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Labor Unions and the Joint Employer Rule

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Two significant rulings by the National Labor Relations Board in 2015 expanded the longstanding interpretation of "joint employment," a designation given when two firms are involved in directing, controlling, training and supervising an employee. The NLRB is a politically appointed board that governs employer relations with labor unions, but its new interpretation of joint employment will have the greatest effect on small businesses.

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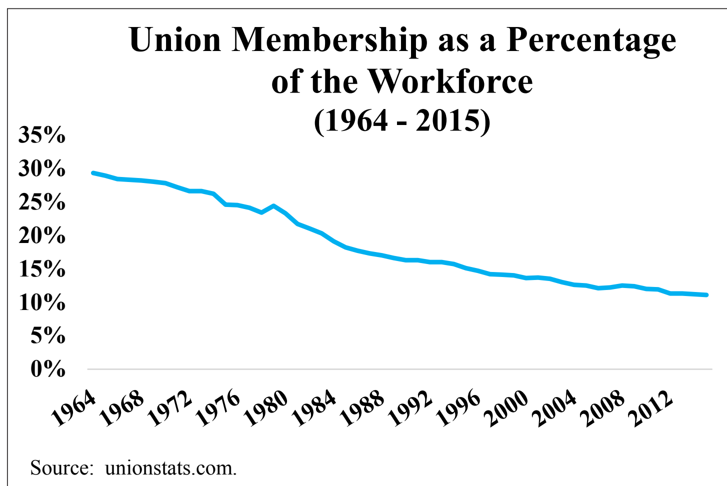
The impetus for the rule is the desire to ease unionization of small businesses that are franchisees of corporations, such as restaurant and retail food chains.

In a 2015 case involving Browning Ferris Industries, the NRLB ruled that Browning Ferris was not only responsible for those it employed directly, but also for contractors and those "indirectly" employed by the firm. Thus, it would be liable for labor violations committed by contractors, even when it has only indirect or "potential" control over employment conditions. In another case, involving McDonald's Corporation, the NLRB ruled that McDonald's is a joint employer and therefore could be responsible for alleged labor and anti-discrimination law violations at its franchises in 30 locations across five states.

Franchises Are Small Businesses. The dictionary definition of a franchise is a store that is given the right to sell a company's goods or services in a particular area. McDonald's has about 2,700 restaurants, 80 percent of which are privately-owned franchises. The franchisor, McDonald's Corporation, creates the line of products sold, markets the store brand through advertising and sets service standards and policies for individual stores to follow. However, individual store owners manage operations, set employee pay rates, hours and schedules and determine other employment policies, such as hiring, firing and promotion. The real issue underlying the McDonald's and Browning Ferris cases has nothing to do with righting alleged wrongs. The ultimate goal is a unionized fast-food workforce in order to boost dues-paying union membership.

Labor Bargaining Units and Regulatory Costs. There is no minimum firm size required for unionization, thus a "bargaining unit" could be one franchise store in one city or it could be an entire chain. Under the joint employer rule, if all McDonald's restaurants are unionized nationwide, employees in one state that vote overwhelmingly against unionization could be overruled by a majority in other states. Small businesses — particularly those with less than 20 employees — already face regulatory costs of nearly $11,000 per employee. The added costs of bargaining and compliance, and potential strikes, lost productivity and reduced profitability, will sink franchise owners.

The Effort to Boost Union Membership. Union membership has declined for the past several decades, due mainly to the loss of



manufacturing jobs. In 1964, 28.4 percent of the workforce belonged to a union, falling to 11.1 percent in 2015 [see the figure]. Private sector union membership declined from 21.5 percent in 1975 to 6.7 percent in 2015, while public sector union membership grew**:**

- Public-sector union membership grew from 23 percent in 1973 to 35.2 percent in 2015.
- Postal, state and local government workers had the highest percentages of union membership in 2015, at 63.5 percent, 30.2 percent and 41.3 percent, respectively.

However, private sector union membership has declined precipitously:

- Construction union membership fell in half, from 29.5 percent in 1973 to 13.9 percent in 2015.
- Manufacturing lost three-fourths of its union membership, falling from 38.9 percent in 1973 to 9.4 percent in 2015.

Unionization and Firm Innovation. It is assumed that employees benefit from union membership through higher wages and representation over grievances, and it is also argued that firms benefit from unions due to lower turnover rates. There is also a hypothesis that laws protecting employees from "bad faith" dismissal help foster firm innovation through increased employee effort because, unlike routine tasks, innovation has a high degree of short-term failure. This is the employee protectionism hypothesis. Another hypothesis is that unions may misalign the incentives of workers, causing them to demand higher wages during a firm's innovation stages, while also encouraging shirking due to reduced negative consequences. Thus, unions could force out more innovative employees.

Researchers at the University of South Florida, University of New Orleans and Indiana University merged data on union elections at 8,809 firms from 1980 to 2002 with those firms' patent applications from 1976 to 2002. They measured firm innovation by the total number of patent applications filed in a given year that were eventually granted, and the total number of non-self citations each patent received in subsequent years, a measure of patent impact. The results:

- Passing a union election led to an 8.7 percent decline in patent counts three years after the election.
- Patent citations fell 12.5 percent three years after an election.
- However, in right-to-work states, where unions have less bargaining power, the effects of union elections were statistically insignificant.
- Finally, the researchers found that firms move innovation activities *away* from states where union elections win.

Unionization and Financial Performance. The results of studies on the effect of labor unions on financial performance have been mixed, mainly because researchers have looked at various countries with different degrees of union influence. However, Paula Voos and Lawrence Mishel at the University of Wisconsin-Madison used data collected by the Joint Economic Committee of Congress on average pre-tax profits/sales ratios for individual supermarket chains (union and non-union) in large U.S. metropolitan areas from 1970 to 1974. They found that:

- Unions lower profitability, particularly of supermarkets with a greater local market share.
- When controlling for other variables that affect profitability — such as market size, market growth, firm size, expenditures on entry and others — unionized supermarket profits were 76 percent lower than non-union supermarkets.
- This effect was most pronounced in concentrated markets rather than more competitive markets.

Conclusion. The franchise sector generates more than $2 trillion in economic activity and employs 20 million people. It would be a mistake to hamstring it with the costs and responsibilities of a poorly interpreted and overreaching rule that would provide no economic benefit to such a significant industry.

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