive markets.

The economic case for the *social dimension* depends upon the existence of significant problems with market failure and a need to combat the forces of *creative destruction*. However, it is not clear if market failure is a significant problem in the EU. Furthermore, the EU may not be the best agency to deal with problems of market failure or with problems with the forces of *creative destruction* because of the diversity of institutional and legal frameworks in the member states. Moreover, the *social dimension* does not seem to have been constructed to tackle these economic problems. Political issues appear to have been the driving force for the development of the *social dimension*.

POLITICAL RATIONAL FOR THE SOCIAL DIMENSION

The debate over the nature and extent of the *social dimension* had elements of an ideological battle over the characteristics of the type of capitalism that should be developed in the EU. The Commission, with the support of most of the governments of the member states, had been seeking to avoid the adoption of the Anglo-Saxon model of capitalism in the EU. This was done by seeking to extend the *social market* model of capitalism throughout the EU. The main method of attempting to accomplishing this outcome was to establish the main components of this alternative model of capitalism in all the member states by use of legislation on minimum standards in the areas of employment rights and working conditions. The opposition to this approach came mainly from the government of the UK. The British view was that the extension of the *social market* model would undermine the ability of companies to create and maintain competitiveness.

The development of the *social dimension* was also an important factor in winning the support of the trade union movement in Europe to the cause of the integration project. The speech by President Delors to the Trades Union Congress (TUC) in the UK in 1989, in which he outlined the importance of the *social dimension* to the integration project, was a major turning point in the conversion of the labour movement in the UK to the cause of European integration. The ETUC was very supportive of the *social dimension*. Indeed the EUTC believed that the *social dimension* did not go far enough and it advocated significant expansion of the social policy of the EU.

Employers' organisations were also subject to pressures to co-operate in the extension of the *social market* model. Employers in those countries that already had versions of the *social market* model were eager to avoid what they regarded as the problem of *social dumping*. Consequently, employers' organisations in these countries did not oppose, in principle, the *social dimension*. Furthermore, many employers' organisations were attracted to the *social market* model because it was identified as one of the major contributing factors to the competitiveness of German companies. Nevertheless, many employers' organisations in the UK were less enthusiastic about the *social dimension*, for example, the Confederation of British Industry and some were hostile - the Institute of Directors and the Federation of Small Businesses.

The differences of opinion across the various employer's organisations contributed to the rather luke warm approach to the *social dimension* by the Union of Industrial and Employers' Confederations (UNICE). Employers' organisations were not strong supporters of the *social dimension* - even those employers' organisations that supported the general principles of the *social market*, expressed strong reservations about the development of EU legislation in the areas of employment rights and working conditions. Notwithstanding these reservations, UNICE played a significant part in the negotiations by the Social Partners, under the auspices of the Social Policy Agreement of the Treaty on European Union, to reach agreement on the European Works Council and the Parental Leave Directives. However, UNICE did not wish to negotiate on

the Directive on the burden of proof in cases of equal pay and treatment. The negotiations by the social partners on atypical workers rights were also hindered by the opposition of UNICE to proposals that they consider would add to the cost of employing such workers.

Notwithstanding the reservations by the government of the UK and by some of the employers' organisations, the Commission managed to build a coalition of interests that has supported the general principles of the *social dimension*. European trade unions have been strong supporters of the *social dimension*. This has helped the Commission to counter concerns that the integration process was contrary to the interests of organised labour. By highlighting the problem of *social dumping* the Commission was able to win the support of those employers who were concerned about competing with companies based in member states that had low employment and working conditions standards. Many companies based in member states that had lower labour standards were attracted to the prospect of enhancing the productivity of their workers by adopting German type labour relations systems.

This coalition helped the Commission to make significant progress in developing the integration process. In many ways the Presidency of Jacques Delors was a golden age for the integration programme and the development of the *social dimension* was an important component in the struggle to win popular support of labour and employers in the member states. This support also enhanced the influence of the Commission at the heart of the economic activity in the member states. Clearly the creation of this coalition was a major political success for the Commission.

However, this coalition of interests has proved difficult to sustain. Organised labour has been disappointed by the outcome of the legislation that has stemmed from the *social dimension*. Unemployment has continued to rise, employers have pushed for greater labour flexibility to adjust to more competitive markets and much of the legislation has not significantly altered the employment conditions of workers. Employers have also been

concerned about the effects of the legislation on the cost of employing labour. The *social dimension* could not deliver outcomes that would please all the members of the coalition. Moreover, the *social dimension* lacked a sound economic rationale and it was not well designed to tackle problems that were capable of resolution by the legislative powers of the EU., for example, legal restrictions on labour mobility.

The Commission has been unable to sustain the momentum behind the *social dimension* and it also found it difficult to implement the Social Action Programme. A new Social Action Programme has been proposed (European Commission, 1995). This Action Programme is largely based on the White Paper on Social Policy and it is considerably less ambitious programme than the First Social Charter Action Programme. Nevertheless, the Second Social Action Programme contains suggestions that more legislation, action programmes and plans are necessary in the area of employment rights and working conditions to create the conditions for a high productivity economy in the EU. Annex I provides a summary of the main proposals for enhancing the *social dimension* that are contained in the Second Social Action Plan.

The Commission has created a significant role for the institutions of the EU in the area of employment rights and working conditions. The Commission, the ECJ and the EP will be able to build on this base and EU laws in this area will continue to grow and develop. The impetus behind the *social dimension* has perhaps been slowed, but it remains, and it has acquired a life within the institutional structures of the EU. In these circumstances it is difficult to prevent the growth and development of legislation in this area. Therefore, the impact of such legislation on the cost of employing labour and the possible impact of these costs of the common commercial policy is likely to become of increasing importance.

THE COST OF LEGISLATION TO COMPANIES

In principle EU law should have equal effect in all member states. However, the normal method of implementing EU law is by use of Directives that must be transposed into the national law of the member states. The national laws that emerge from the Directives should achieve the same outcomes, in terms of the

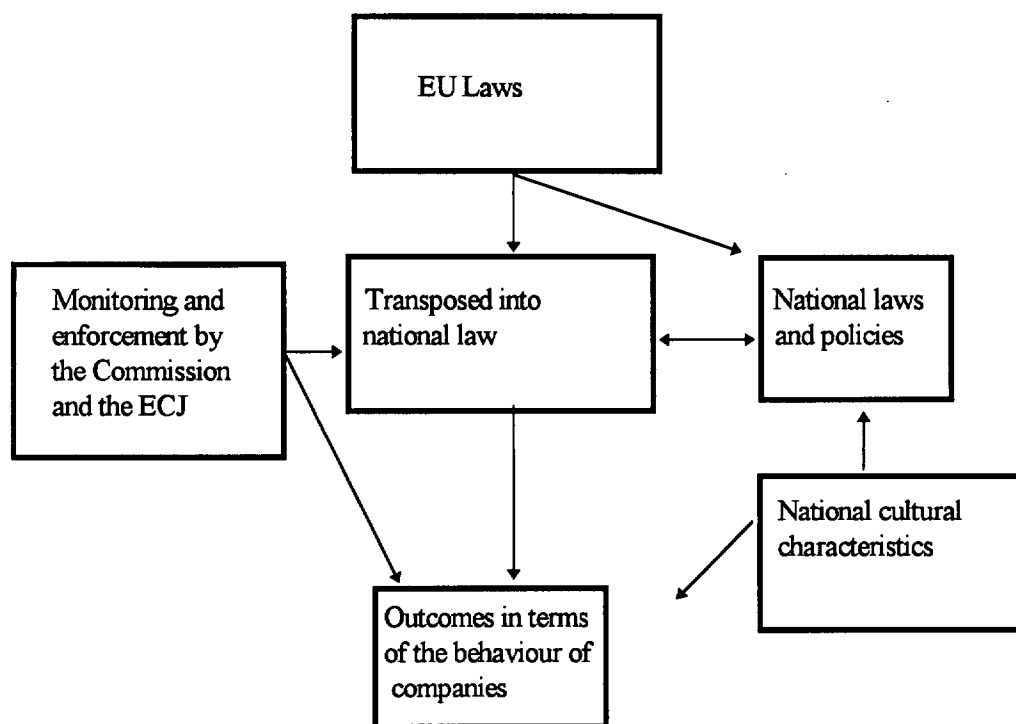
required behaviour of those affected by the law, in all member states. Therefore, the characteristics of national legal systems should not lead to outcomes that are different from those specified in the Directives. However, there exists considerable diversity in national legal systems and this may lead to different outcomes across the member states.

The Commission and ultimately the European Court of Justice (ECJ) has the responsibility to ensure that EU law has equal effect in all member states. Consequently, the decisions of the Commission and particularly the ECJ have important implications for the way that EU law affects outcomes in the member states. However, cases have to be brought to the attention of the Commission and/or the ECJ in order for problems of EU law not having equal outcomes across the member states to be resolved. In most cases the Commission depends on complaints and comments from institutions and individuals in the member states as an indicator of failure to implement EU law in a manner that results in equal outcomes. The number of such complaints that are received is affected by the attitude that institutions and individuals in the member states adopt towards EU law. If channels of communication are well developed the flow of complaints and comments to the Commission will be fairly easily accomplished and action to rectify non-compliance will be more likely. These factors may lead to EU law being transposed into national law in such a way as to lead to outcomes that are not in accordance with the desires expressed in the original Directives. However, the ability of the Commission and the ECJ to rectify such problems may vary across the member states. Furthermore, EU law, in the area of employment rights and working conditions, normally provide only minimum rights and conditions. National laws may grant more extensive rights than EU law. Moreover, differences in culture and business practices may mean that in some member states more emphasis is placed on fully implementing EU law than is the case in other member states

The major factors that affect outcomes from EU law are illustrated in figure 1.

Figure 1

Factors Influencing The Outcomes From EU Law



The potential for different outcomes can arise from differences in national laws, policies and cultural determined attitudes that prevail in the member states. Moreover, the monitoring and enforcement activities of the Commission and the ECJ may not be evenly applied across the member states.

Empirical work by labour economists suggests that in most European countries employment protection legislation has small but harmful effects on employment levels and on the ability of companies to quickly respond to changes in their competitive environment. Legislation also tends to bias employment towards workers who have lower employment protection rights, for example, atypical workers (Beatson, 1995). Most of this work has been conducted on an aggregated basis. The impact on particular sectors of the economies has not been extensively examined. However, it is possible that some sectors, for example, SMEs in highly price competitive markets, may be more severely affected by legislation than large companies in markets that are characterised by competition by the quality of products or services. Furthermore, EU law may have more

impact in those member states that adopt strong versions of the Directives and where the institutional and cultural structures are supportive of the aims and objectives of EU law (McDonald, Potton and Tuselmann, 1996).

Very little empirical work has been carried out on the compliance cost to companies of implementing EU legislation in the area of employment rights and working conditions (Holtermann, 1995). Estimates by the Department of Employment of the cost to UK companies of implementing the Maternity Leave Directives by the Department of Employment indicate that the costs of replacing workers on maternity leave and of extra administration costs are approximately £100 to £250 million per annum. If ten days paid leave (paternal leave) is provided by employers, this would cost would rise to £425 million. If leave for family reasons was paid at statutory sick pay the cost would be £35 million, but if pay was at the going wage rate the cost would rise to £335 million (Holtermann, 1986, Holtermann and Clarke, 1992). Estimates by the Department of Employment, (in 1992) of the cost of the Working Time Directive indicated that employers could face an increase in their wage bill of £2.5 billion, extending rights for a-typical workers could add £1.2 billion. The Forum for Private Business estimate that the Working Time Directive will cost £3000 per annum for a typical small company that employs 20 people, this study also found that 74 per cent of small companies thought that the Working Time Directive would significantly add to their costs (Forum of Private Business, 1997). These estimates, especially those from the Department of Employment, have been subject to a great deal of criticism and they are nearly certainly overestimates of the true costs (Holtermann, 1995). However, even if these estimates are on the high side, companies face significant costs in meeting the requirements of EU legislation in the area of employment rights and working conditions.

Companies face two major types of costs when they comply with legislation - initial implementation costs and the costs associated with the managing the implementation of laws in daily operations. A study by the Forum of Private Business found that the average initial implementation costs of employment regulations (including

pensions and social benefits) and health and safety regulations for UK SMEs were 19 per cent of total compliance costs and 10 per cent of managing daily compliance costs. This compared with 49 per cent and 12.3 per cent (respectively) for the compliance costs of taxation regulations (Forum of Private Business, 1996). Therefore, regulations in the area of employment rights and working conditions (much of which are influenced by EU law) are a significant part of the compliance costs of SMEs. Compliance costs are high in the agenda of SMEs as a major impediment to their ability to develop and grow (Forum of Private Business, 1997).

Clearly the growth of EU legislation in the area of employment rights and working conditions has significant implications for the cost of employing labour. Moreover, SMEs and companies in member states that have institutional frameworks that enhance the objectives of the EU laws will face the most pressure on their cost structures. Many companies, particularly SMEs in price competitive markets, may find these cost increases cause them considerable difficulties. If these companies face competition from non-EU imports they may resort to the instruments of the Common Commercial Policy to seek refuge from what they consider is unfair competition.

THE COMMON COMMERCIAL POLICY

The Common Commercial Policy of the EU is, in principle, geared to working towards open and competitive trading relationships. The Policy is supposed to be supportive of the attempts by the WTO to liberalise market access and to removing tariff and non-tariff barriers. However, on average the EU, together with the USA, operates a more restrictive trading policy than does Japan (Daly and Kuwahara, 1997). The EU is committed to the provisions of the Uruguay round of GATT to adopt measures to ensure that the use of anti-dumping duties and other instruments to control imports are only to prevent unfair trade practices (as defined by WTO rules). However, there is no evidence that the EU is taking this commitment seriously (Grimwade, 1996). The number of cases in which anti-dumping duties fell in the early 1990s, but they have begun to rise again as have the appeals to the Commission to institute anti-dumping cases or surveillance procedures.

Furthermore, the number of countries that are subject to anti-dumping duties is also rising. China and the Asian tigers figure prominently in the cases of anti-dumping duties and in surveillance procedures, but the countries of Central and Eastern Europe are also increasingly being subject to the unfair trading provisions of the Common Commercial Policy (European Current Law Year Book, 1996).

A new system of trade barrier regulations has been devised to encourage companies to seek action to impose trade barriers on countries that are thought to impose unjustified barriers to access to their markets (European Commission, 1997b). The Commission is also developing ideas on how to force trading partners to grant fair access to European companies by use of trade barriers to encourage them to open-up their markets (European Commission, 1997c). Furthermore, countries that have are thought to use exploitative working practices may be classified as operating unfair trading practices (European Commission, 1996).

The EU appears to be adopting a tougher line on what it considers to be unfair trading practices. Furthermore, the new system of trade barriers regulations enhances the opportunities that companies have to press for trade restrictions to be imposed on non-EU countries that are considered to be operating unfair trading restrictions. The use of anti-dumping duties and surveillance measures also seems to be on the increase. Furthermore, the idea that countries that use labour practices that are prohibited in the EU are guilty of unfair trading practices is also gaining ground. Companies that face competition from non-EU imports and/or who feel that they are unfairly excluded from some foreign markets are likely to have more opportunities to seek redress through the provisions of the Common Commercial Policy. The development of the *social dimension* has increased the pressure on companies EU by adding to the costs of employing labour. Some companies may react to this by seeing protection from foreign competition. The EU may be encouraging this type of behaviour by adopting an increasingly hostile attitude to trading relations, particularly with countries that have considerably lower labour standards than those that prevail in the EU. The EU may have created a dilemma for itself - by pursuing a strong social dimension it is adding to the

pressures for the abandonment of the pursuit of open and competitive markets. Although the pressures to develop the *social dimension* are diminishing, the legislative programme is likely to continue and to be developed and extended. Moreover, the legislation that has already been approved has the potential to significantly add to the costs of employing labour.

CONCLUSION

The EU has made considerable progress in developing the *social dimension* of the integration process. This allowed the Commission to obtain the support of a coalition of trade union and employers' organisations for the integration process. The impetus for expanding the *social dimension* has been slowed, but the successful launch of a raft of legislation in the area of employment rights and working conditions has created a platform from which the institutions of the EU will be able to develop their role and influence. However, the legislation is not based on an attempt to boost the competitiveness of companies (although this claim has been made) and this has led to a distinct cooling of support from many employers' organisations. Indeed the possibility of significant increases in the cost of employing labour arising from the legislation may cause significant problems, especially for parts of the SME sector. There are serious problems arising from the unleashing of the forces of *creative destruction* and the *social dimension* could be developed to help in the search for solutions to these problems. However, this is likely to require fundamental change to institutional frameworks. The EU has not, thus far, adopted such an approach. Moreover, it is not clear if the EU is the correct agency to use to reconstruct institutional frameworks in the member states. If the EU is the appropriate agency and if it engages in such institutional design and development, the role of the institutions of the EU in the government of economic activity in the member states would be significantly expanded. However, it may not be possible to curb the forces of *creative destruction* and to simultaneously promote an external trade policy that is based on open and competitive markets. The enhancement of employment rights and working conditions that have already been approved may lead to increased pressures on the Commission to use the instruments of the Common Commercial Policy to protect vulnerable companies that can not compete with companies based in countries with lower labour standards. If the *social dimension* is further

developed in response to the unleashing of the forces of *creative destruction* this policy dilemma will become more acute.

Annex I - Summary Of Main Legislation In Employment Rights and Working Conditions Related To The Social Dimension

A Legislation Connected to the Social Charter Action Programme and other Social Dimension Agendas

Health and Safety

Approved Legislation

* The Framework Directive on Health and Safety [89/391/EEC] lays down general principles relating to obligations on employers to provide training and information about health and safety issues and to assess the risks associated with the work environment. The Directive also provides for procedures for information sharing and consultation on health and safety issues.

A large number of Directives have been approved for specific health and safety issues. Some of the main Directives are listed below.

- * Minimum health and safety requirements at the workplace [89/96/EEC].
- * Minimum health and safety requirements for workers using machines, equipment and installations [89/85/EEC].
- * Minimum individual protection equipment requirements [89/656/EEC].
- * Minimum health and safety requirements for handling heavy loads [89/213/EEC].
- * Minimum health and safety requirements for work with visual display units [89/195/EEC].

Proposed Legislation

* Protection of workers from risks related to chemical agents [165/93 amended by [191/94]. Two proposed Directives on health and safety from physical agents and in transport activities have been dropped.

Employment and Working Conditions

Approved Legislation

- * The collective redundancies Directive [75/129/EEC] was amended in 1992. The Directive imposes obligations on employers to consult trade unions before proceeding with collective redundancies.
- * The working time Directive [93/104/EC] provides for minimum daily and weekly rest periods, annual paid holidays, a limit to working more than 48 hours per week including overtime (unless by voluntary agreement between employers and employees) and restrictions on night work. The transport industries, sea fishing and doctors in training are excluded. Moreover, most management workers are exempt from the provisions of the Directive. Derogation from the provisions on rest periods and night work are possible if the imposition of the rules would lead to unacceptable disruption to the services supplied by workers.

- * The European Works Council Directive [94/45/EC] was agreed by use of the Social Policy Agreement of the TEU. The Directive requires the establishment of works councils to provide a forum for information sharing and consultation on matters connected to the operation of organisations. This Directive applies to companies with over 1000 employees (with at least 150 employees in at least two member states).
- * The posting of workers in the services sector Directive [220/96/EC] grants employees, who are temporarily posting from one member state to another, minimum employment and working conditions - including pay. Posted workers must have employment and working conditions that are in line with those that prevail in the host member state.

Proposed Legislation

- * Replacement of the acquired rights (transfer of undertakings) Directive [77/187/EEC] with a new Directive [274/94] to clarify the position of employees in undertakings that have changed ownership. The Directive relates to the right of employees to the continuance of existing terms and conditions of employment when there is a transfer of ownership of an organisation and grants rights in the area of information and consultation about the implication of a transfer of ownership.
- * Proposed modifications to the Statute for a European Company [263/89 amended by 138/91 and 99/92 amended by 236/93] to provide for consultation and involvement of workers in the European Company. These proposals have been deadlocked for most of the 1990s. These modifications could be withdrawn if the European Works Council Directive is deemed to cover the workers who are the subject of these modifications.

A-typical work

Approved Legislation

- * The health and safety for a-typical workers Directive [91/383/EEC] guarantees a-typical workers the same health and safety rights as typical workers.

Proposed Legislation

- * Proposed directives affecting a-typical workers on approximation of the laws of the member states relating to contracts and employment relationships with regard to working conditions [224/90] and on contracts and employment relationships involving distortions of competition [90/533] were blocked and were subsequently referred to the *Social Partners* under the provisions of the Social Policy Agreement of the TEU - *Community action on flexibility in working time and security of workers*. The *Social Partners* have, thus far, been unable to reach agreement on this issue.

Equal Opportunities

Approved Legislation

- * The maternity benefits Directives [92/85/EEC] granted protection of employment rights and provided for minimum paid leave for pregnant women and women who are breast feeding.
- * The parental leave Directive [84/631] was blocked and was referred to the Social Policy Agreement of the TEU. The *Social Partners* reached agreement that guarantees parental leave for at least three months in the event of the birth or adoption of a child up to the age of eight years. The agreement also provides for leave for urgent family reasons such as death or serious illness. Both men and women workers (on

a non-transferable basis) would have right to parental leave. Payment terms for parental leave will be decided by national governments.

Proposed Legislation

- * An amendment [218/95] to Directive [86/378/EEC] on equal treatment for men and women in occupational social security schemes bringing the original Directive into line with the ECJ's decision in the Barber case.
- * An amendment [179/96] to the Directive [76/207/EEC] on equal treatment for men and women as regards access to employment, vocational training and promotion, to clarify the position of positive discrimination considering the ECJ's decision in the Kalanke case.
- * The proposed Directive [176/88] to transfer the burden of proof in the area of equal pay and equal treatment to employers was blocked and transferred to the Social Policy Agreement of the TEU. The *Social Partners* did not want to negotiate on this topic so the Commission has presented a proposal for a Directive [332/96] to deal with this issue.

B Planned Legislation and Actions in the Second Social Action Programme

The Second Social Action Programme includes commitments to continue, where possible, with the proposed legislation mentioned above. Suggestions are also made for new legislation and actions in the area of health and safety and employment and working conditions.

Proposed Directives

Health and Safety

- * Directive on health and safety risks in explosive atmospheres.
- * Updating of the Directive on carcinogens.
- * Updating of the Directive on biological agents.

Employment and working conditions

- * Directives on individual dismissals; individual rights to consultation on internal company matters; right of payment for public holidays and during illness; the prevention of illegal work; the protection of the privacy of workers.
- * Extension of working time Directive to deal with the excluded sectors.
- * Amendment to the Directive on insolvency to protect the rights of workers.
- * Consolidation of the 1975 and 1992 Directives on collective redundancies.

Equal opportunities

- * Directive on reconciling professional and family life.

Codes of Practice and Action Plans

- * Codes of good practice will be issued on equal pay for work of equal value and on employment of disabled workers.
- * Guidelines will be issued on flexibility and work organisation.
- * Action plans and recommendations are planned to combat racism, discrimination against disabled workers and to aid homeworkers and teleworkers.

Plans to Improve the Effectiveness of the Implementation of Legislation

- * Action will be taken to improve the control of the implementation and enforcement of social legislation by requiring the member states to notify the Commission of its implementation measures by submitting a report to the Commission. Member States will also be required to provide a contact point in the national administration to facilitate the monitoring and enforcement of legislation. Attempts will also be made to include the social partners in the implementation of Directives. Furthermore, the Commission will provide information and guidance to interested parties in the member states on social legislation. This will include information on the extent and scope of social legislation and on the state of play of the implementation process in the member states.

Related Action Programmes

- * Fourth Action Programme for Equal Opportunities for Women and Men: 1995-2000
- * Fourth Action Programme concerning Safety, Hygiene and Health Protection at Work: 1995-2000

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