



# REJECTING THE UNION DISADVANTAGE

by Matthew Lau

**A**s noted recently by Clemens and Veldhuis (2015) in the *Financial Post*, Canada's political leaders seem to be reaching some consensus on tax policy: high tax rates on businesses and individuals discourage investment, job creation, work effort,

and entrepreneurship—all of which are needed to build a prosperous society.

If only more politicians had the courage and inclination to identify and take action on another issue holding back economic growth: Canada's outdated labour relations

laws. An empirical analysis of private sector labour relations laws conducted last year by the Fraser Institute found that compared to the United States, “Canadian jurisdictions generally maintain much more biased and prescriptive labour relations laws” (MacIntyre and Lammam, 2014).

**The total unionization rate in Canada is four times the unionization rate in right-to-work states in the United States.**

One of the results is that unions are much more prevalent in Canada than in the United States. The total unionization rate in Canada is four times the unionization rate in right-to-work states (the 25 US states in which non-union employees in a union workplace are not forced to pay full union dues) and almost twice as high as in non-right-to-work states (Lammam and MacIntyre, 2015).

Unfortunately for Canadians, the economic evidence indicates that jurisdictions with more biased and prescriptive labour relations laws tend to have inflexible labour markets which are less economically productive (MacIntyre and Lammam, 2014). On the other hand, increased market flexibility “permits employees and employers to reallocate resources to maximize productivity” (MacIntyre and Lammam, 2014).

The high unionization rates themselves also tend to have negative economic effects, such as lower job

growth. Long (1993) analyzed the employment in 510 Canadian firms from 1980 to 1985, and found that “within the manufacturing sector, union firms grew 3.7% more slowly per year than nonunion firms, and within the nonmanufacturing sector, union firms grew 3.9% more slowly than nonunion firms.” The presence of unions also tend to reduce investment: a study by Odgers and Betts (1997), which analyzed 18 industries over a 20 year period, found that “in an industry moving from no unions to the mean level of unionization, net investment and gross investment are predicted to fall by 66–74% and 18–25%, respectively.”

Furthermore, as argued by Kozhaya (2005), because unions reduce the wage gap between highly skilled and unskilled workers, they discourage personal investment in education and training. Unions also discourage work effort by promoting compensation systems based on seniority instead of merit (Kelly-Gagnon, 2015). As a result, unionized businesses become less competitive. “Empirical evidence shows unambiguously that unionization leads to lower profitability,” according to Hirsch (1997), who notes that “most studies obtain estimates suggesting that unionized firms have profits that are 10 percent to 20 percent lower than the profits of non-union firms.”

Given the negative economic effects of unionization, it is unsurprising that since 1999, trade unionization rates (the percentage of wage and salary earners who are members of a labour union) have declined in 29 of 34 OECD countries, according to

the most recent data available on the OECD website (undated).

There is one sector, however, where unions are thriving: the government sector. The unionization rate among Canada's government employees is 74.8%, compared to only 16.8% in the private sector (Lammam and MacIntyre, 2015).

**In one sector, unions are thriving: the government sector.**

One of the reasons that the unionization rate is so high in the government sector is that government unions operate in a monopolistic environment and are isolated from market realities like bankruptcy and competition (Lanigan, 2015). At least in the private sector, companies generally face competition, which "forces an economic reality check... it forces employees and management

to pay attention to what the rest of us need and want. Not so in government" (Milke, 2015).

**The result of high unionization rates and lack of competition is inflation in the cost of government labour.**

The result of high unionization rates and lack of competition is inflation in the cost of government labour. According to the Fraser Institute, government employees in Canada receive a 9.7 percent wage premium on average over comparable private sector workers (Lammam, Palacios, Ren, and Clemens 2015). Furthermore, 83 percent of government employees have defined benefit pensions compared to only 11 percent of private sector workers. Government employees also tend to retire earlier,



are absent almost 50 percent more often, and have much better job security (Lammam, Palacios, Ren, and Clemens, 2015).

A literature review by the Fraser Institute shows that numerous other studies in the last few decades have also confirmed government sector compensation premiums of various sizes in Canada (Lammam, Palacios, Ren, and Clemens, 2015). In particular, Gunderson, Hyatt, and Riddell (2000) found that the government wage premium was 11.2 percent—which decreased by roughly one-third when controlling for the impact of unions. Milke (2013) notes that while “unionization does help explain part of the public sector pay and perks advantage”, it is only an explanation, not a justification.

**Federal government workers receive a 13.0 percent wage premium over private sector workers, which increases to 33.2 percent when benefits such as pensions and working hours are considered.**

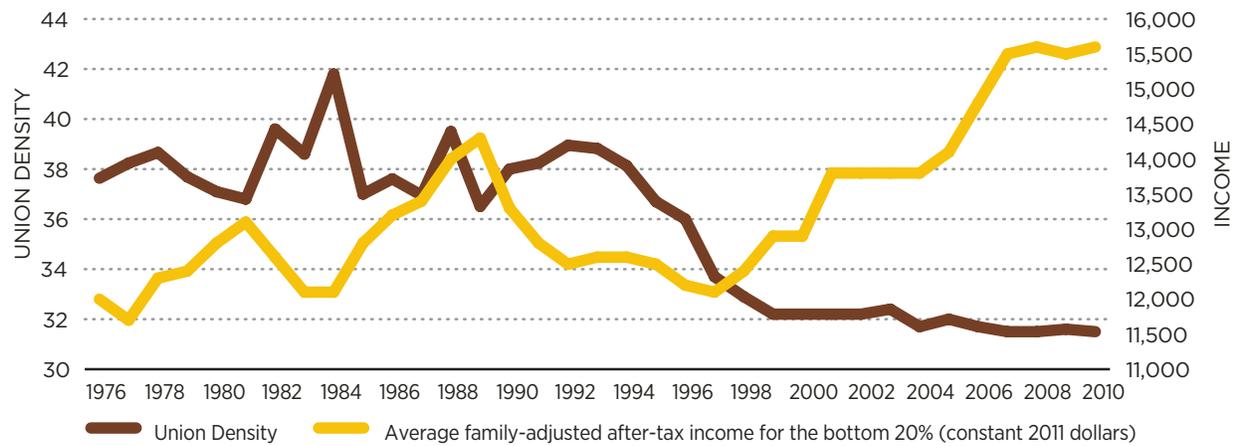
The pay and perks advantage enjoyed by public servants is highest in the federal government. According to a recent analysis by the Canadian Federation of Independent Business, federal government workers receive a 13.0 percent wage premium over private sector workers, which increases to 33.2 percent when benefits such as pensions and working hours are considered as well (Mallett, 2015).

Clearly, there is significant economic benefit to updating laws and policies governing unionization in Canada, since the evidence shows that high unionization rates hinder private sector investment and job creation and are a contributing factor to the wage and benefit premiums received by public servants.

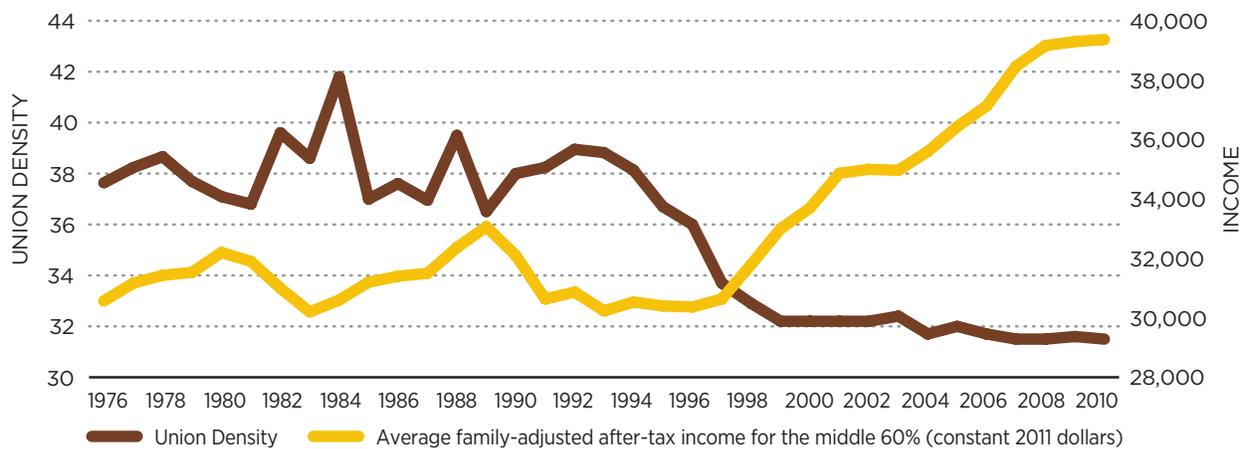
Of course, unions and their allies vigorously oppose reforms to Canadian labour relations laws that favour them. A report sponsored by the National Union of Public and General Employees complains that since the “assault on labour rights and unions began, income inequality in Canada has been steadily rising” and that “in countries where union density has declined, the top 1 percent has been able to reap the gains” (Sran, Lynk, Clancy, and Fudge, 2013). The Canadian Centre for Policy Alternatives points out that the decline in unionization rates in Canada in the past several decades coincides with a rise in income inequality—the implication being that unions are needed to increase the wage of the workers, strengthen the middle class, and reduce inequality (Mackenzie and Shillington, 2015).

Such arguments ignore the disemployment and other negative economic effects of unionization. In fact, incomes for lower- and middle-class households in Canada actually rose when unionization declined—in the latter case, graphing middle-class income against unionization rates over the last few decades produces an almost mirror image. (See Figures 1a and 1b).

**Figure 1a: Unionization rate versus income for the bottom 20% of households in Canada**



**Figure 1b: Unionization rate versus income for the middle 60% of households in Canada**



This evidence doesn't prove that unions hold back the lower-and middle-classes (correlation does not prove causation), but at least provides preliminary data to counter the myth often put forward by unions and their allies that high unionization rates are the silver bullet to strengthening the middle class and reducing poverty.

Given the adverse economic effects of prescriptive labour relations laws

and increased unionization, Canada should consider reforming these laws in a way that makes them more balanced and less prescriptive. **C**



*Matthew Lau is a finance and economics student at the University of Toronto. He will graduate in Spring 2016*

## WORKS CITED

Clemens, J. and N. Veldhuis (2015, September 4). Trending to taxation consensus. *Financial Post*. <<http://business.financialpost.com/fp-comment/trending-to-taxation-consensus>>, as of September 5, 2015.

Employment and Social Development Canada (undated). *Financial Security – Income Distribution*. <<http://well-being.esdc.gc.ca/misme-iowb/.3ndic.1t.4r@-eng.jsp?iid=22?>>, as of September 7, 2015.

Gunderson, M., D. Hyatt, and C. Riddell (2000, February). *Pay Differences between the Government and Private Sectors: Labour Force Survey and Census Estimates*. Canadian Policy Research Networks. <[http://www.cprn.org/documents/15680\\_en.pdf](http://www.cprn.org/documents/15680_en.pdf)>, as of September 7, 2015.

Hirsch, B. T. (1997). *Unionization and Economic Performance: Evidence on Productivity, Profits, Investment, and Growth*. Fraser Institute. <<https://www.fraserinstitute.org/sites/default/files/UnionizationEconomicPerformance.pdf>>, as of September 28, 2015.

Kelly-Gagnon, M. (2015, February 17). Why Performance Pay Beats Unions. *Huffington Post*. <[http://www.huffingtonpost.ca/michel-kellygagnon/union-performance-pay\\_b\\_6694350.html](http://www.huffingtonpost.ca/michel-kellygagnon/union-performance-pay_b_6694350.html)>, as of September 5, 2015.

Kozhaya, N. (2005, August 26). *The consequences of a strong union presence in Quebec*. Montreal Economic Institute. <[http://www.iedm.org/files/sept05\\_en.pdf](http://www.iedm.org/files/sept05_en.pdf)>, as of September 5, 2015.

Lammam, C. and H. MacIntyre (2015, September 3). *Improving Union Accountability with Worker Choice*. Fraser Institute. <<http://www.fraserinstitute.org/sites/default/files/improving-union-accountability-with-worker-choice.pdf>>, as of September 6, 2015.

Lammam, C., M. Palacios, F. Ren, and J. Clemens (2015, June 4). *Comparing Government and Private Sector Compensation in Canada*. Fraser Institute. <<http://www.fraserinstitute.org/research/comparing-government-and-private-sector-compensation-canada>>, as of September 6, 2015.

Lanigan, T. (2015). *Fighting for Taxpayers: Battles Fought and Battles Ahead*. Canada: Thomas & Black Publishers.

Long, R. J. (1993, July). The Effect of Unionization on Employment Growth of Canadian Companies. *Industrial and Labor Relations Review*, Vol. 36, No. 4, pp. 691-703. Retrieved September 26, 2015, from JSTOR <<http://www.jstor.org/>>.

MacIntyre, H. and C. Lammam (2014, August 28). *Labour Relations Laws in Canada and the United States: An Empirical Comparison* (2014 Edition). Fraser Institute. <<http://www.fraserinstitute.org/sites/default/files/labour-relations-laws-in-canada-and-the-united-states-2014-rev.pdf>>, as of September 6, 2015.

Mackenzie, H. and R. Shillington (2015, May 1). *The Union Card: A Ticket Into Middle Class Stability*. Canadian Centre for Policy Alternatives. <[https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2015/05/Union\\_Card.pdf](https://www.policyalternatives.ca/sites/default/files/uploads/publications/National%20Office/2015/05/Union_Card.pdf)>, as of September 7, 2015.

Mallett, T. (2015, March). *Wage Watch: A Comparison of Public-sector and Private-sector Salaries and Benefits*. Canadian Federation of Independent Business. <<http://www.cfib-fcei.ca/cfib-documents/rr3348.pdf>>, as of September 5, 2015.

Milke, M. (2015, September 7). Labour unions have their place, but not in a monopoly. *The Globe and Mail*. <<http://www.theglobeandmail.com/report-on-business/rob-commentary/labour-unions-have-their-place-but-not-in-a-monopoly/article26240371/>>, as of September 7, 2014.

Milke, M. (2013). *Tax Me I'm Canadian! A taxpayer's guide to your money - and how politicians spend it*. Calgary, Alberta: Thomas & Black Publishers.

Odgers, C. W. and J. R. Betts. Do Unions Reduce Investment? Evidence from Canada. *Industrial and Labor Relations Review*, Vol. 51, No. 1, pp. 18-36. Retrieved September 26, 2015, from JSTOR <<http://www.jstor.org/>>.

OECD (undated). *Trade Union Density*. <[https://stats.oecd.org/Index.aspx?DataSetCode=UN\\_DEN](https://stats.oecd.org/Index.aspx?DataSetCode=UN_DEN)>, as of September 5, 2015.

Sran, G., M. Lynk, J. Clancy, and D. Fudge (2013, March). *Unions Matter: How the Ability of Labour Unions to Reduce Income Inequality and Influence Public Policy has been affected by Regressive Labour Laws*. Canadian Foundation for Labour Rights. <[http://www.labourrights.ca/sites/labourrights.ca/files/documents/cflr\\_unions\\_matter.pdf](http://www.labourrights.ca/sites/labourrights.ca/files/documents/cflr_unions_matter.pdf)>, as of September 7, 2015.