Efficiency and Equity at Work: The Need for Labour Market Regulation in Australia

JOHN BUCHANAN AND RON CALLUS*

The current reform objective of developing more competitive workplaces has been incorrectly identified with an alleged ‘need’ to ‘deregulate’ the labour market. An examination of current reform proposals reveals that there is an attempt to increase the importance of internal modes of regulation controlled by managers at the expense of external regulation such as awards. Such a development is likely to increase inefficiency and inequality in the labour market, as formal, external modes of regulation can promote both international competitiveness and fairness. Greater attention should be devoted to identifying better ways of linking external and internal modes of regulation to improve both efficiency and equity at work.

The movement to fundamentally reform Australia’s industrial relations system has become more vocal, well organized and influential since the mid-1980s. While the outcome of this process is yet to emerge, it is now clear that basic changes in Australia’s industrial relations system will occur.

Driving recent calls for industrial relations reform has been a recognition by the major industrial parties that if Australian industry is to become more internationally competitive, workplaces will have to become more efficient and productive. It has been argued that to achieve this industrial relations institutions should be restructured (Blandy et al., 1986). The problems of low productivity levels and inefficiency, it is often asserted, are caused by strict demarcation of duties prescribed in award job classifications and work practices that restrict managers’ ability to use human and capital resources efficiently. In addition the insensitivity of the wage fixing system to the needs of individual enterprises has been singled out for special attention (Brown & Rowe, 1986). These problems, it is claimed, arise from our industrial relations institutions: the structure of unions, the industrial tribunals and the plethora of industrial regulations and laws that limit employers’ ability to organize the means of production as they see fit. It is argued that many of these rules and regulations should be reduced if the objectives of labour market reform are to be achieved. According to some advocates of industrial relations reform, efficiency can only be improved if the shackles of regulation are abolished, or at least greatly reduced, and replaced with rules that are prescribed by management or management in consultation with employees or unions. This reform position is widely known as the movement for labour market deregulation.

Casting the debate as a choice between a ‘regulated’ or ‘deregulated’ labour market, however, is misleading. Those advocating radical reform are not seeking to

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deregulate the labour market but rather change how the labour market is regulated. 'Deregulationists' wish to replace regulations that are external to the workplace with rules that are determined within business units. In this paper we examine the different forms of 'deregulation' that have been proposed. We have called these the 'deregulationist' and the 'managed decentralist' approaches. Both concentrate on the alleged negative affects of external forms of regulation, ignoring the significant flexibility available to managers, unions and employees to negotiate suitable arrangements at workplace level within the present regulatory system. Both positions neglect the role and importance of externally devised regulations for promoting equity and efficiency at workplaces. We go on to examine the role of external forms of regulation in promoting efficiency and equity in the labour market. We conclude by arguing that the debate on equity and efficiency at work should move away from a preoccupation with 'labour market deregulation' and internal forms of regulation. Instead, greater attention should be devoted to identifying better ways of linking internal and external forms of regulation to improve labour market operations.

Throughout this paper we refer to both 'equity' and 'efficiency' as objectives to be promoted by labour market regulation. These terms are widely used, but their meaning is often unclear. Orthodox economists often argue that efficiency and equity issues should be treated separately: first improve economic performance and then decide how to distribute the benefits. It is alleged that, unless the two policy objectives are kept distinct, efficiency is compromised, which in turn limits the resources available for distribution (Rees, Rodley & Stilwell, 1993, p. 9).

We do not share this view. Production and distribution issues are often intimately related. For example, we believe that the hallmark of an efficient economy is one that operates at a full employment level of capacity utilization. Less than full employment means that labour and capital resources are not used to their full potential. In this way high levels of unemployment are not just unfair, they are also inefficient (Pasinetti, 1981, pp. 148–50). At the micro level a longstanding literature has explored the importance of workers' perceptions of fairness for their productive efficiency on the job (Jacques, 1961; Lewin & Peterson, 1988; Brown, 1989; Sheppard, Lewicki & Minton, 1992). The insights from this and related literature have informed the 'new Keynesian' theory of efficiency wages (see, for example Groschen, 1991, pp. 369–73). As Streeck argues, equity does not only refer to 'entitlements for consumption, but [also] to rights of access and utilisation of productive capacities' (Streeck, 1991, p. 27). We argue that labour market regulation has an important role to play in simultaneously promoting efficiency and equity at work.

The drift to a 'deregulated' labour market
There has been a long history of advocates calling for a fundamental restructuring of Australia's distinctive industrial relations system. From the introduction of arbitration at the turn of the century until the mid-1980s such proposals had only minor relevance to mainstream research and policy debates. Since the mid-1980s, however, the push for labour market deregulation has grown in intensity and political support.

Increasing organizations' productivity and effectiveness through what became known as labour market flexibility reforms was also a fashionable trend among OECD countries during this period (Sarfati & Kobrin, 1988; Pollert, 1988, 1991)
Proponents of ‘labour market flexibility’ based on the assumption of a rational free market argued that organizations needed to become more adaptable in such things as their hours of operation, the use of their labour resources and the payment systems and the methods of wage fixing they used. These proposals, many believed, could only be put into practice through fundamental industrial relations reform.

In Australia during the 1980s the most vocal advocates of reform were a number of influential media commentators, business leaders and employer organizations, most notably the Business Council of Australia (BCA). The demand for reform was couched in terms of a call for less external industrial regulation of business. This was made forcefully in the council’s report, *Enterprise Based Bargaining Units: A Better Way of Working* (1989). While ostensibly arguing for a more decentralized system of industrial relations that was more responsive to workplaces’ particular requirements, it assumed that this could only be achieved by reducing the role of external regulatory bodies such as the Australian Industrial Relations Commission. This view was expressed clearly in the BCA’s 1989 report, which stated that what was needed was

> a fundamental reorientation of the system away from one largely focussed outside the enterprise and adversarial in nature towards one which is centred on the enterprise ... (BCA, 1989, p. ix).

At the same time the Australian Council of Trade Unions (ACTU) and the federal Labor government detailed plans for restructuring Australian unions, reforming the system of awards and giving collective bargaining a greater enterprise focus. In 1988 the minister for industrial relations, Ralph Willis, issued a blueprint for labour market reform that generally endorsed the need for greater labour market flexibility as part of the government’s broader microeconomic agenda. The centrepiece of this approach was the call for award restructuring, which would ‘remove obsolete classification, reduce the number of classifications, broadband a range of jobs under a single classification and establish links between training, skills and wages which result in career paths for workers’ (Willis, 1988, p. 12). The trend in government policy changed more noticeably in the early 1990s. In May 1991 the then treasurer, Paul Keating, was particularly critical of the Australian Industrial Relations Commission following its rejection of widespread calls to promote enterprise bargaining. In an interview with the Australian on 1 May 1991 he made the following points:

Q: You obviously see this as a fundamental turning point for wage fixation?
A: I saw it as that in January 1990. That’s when I saw it. It might have dawned on many other people in April 1991.

Q: What you are really saying is that you’re deregulating the labour market?
A: In an evolutionary way, yes.

These calls for deregulation and reform have led to some dramatic policy developments in the area of wage fixation and workplace reform. One of the most obvious effects has been to reduce the role of industrial tribunals in determining movements in wages. As early as 1987, in response to pressures for wages policy to be less prescriptive, the system of wage fixation became far more decentralized and the role of the Australian Industrial Relations Commission more circumscribed. In recent years amendments to the Industrial Relations Act have reduced the ability of the commission to administer a coherent and workable wages policy. While the arbitration system has never ‘controlled’ aggregate wage outcomes, it has, over the
years, played an important role in managing the growth of earnings. The push for the 'deregulation' of our wages system has been based on a desire to reduce the influence of the longstanding comparative wage justice principle in Australian wage fixing. In its place has been the objective of linking wage movements more closely to productivity growth within the enterprise. The assumption is that Australia's system of national wage cases and multi-employer award coverage penalizes those employers unable to pay wage rises based on price and productivity increases at national or industry level. Wage determination that is more directly concerned with individual enterprises' 'capacity to pay' will, it is argued, improve efficiency.

Another legacy of the push for labour market deregulation has been manifested in an increased demand for workplace reform. Experimentation with work redesign and work restructuring has a tradition in Australia that dates back to at least the early 1970s when industrial democracy or employee participation attracted considerable policy interest, particularly from the South Australian government (Davis & Lansbury, 1986). These 'experiments' saw the introduction of schemes such as semi-autonomous work groups and quality circles in a range of organizations, although it is unclear how widespread these initiatives were in Australian organizations. In contrast, the more recent calls for workplace reform are not essentially designed to democratize work. Instead, current reforms aim to change or eliminate rules that demark duties, remove restrictions on work time arrangements and work practices, and inefficiencies that are allegedly codified in awards or enforced through custom and practice. Some supporters of award restructuring and workplace change believe that a degree of labour market deregulation is a necessary part of this reform process. They believe that the present formal external regulatory framework is too rigid and distant from the needs of enterprises (Niland, 1978; Niland, 1989; Angwin & McLaughlin, 1990). The problem, it is claimed, is that organizations have been forced to live with rules and regulations that have been imposed by external bodies, such as the Australian Industrial Relations Commission, that seek to codify conditions across a range of employers and sometimes across industries. As a result the rules that organizations must live by are not necessarily the most appropriate to their needs or circumstances. Reducing the role of industrial tribunals is therefore seen as a necessary prerequisite for promoting joint or negotiated regulation between employees/unions and employers at the enterprise level. The more strident advocates of deregulation, while supporting workplace change, believe that the change should be determined unilaterally by management who are in the best position to decide what is best for their own organizations.

In short, the preoccupation with workplace reform has resulted in either hostility or indifference to the importance of labour market regulation. Just how well formulated is this push for change? This question requires consideration of what labour market regulation involves.

The dimensions of regulation
Part of the difficulty in distinguishing between industrial relations reform options is the imprecision of the terminology. The term 'deregulation' as it has been used suggests that industrial relations can, in time, become unregulated. As industrial relations scholars have noted for years, however, such an outcome is impossible. (For recent examples, see O'Brien, 1990; Dabscheck, 1993).

Following Bray, we define labour market regulation as 'the creation and enforce-
ment of rules which are designed to control the actions of individuals and groups who are a party to the production of goods and services' (Bray, 1990, p. 1). This definition implies that rules will always be a basic element of any industrial relations system. The production of goods and services requires the co-ordination of activities that transform resources into an activity or product. To achieve these it is necessary to have procedures or rules that will ensure efficiency. In reality, then, the debate is not about whether there should be rules but about the source of rules and what form they should take.

How rules concerning work are created and enforced has been the central concern of industrial relations research (a fact that might easily be forgotten, given the limited role industrial relations researchers and academics have played, to date, in the deregulation debate in Australia). It was Allan Flanders, writing nearly thirty years ago, who described industrial relations as 'a study of the institutions of job regulation' (Flanders, 1965, p. 10). In that seminal essay Flanders distinguished between internal and external sources of job regulation. Internal regulation arises because every business or organization 'has a structured pattern of relationships which have a permanence and a distinct identity, irrespective of the individual personalities involved'. External regulation derives from 'the external environment in which the enterprise is placed. These limit the freedom of the enterprise and its members in their rule-making activities'. Flanders argued that the different sources of rules addressed quite different problems. External forms of job regulation arose to protect workers from 'the devastating and degrading effects of unregulated labour markets' and to keep the 'conflict between unions and employers within reasonable bounds ...' Internal forms of regulation, on the other hand, responded to another need. 'Here the principal drive has come from managements seeking to bring the work behaviour of employees under greater control' (Flanders, 1965, pp. 15-18).

Another leading British industrial relations researcher, Hugh Clegg, has argued that it is important to note the different forms that work rules can take. Writing for the Donovan Commission in the late 1960s, he argued:

> Britain has two systems of industrial relations. The one is the formal system embodied in the official institutions. The other is the informal system created by the actual behaviour of trade unions and employers' associations, of managers, shop stewards and workers (quoted in Clegg, 1990, p. 4).

Even though Clegg referred to two 'systems' of industrial relations, the concepts of 'formality' and 'informality' can also usefully be applied to the nature of rules. Formal rules can arise from the authority of official institutions such as government agencies or managers in the workplace. Informal rules may come about as the result of custom and practice at the workplace and may be based on no more than a shared understanding between the parties or the culture of a workplace. Equally the behaviour and actions of groups such as unions and employer associations beyond the workplace may result in the application of informal rules that regulate activities within organizations. A shared understanding between employers about wage rates and wage movements is one example of this type of informal rule making. Differences in the degree of formality of rules are also associated with how rules are enforced. Formal rules are most often sanctioned by law or authorities with legal standing, such as industrial tribunals or executive government agencies. Informal rules, on the other hand, are not usually enforced by official institutions but rather by
actions of the parties, such as threats of non-co-operation where there has been a breach of workplace customs or 'norms', and ostracism in the case of workers or employers who breach the ‘rules’ or understandings of their peers. The informality of the sanctions does not necessarily make them any less real or effective.

There are, therefore, two key dimensions to labour market regulation: the sources of rules (internal and external) and their status (formal or informal).

It has long been recognized in Australia that there is a role for external forms of regulation in a number of areas that affect the way organizations are run. It is generally accepted that sometimes decisions based on self-interest or profitability may not be in the best interest of consumers. In the interest of fairness and equity the market may not be the most effective mechanism for achieving national objectives. In Australia external regulation takes a variety of forms. The industrial tribunal system is probably the most visible and best known. In addition, there are numerous federal and state statutes that regulate aspects of employment and business organization. These cover issues such as equal employment opportunity (EEO), occupational health and safety and training, discrimination in employment and long service leave. While the popular perception of external regulation is of prescriptive legislation, external regulation can also be voluntary. Multi-employer ‘understandings’ of acceptable levels of general wage rises or relativities are examples of this form of regulation. Training arrangements such as group apprenticeships can also involve both formal and informal externally generated rules regulating aspects of workplace activity.

The internal dimension of regulation can also be formal or informal in nature. The most prevalent and obvious formal regulations found in organizations are rules and procedures devised by managers and codified in personnel manuals. These specify employees’ obligations and rights and often deal with matters such as the handling of grievances, and procedures for disciplining employees. Where these matters are not codified the rules that prevail are usually determined by employers unilaterally as a matter of management practice. Rules within organizations can also be devised on a joint basis. Such rules can be very informal and simply prevail on the basis of custom and practice. They can be more formal, however, such as enterprise agreements negotiated and registered under section 134 of the Australian Industrial Relations Act or enterprise agreements under state legislation. Should the use of individually negotiated contracts become more prevalent, this would be another example of the increasing importance of internal formal regulation.

The key dimensions of labour market regulation and examples from the Australian industrial relations system are summarized in table 1.

Advocates of deregulation seek to increase the significance of internal modes of regulation at the expense of external modes. Under such a system managers, unilaterally or in consultation with their employees, would determine the rules. Rules arising from outside an organization are regarded as insensitive to its particular needs and are therefore seen as a source of inefficiency. There is no suggestion in the deregulation literature that rules made by management for individuals or groups within organizations should be removed. If some form of regulation is an inevitable and necessary requirement for organizational efficiency, what deregulationists are demanding is a change in the source of rules and/or the form they take. Essentially the call for deregulation is a call for less external regulation and the consequential increase in the importance of internal regulation by organizations. The key issue that
any policy debate about equity and efficiency at work should address, however, is not whether to ‘regulate’ or ‘deregulate’, but rather how to regulate the labour market.

**Approaches to labour market regulation**

Three approaches to labour market regulation can be readily identified in the current policy debates on industrial relations reform. First, there are those who argue for the total deregulation of the labour market. These we call ‘free market deregulationists’. A critical assumption of this approach is that so called ‘unregulated’ labour markets will produce the best social and economic results. The role of government is to provide only a minimal framework that will facilitate the operation of market forces; that is, the external regulatory environment merely provides the framework for internal regulation. In this way the legal system, through contract law, provides organizations with the framework that makes contracts possible within the enterprise. Most importantly, the legal system provides the mechanism to ensure that formal rules determined within organizations are honoured and, if necessary, enforced.

Supporters of this approach believe the market for labour is no different from any other. It is assumed that suppliers of labour (workers) sell their product to the highest bidder (employers). Competition will ensure full employment and the efficient allocation of workers to different jobs. Workers and employers must be allowed to reach individual agreements free of ‘interference’ by external regulatory agents such as unions and government bodies. Such agreements should only be regulated by the common law of employment. To this extent, ‘free market deregulationists’ acknowledge a limited role for external regulation, primarily through the rule of law, but the law only provides a framework for facilitating and enforcing rules determined within organizations. This view of the labour market has a long tradition, and informed nineteenth-century labour law.

The three most influential schools of thought informing this approach to labour market reform are laissez-faire economics, the common law tradition and, more recently, some elements of mainstream human resource management theory. The

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**Table 1** Dimensions of regulations

<table>
<thead>
<tr>
<th>Status of rules</th>
<th>Source of rules</th>
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<tbody>
<tr>
<td>Formal</td>
<td></td>
</tr>
<tr>
<td>Industrial tribunals</td>
<td>Registered enterprise agreements</td>
</tr>
<tr>
<td>Training Guarantee Act</td>
<td>Personnel and disciplinary procedures</td>
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<tr>
<td>Occupational health and safety acts</td>
<td>codified in manuals</td>
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<tr>
<td>Equal employment opportunity and anti-discrimination legislation</td>
<td></td>
</tr>
<tr>
<td>Informal</td>
<td></td>
</tr>
<tr>
<td>Union/employee notions of fair relative wage rates</td>
<td>Workplace customs and practices</td>
</tr>
<tr>
<td>Tacit agreements among employers on the going rate of pay</td>
<td>Unregistered and unwritten workplace agreements</td>
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influence of laissez-faire economics has fluctuated over the years. In the early phases of industrialization in England the policy was strongly supported by a number of influential social philosophers, as well as parliament and the judiciary (Atiyha, 1979). After the Second World War more active government involvement in economic regulation received extensive legitimacy with the emergence of Keynesian economics. From the early 1970s the Keynesian challenge came under attack from a resurgent laissez-faire movement. Supporters of the free market solution still remain influential in the economics profession (Nevile, 1990; Pusey, 1991). Many elements of a laissez-faire outlook still inform the common law. This is especially the case with the law of employment and the law of trade unions. Common law notions of freedom of contract and restraint of trade provide a powerful complement to laissez-faire economics. More recently some of the human resource management literature has also argued for a reduction in state and union influence at the workplace.

The primary supporters of this 'free market deregulationist' approach to labour market reform have been the Liberal–National Party Coalition at federal and state levels and employer organizations such as the Business Council of Australia, the Australian Chamber of Commerce and Industry and the National Farmers Federation. Influential pressure groups include the H. R. Nicholls Society and the small business lobby (Dabscheck, 1989, 1990). Within the federal bureaucracy significant and persistent support for this position has come from the federal Treasury and the Industry Commission.

The second approach to labour market regulation is sometimes referred to as the 'managed decentralism' approach (McDonald & Rimmer, 1989). Supporters of this position see the critical issue as the need to decentralize the system of industrial relations. Some reduction in the extent of external forms of regulation is believed to be a necessary pre-condition if a more responsive and effective decentralized industrial relations system is to emerge. Advocates of this position claim that the economy's performance can only improve if individual workplaces and enterprises are restructured. They assume that the external industrial relations regulatory system has hindered the workplace change process.

The intellectual traditions informing this position are diverse. Industrial psychology has played a large role in influencing reforms such as job redesign and work reorganization and improving the performance of teams within the workplace (Berg, Freedman & Freedman, 1978; Rose, 1988, 1990). Industrial psychologists have largely been silent on the role of external regulation. However, implicit in their analysis is an assumption that workplace reform requires a restructuring of work relations and the provision of more challenging and intrinsically rewarding jobs, and that this cannot be achieved within the restrictions of prescriptive awards and regulations that have been determined externally. To the extent that the external regulatory system, through awards, imposes restrictions on organizations' ability to restructure work, there is a need to reduce such forms of regulation. Some advocates of flexible specialization argue that the critical issue is improving the responsiveness of organizations to an increasingly volatile external environment (Piore & Sabel, 1984). They argue that markets for mass produced goods have become satiated and that the traditional tools of macroeconomic management can no longer work effectively to improve economic performance. Only business units that are responsive to change will perform well, and co-
operative forms of work organization within enterprises are needed to provide the responsiveness needed for competitive success. Employee participation and individual or collective bargaining between employers, employees and unions at enterprise level are regarded as essential to solving our current economic problems. Recent developments in wages policy, most notably the award restructuring and enterprise bargaining principles, have been informed by these concerns. As Curtain and Mathews (1990) put it,

Award restructuring, by linking wages with new job structures based on skills acquisition, will free up the external constraints which have reinforced Taylorist forms of work organisation. (Curtain & Mathews, 1990, p. 436)

While ‘free market deregulationists’ advocate the wholesale dismantling of the award system, supporters of ‘managed decentralism’ believe that the current system still has a role to play, particularly in maintaining minimum standards for wages and conditions.

An extensive array of forces and interest groups is clustered around this position. It includes the federal Labor government and parts of the union movement. Arguably the most vocal advocates of this position have been industrial relations and workplace change consultants (Ewer et al., 1991).

Finally, there is the position we call ‘co-ordinated regulation’. Supporters of this position believe that external forms of regulation are important in redressing inequalities and inefficiencies that may emerge where too much reliance is placed on internal modes of regulation. Matters of particular concern are inequalities based on gender and ethnic differences and the effect that workers’ notions of fairness about wages and conditions earned by employees undertaking similar work for different employers can have on relative pay and work performance. Such issues can have major implications for efficiency as well as equity within the labour market.

The intellectual underpinnings of this group come from a number of sources. Keynesian and post-Keynesian economists have long argued that it is erroneous to analyze the labour market on the basis of the simple price auction model. For these economists problems such as unemployment can only be addressed by regulating the labour market on an economy-wide basis (See, for example, Layard, Nickell & Jackman, 1991). Labour market segmentation theorists, building on the insights of earlier generations of institutional labour market researchers, have noted that there is not one labour market but myriad groups based on occupation, industry and organizational structure (see, for example, Villa, 1986). Moreover, social customs such as attitudes to women often have a powerful influence on the way individuals and firms perform in the labour market. Much classical industrial relations research and many labour historians have examined institutions associated with labour market structures and argued for the importance of understanding the context in which workers and workplaces operate (Marsden, 1986; Brown & Nolan, 1988). For many in this tradition, regulation is only one factor influencing the labour market and it is often required to redress some of the inefficient and inequitable results that arise from market forces.

Disparate people and institutions have expressed concerns about reducing the importance of externally determined rules. They argue that there is a critical role for some form of external regulation if equity is to be an objective of economic reform. Many women’s groups and welfare organizations have expressed concern about the...
possible detrimental effect on their constituents if external modes of regulations are reduced, and have asserted that a preoccupation with enterprise performance diverts attention from other labour market issues. Among industrial groups, and for different reasons, the Metal Trades Industry Association has persistently supported an active role for Australia's industrial tribunals in regulating the labour market. The association's interest in regulation arises from its experiences in the 1970s and 1980s, when a form of over-award enterprise bargaining resulted in a wage breakout in the metals sector. The association is concerned that too great a reliance on internal modes of regulation may lead to excessive wage increases in the recovery phase of the business cycle (Boland, 1992). External forms of regulation that assist in coordinating wage movements can be important for preventing this problem or minimizing the extent of wage movement when recovery begins. A number of arbitration commissioners have also noted the importance of the tribunals for efficiency and equity (Hancock, 1985; Isaac, 1982). They argue that the tribunals play an important role in rectifying labour inefficiencies and inequalities such as unfairness in male–female earnings relativities.

Table 2 summarizes the key elements of the different views of regulation.

The limitations of the current policy options
Both the 'free market deregulationists' and the 'managed decentralists' overestimate the gains that may come from significantly reducing the extent of external regulation of the labour market. Their case for reducing external regulation rests on a belief that this form of regulation significantly limits the ability of organizations to regulate their own affairs internally.

There is now a body of evidence that suggests that the formal external regulatory environment, particularly the tribunal system, does not greatly inhibit firms' strategic choices. The Australian tribunal system has been shown to allow a large degree of flexibility within a broad framework of minimum conditions (Isaac, 1990; Green & MacDonald, 1991). The Australian Workplace Industrial Relations Survey (AWIRS)1 indicated the degree of flexibility and diversity at workplaces operating within the award system. Indeed, in terms of payment systems, 52 per cent of workplaces with twenty or more employees paid over-award rates, and nearly one-third (32 per cent) of workplaces operated performance-related payment schemes. Profit-sharing schemes (8 per cent) and share ownership schemes (13 per cent) were rare, but were still possible under the regulatory system. It would seem that the incidence of these 'flexible' payment schemes has more to do with management and employee attitudes than with any prohibition or difficulty arising from the external regulatory system.

Historically, the external regulatory system has preserved management's prerogatives against the encroachment of union demands over a range of issues (see, for example, Sorrell, 1979). As Carroll states, the tribunals recognize 'that subject to employees not being prejudiced or their rights affected management should have the right to regulate its operations in the most efficient manner' (cited in

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1. This survey involved personal interviews with union and management representatives from more than 2300 workplaces in all industries except agriculture and defence. It was undertaken throughout Australia between November 1989 and May 1990. Full details of the survey are provided in Callus, Morehead, Cully and Buchanan, 1991.
<table>
<thead>
<tr>
<th></th>
<th>Managed decentralism</th>
<th>Co-ordinated regulation</th>
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<tr>
<td><strong>ree market deregulation</strong></td>
<td>The importance of internal rule making should be increased to improve enterprise performance</td>
<td>Better links should be established between external and internal modes of regulation</td>
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<tr>
<td><strong>iews on external and internal regulation</strong></td>
<td>Some external regulation is needed to maintain minimum standards</td>
<td>External regulation has an essential role to play in promoting efficiency and equity</td>
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<tr>
<td><strong>ime of external regulation is to uphold internal rule taking (e.g. contract law)</strong></td>
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<td><strong>ost influential analytical traditions</strong></td>
<td>Organizational behaviour</td>
<td>Keynesian/post-Keynesian economics</td>
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<tr>
<td><strong>aissez-faire economics (born-again neoclassical fundamentalists)</strong></td>
<td>Harvard Business School HRM and industry development work</td>
<td>Traditional industrial relations and labour process research</td>
</tr>
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<td><strong>onmon law</strong></td>
<td>Some versions of post-Fordism/flexible specialization</td>
<td>Labour market segmentation theory</td>
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<td><strong>initarian approach to human resource management</strong></td>
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<td>Feminist analyses of the labour market</td>
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<td><strong>search priorities</strong></td>
<td>Organizational/enterprise performance</td>
<td>Understanding the operation of labour market segmentation and multi-employer relations</td>
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<td><strong>nderstanding the operation of market mechanisms, the generation of legal precedents and management decision-taking processes</strong></td>
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<td><strong>olicy priorities</strong></td>
<td>Workplace reform and flexibility and enterprise bargaining above minimum award standards</td>
<td>Maintenance and promotion of consistent labour standards to improve equity and efficiency in the labour market</td>
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<td><strong>alue priorities</strong></td>
<td>Efficiency and equity</td>
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Dufty & Fells, 1989, p. 36). Indeed, for management a further reduction in external modes of regulation may mean that issues that have previously not been regarded by the tribunals as legitimate industrial issues may become bargaining issues between the parties, particularly if the tribunals no longer have a role in determining which issues are ‘negotiable’ and which are not (Callus, 1992).

There is reason to believe that the alleged negative effects of the external regulatory system have been overestimated. Indeed, it appears that organizations may be more influenced by management culture, product market conditions and management initiated ‘restructures’ than by the regulatory environment in which the organization operates. For example, when asked about the major barriers to efficiency in their organization workplace managers interviewed in AWIRS rarely mentioned industrial relations matters. While 57 per cent felt that no change was needed, around 80 per cent of those facing serious constraints indicated that non-industrial relations issues were the problem. Their responses are summarized in table 3.

Table 3 Reasons why managers feel they cannot make efficiency changes at their workplace

<table>
<thead>
<tr>
<th>Reason</th>
<th>Private</th>
<th>Public</th>
<th>All</th>
</tr>
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<tbody>
<tr>
<td>Lack of money or resources</td>
<td>32</td>
<td>24</td>
<td>29</td>
</tr>
<tr>
<td>Management or organization policy</td>
<td>14</td>
<td>32</td>
<td>20</td>
</tr>
<tr>
<td>Unions</td>
<td>14</td>
<td>14</td>
<td>14</td>
</tr>
<tr>
<td>Government rules and regulations</td>
<td>9</td>
<td>18</td>
<td>12</td>
</tr>
<tr>
<td>Awards</td>
<td>6</td>
<td>9</td>
<td>7</td>
</tr>
<tr>
<td>Other</td>
<td>28</td>
<td>15</td>
<td>24</td>
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</tbody>
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Population: Australian workplaces with at least twenty employees, where the general manager felt an efficiency change was needed but could not be made. Figures are weighted and are based on responses from 891 general managers. Some managers gave more than one response. It should be noted that responses varied according workplace size, with those employing 500 or more workers being twice as likely as workplaces with 20–50 employees to report problems with unions and awards.

Source: Callus et al., 1991, p. 204.

The belief that reducing the importance of external modes of regulation will result in significant and sustainable productivity improvements appears to be quite unfounded. According to workplace managers, sustained productivity improvement is far more likely to arise from investment in new capital equipment and more effective management practices.

Efficiency and equity: the importance of external regulation

In recent times contributors to the analytical and policy debate on industrial relations reform in Australia have largely ignored the positive role external and formal modes of regulation can play in achieving a more efficient and equitable labour market. As noted, supporters of ‘free market deregulation’ believe that the operation of market forces will deliver economic efficiency. A key assumption is that the market for
labour is the same as any other. Relations within it, they believe, are settled by myriad individual buyers and sellers exchanging services (labour) for money (wages), regulated on the basis of the law of contract.

The major weakness of this conception of the labour market derives from this basic assumption. Generations of industrial relations and labour researchers have questioned the validity of this abstraction. Labour is not a tangible commodity—what is traded is a worker’s ability to work, not the work itself. Trade in this potential service cannot be analyzed in the same way as trade in tangible commodities such as second-hand sports cars or antique clocks. Labour supply is primarily determined by demographic trends and social customs, such as the changing role of women and young people in the workforce. Labour demand is primarily a function of anticipated demand for output. The price of labour is most strongly influenced by notions of acceptable living standards. While conditions of supply and demand have some influence, they are not the critical factors determining pay rates. Consequently, while in theory adjustment in the labour market can involve changes in wages or employment, most change occurs in employment levels (Schultz, 1985; Villa, 1986; Marsden, 1986; Kaufman, 1988; Kruger & Summers, 1988; Groschen, 1991).

The labour market, far from being a potential clustering of harmony and order arising from free choices made by isolated individuals, is in fact highly structured. Segments of the workforce do not compete with each other for jobs. Instead, the workforce is divided into myriad groups on the basis of industry, firm or enterprise and occupation. The precise nature of segmentation in any one sector of the economy varies on the basis of production technology, industrial structure and product market conditions. Within these constraints the results of strategies pursued by employers, employees, unions and state agencies also influence the nature of labour market segmentation (see Villa, 1986 and Groschen, 1991).

The importance of rules made outside the workplace has often been neglected or overlooked by those advocating workplace change and managed decentralization of the current system. Their concentration on organizational performance, workplace change and enterprise bargaining has meant that little attention has been given to examining and improving the structure of the current institutional environment. Given the nature of labour market structures, it is obvious that many equity and efficiency problems cannot be solved on a workplace-by-workplace or enterprise-by-enterprise basis. The problems involve practices and arrangements that are common to many business units. They require strategies involving external modes of regulation that promote consistent standards across business units.

For example, if the importance of the external regulatory environment is reduced, the results of workplace bargaining will depend largely on the relative power of the parties. The market mechanism or even workplace bargaining under such a system cannot ensure that results are equitable or fair; those parties with most bargaining power will do best. If fairness is to remain an important consideration in evaluating the operation of our industrial relations system, externally generated rules that are applied to all organizations may be the only way of guaranteeing it.

Additional benefits of external methods of regulation can be shown by considering a number of problems that regularly occur in the labour market. These range from macroeconomic issues, such as unemployment, to microeconomic issues, such as training and labour mobility, and longstanding equity issues, such as male–female wage relativities.
The problem of unemployment is a recurring one. While it is important to acknowledge that labour market factors are not the only factors having a bearing on it, they do have some effect. As Soskice (1990) in particular has argued, informal co-ordination between employers has often underpinned the superior performance of Swiss and Japanese labour markets.\textsuperscript{2} This research indicates that informal, external modes of regulation, such as tacit multi-employer agreements, produce better results than modes based on unco-ordinated enterprise bargaining where only factors internal to the enterprise or workplace are taken into account. Some form of external co-ordination appears to be associated with superior employment outcomes.

More recently a number of studies in the United States and the United Kingdom have established that under certain conditions raising statutory based minimum rates of pay can increase employment levels in particular industries, rather than reducing them. (Katz & Krueger, 1992; Card & Krueger, 1993; Dickens, Machin & Manning, 1993) These studies raise serious questions for those economists who believe that formal labour market regulation only causes higher levels of unemployment (such as Anderson & Blandy, 1993).

The issue of relative pay is another recurring cause of concern in the labour market. ‘Free market deregulationists’ have argued that wages should only be related to internal factors, such as individual performance and the enterprise’s capacity to pay. However, the maintenance of consistent wage standards across workplaces for workers in similar occupations has important efficiency and equity benefits. As long ago as the 1930s the American labour economist Paul Douglas noted that it was unhelpful to link an individual’s pay to her or his productivity (Douglas, 1934, cited in McNulty, 1980; see also Oswald, 1992). For example, if wages were strictly linked to productivity the pay of labourers in industries with slow productivity growth (e.g. road maintenance workers) would drop significantly relative to those where productivity growth was strong (e.g. process workers in chemical manufacturing). Over time no one would apply for jobs in road maintenance and there would be an oversupply of applicants for positions in the chemicals sector. Such a wage system would also reduce the profits available for further investment arising from productivity growth. Relating wages to internal factors encourages neither efficient labour allocation nor investment. It is far more efficient to have a stable relative wage structure that is based on skill content and quality of labour rather than the luck of where a worker is placed in the economy as far as productivity growth is concerned. Externally agreed benchmarks for pay (such as award rates or industry-wide industrial agreements) help maintain stability in the labour market and prevent inefficient movements in wages and workers that would arise with enterprise-based wage arrangements.

A related issue is occupational mobility and the transferability of skills. Major efficiency gains can result from multi-employer training arrangements underpinning common occupational structures that are used by a range of employers. The benefits of such arrangements have been identified by a number of studies (Daley, Hitchens & Wagner, 1985; Steedman & Wagner, 1987 and 1989; Prais, Jarvis &

\textsuperscript{2} In referring to the ‘success’ of Japanese labour market, we are only referring to its relatively impressive aggregate unemployment performance. We do not believe that other features of its labour market, such as its large subcontractor sector or the increasing differential in male-female earning, are desirable, either for Japan or anywhere else. See, for example, Itoh, 1990, pp. 192–8 and Rowthorn, 1992.
Wagner, 1989). A comprehensive study of German and French manufacturing involved comparing the performance of a series of factories of similar size and production technology in the two countries' chemicals and metals industries (Maurice, Sellier & Silvestre, 1984, 1986). The researchers identified how firms' practices were intimately related to their operational environment, especially education, training and wage determination systems. For instance, the well-developed vocational training system in Germany ensured that a steady supply of technically competent workers was available to employers. These workers could easily be deployed as work requirements changed. France's generalist education system meant that employers had to rely on internal labour markets and closer supervision arrangements to ensure that work was performed efficiently. The study highlighted the importance of multi-employer arrangements (that is, external modes of rule making) for improving efficiency. Increased reliance on internal modes of regulation is likely to promote enterprise-based training systems, and to reduce the number of workers with transferable skills, as each employer seeks to limit the mobility of trained workers. This in turn is likely to result in skills bottlenecks as the economy expands. Osterman (1988) and Mitchell, Peng and Zaidi (1992) have documented problems such as these arising from the inflexibilities of internally based employment systems in the United States.

External regulation of wage rates can also promote the growth of a 'high wage, high productivity' economy. If a company increases market share for its products by reducing costs through wage cuts, this places pressure on other firms to do likewise. In time, segments of the economy that are reliant on low wages can emerge, drawing capital away from other possible uses, and as a consequence low wages can retard economic development in the long run. This was one of the reasons why Australia established a minimum wage. In 1909 Justice Higgins argued that if a company could not pay fair wages it did not deserve to remain in business (Higgins, 1922). He saw no reason why employees should subsidize the inefficiencies of their employers. The rationale was that wages policy should assist in determining the structure of the economy by preventing the emergence of a low-wage sector. One of the legacies of the conservative governments of the 1980s in the United Kingdom and the United States appears to be the establishment and growth of such low-wage sectors (Brosnan & Wilkinson, 1988; Harrison & Bluestone, 1988; Bluestone & Harrison, 1990).

The equity implications of external regulation can be seen in the case of women's pay. It is recognized among labour economists that Australia achieved one of the most comprehensive and rapid changes in male–female earnings ratios in the world because of the very extensive nature of Australia's labour market regulatory institutions (Gregory & Duncan, 1981; Whitehouse, 1990).

Finally, employers do not always have the motivation or initiative to undertake efficient labour management practices. It is now well recognized in management research that better communication, information and consultation between management and employees can lead to a more productive, stable and efficient labour

3. A more developed theory along these lines was devised by the Swedish labour movement in the 1940s and 1950s and underpinned the high wage, high productivity economy that developed there in subsequent decades. See, for example, Martin, 1985.

4. The equity problems associated with more enterprise-based industrial relations systems in Canada, Japan and the United States are considered by Brav, 1993.
force. Yet while the methods of communication and management—employee communication remain almost completely free of external forms of regulation, the majority of Australian workplace managers do not communicate with or consult the workforce on key issues. This was clearly demonstrated by the AWIRS finding that at the majority of workplaces management did not consult employees about the introduction of a major organizational change that was going to affect them. Figure 1 indicates the roles of different groups in the decision to introduce major changes at the workplace. Consultation was not the normal practice in most workplaces. In many workplaces managers did not even bother to inform, let alone involve, their employees in decisions concerning the most significant changes.

In this case it appears that an environment free of external regulation does not necessarily produce more efficient practices.

It is clear that the underpinnings of the deregulationist and ‘managed decentralist’ approaches have significant limitations. A preoccupation with informal and internal modes of regulation means that insufficient attention is devoted to the problems that arise from the labour market’s tendency spontaneously to segment. Many of the problems of segmentation can only be avoided where effective minimum standards are maintained throughout the labour market.

Having established the importance of the formal and external modes of regulation, the question remains: how should the twin objectives of equity and efficiency at work be promoted?

**Linking external and internal modes of regulation: the critical issue for labour market reform**

Supporters of ‘deregulation’ believe that the only role for regulatory bodies beyond the workplace is to enforce agreements reached internally within organizations. The assumption is that substantive rules about how work should be regulated are best settled between individuals in organizations. The role of the law is to uphold these agreements if they are not honoured.

The previous section attempted to establish that there is a role for external rules beyond this very limited, procedural function. Specifications for actual (minimum) rates of pay, agreed definitions concerning occupational skills and agreements concerning principles of general movements in wages were all shown to have potentially positive implications for efficiency. The findings of overseas studies of comparable workplaces from different countries also highlight the importance of factors external to the workplaces for improving efficiency within them. This research indicates that the critical factors determining good economic performance are neither internal nor external to the workplace, but come from linking both forms of regulation.

This issue has recently received some attention from labour researchers working at the OECD and International Labour Office. For example, the Manpower and Social Affairs Committee of the OECD has argued in its *Labour Market Policies for the 1990s* (OECD, 1990) that labour market efficiency depends on ensuring that there is an appropriate balance between internal and external flexibility. It expressed concern that too great a reliance on internal modes of regulation could tie workers to the particular needs of firms and limit their mobility to other parts of the labour market. It was particularly concerned that ‘this could easily lead to a situation in which external market transactions and market pricing of particular
Figure 1 Who decides significant workplace change?

Population: Australian unionized workplaces with at least twenty employees, which have operated for at least two years and which have instituted significant workplace change affecting employees in the two years prior to the survey. Based on responses from 1384 workplace managers. All estimates are weighted.

Source: Callus et al., 1991, p. 204.

skills could disappear' (pp. 78–9). And it noted:

For these reasons some minimum level of regulation or provision negotiated between the social partners should ensure flexibility in both internal and external labour markets. In particular this will be indispensable when old job boundaries are removed and broader job classifications are introduced (p. 79).

The OECD Manpower and Social Affairs Committee has demonstrated the importance of external regulation, whether it be formal or informal in status. Guy Standing, research co-ordinator at the International Labour Office, has identified the
need for formal external regulations. Standing has considered these issues in the context of research into alternative routes to flexibility and the emergence of what he calls social adjustment. He argues:

The crucial difference between the current [free market] orthodoxy and a social adjustment view is that the former sees protective regulations as costs and barriers to growth, whereas a social adjustment view is that they express social objectives in themselves and are also instrumental in pushing firms to be more dynamic and co-operative in nature (Standing, 1991, p. 34).

Similar sentiments have been expressed by Streeck. He has argued that preoccupation with enterprise issues can result in the emergence of ‘islands of excellence’ in a sea of mediocrity (Streeck, 1989, p. 94 and Elam, 1993, p. 22). In this context he argues that a critical issue for improved competitiveness at enterprise and national level is the development of effective co-operative networks between firms. Formal external regulations or constraints are often important in this regard as they can ‘impose limits on the hierarchical exercise of property rights so as to force managements … to substitute intelligence for power’ (Streeck, 1992, p. 29).

A comprehensive consideration of issues related to these matters has been undertaken by Paul Osterman (1988), who argues that the operation of internal labour markets can only be understood in the context of wider dynamics occurring in the labour market more generally. According to his analysis, internal labour markets in the United States are experiencing severe strains because of independent changes in the nature of labour supply and demand (pp. 46–7). While difficulties arising from these changes afflict many organizations, they are not unique problems, but part of deeper structural changes occurring across the labour market. For Osterman, the only way to address these problems is to develop a range of public institutions to implement a comprehensive labour market policy that engages with firms’ internal employment practices. The key elements of such a policy would involve government agencies

acting as a midwife to the reform of internal labour markets to help them provide both employment security and labour that can be flexibly deployed to meet changing conditions (Osterman, 1988, pp. 149–51).

Such proposals would obviously involve the better linking of internal and external modes of regulation.

Recent research on industry development and parts of the management literature have also highlighted the importance of linkages between firms as a factor contributing to their collective competitive success (Pettigrew & Whipp, 1991, especially pp. 25–34; Sayer & Walker, 1992, especially chapter 3). This literature indicates that the choices available within firms increase when they co-ordinate activities with other related firms and relevant government agencies. External modes of regulation, be they formal or informal, can play important roles in promoting and facilitating such linkages.

Just how external and internal modes of regulation are best balanced will vary according to workplace size, industry and the matters being regulated. As a start, however, far more attention should be devoted to identifying ways of improving the current linkages between external and internal modes of regulation. On the basis of recent experience, it would seem that general movements in wages should be regulated by national wage cases. Training arrangements, skill standards and many
Employment conditions (e.g. maternity leave, long service leave) are probably best regulated on an industry, occupational and/or regional basis. Issues such as the span of hours worked in the workplace, on-the-job training arrangements and allocation of overtime are perhaps best handled at enterprise or workplace level. Some of this co-ordination already occurs in the industrial relations system. Current arrangements, however, have been developed in an ad hoc manner. The challenge is to make these arrangements more coherent.

Conclusion

Equity and efficiency at work are vital issues affecting both the creation of national wealth and the quality of working life. To date, both academic and policy debate has been preoccupied with the issues of 'deregulation' or reducing the role of external regulation and improving workplace performance. Little attention has been given to the important role of external modes of regulation. To this extent, we would argue, the policy debate has been partial and misdirected.

The fact that the industrial relations policy debate has been cast as a choice between regulation and deregulation in part reflects the dominant role economists have played in this process. The laissez-faire economists who saw the necessity for 'deregulating' the finance market in the 1980s took the next logical step and began focusing on the 'need' to 'deregulate' the labour market (Kelly, 1992). Why the industrial relations research community, which has had a longstanding interest in the modes of labour market regulation, has been so marginalized in this debate is unclear. It may, in part, reflect the preoccupation among many industrial relations researchers with documenting changes that are occurring within a framework set by the policy initiatives of the labour movement and the federal government.

External forms of regulation have a vital contribution to make in improving equity and efficiency at the workplace. Implementation of 'deregulation' as it is popularly perceived would simply result in internal modes of regulation (usually only involving management) becoming the dominant form of rule making. This appears to have been the experience in the United States and the United Kingdom (Harrison & Bluestone, 1988; Bray, 1993; Archer, 1993)

If we are to achieve the twin objectives of improving efficiency and equity the central issue must be: how is an appropriate balance to be struck between internal and external forms of regulation? Calls for the total dismantling of the external formal mechanisms of regulation would exacerbate, not resolve, our labour market problems. Concentrating solely on workplace reform and enterprise bargaining will only segment the labour market even further. If labour market reforms are to make a positive contribution to improved efficiency and equity within Australia, current regulatory arrangements should be improved so that there are better linkages between internal and external forms of regulation. The nature of the linkages will vary according to industry, workplace size and the issue concerned. Industrial relations researchers have an important responsibility to contribute to the development of such initiatives and critically assess panaceas that purport to 'roll back' the frontier of regulation or promise economic salvation through a 'workplace change'-led recovery. The basic ingredients for better economic results revolve around investment decisions, external product market factors and developing trust between management and employees. The external regulatory system provides a minimum floor successful firms rarely fear, as they invariably provide their employees with
more than the required minimum. Moreover, their performance, and that of other firms at present performing less well, can only be enhanced if there are better linkages between external and internal modes of regulation.

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