

# Social Europe, EU Employment Legislation and the UK Labour Market

Report of the hearing held on 16th December 2015



LSE Commission on the Future of Britain in Europe

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## Foreword

This is the report of the third Hearing for the LSE Commission on the Future of Britain in Europe focusing on 'Social Europe, EU Employment Legislation & the UK's Labour Market', which took place on Wednesday 16 December 2015 at the LSE. The Hearing was convened by Dr Steve Coulter and Dr Bob Hancké. The convenors are extremely grateful to the 16 participants in the hearing who contributed to a lively and informative debate. A list of their names and organisations can be found in the appendix. We also gratefully acknowledge the help of Pieter Tuytens with preparing and recording the hearing and drawing up the report of the meeting, and Amir Rozlan who provided research backup.

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# 1. Introduction

The EU's involvement in employment policy is controversial for a number of reasons. First, by attempting to impose minimum standards across countries with diverse labour markets it arguably interferes with member states' discretion to regulate these in accordance with national economic models. Second, the policymaking process in Brussels is said by its critics to be opaque and undemocratic, sometimes producing flawed regulation.

Concerns about the effect of EU employment regulation on employers' costs and the operation of the UK labour market had therefore been expected to form a key part of the government's renegotiation of the terms of the UK's membership of the EU. The Conservatives' 2010 election manifesto had pledged to repatriate key powers over employment and social legislation, and the Coalition Agreement signed with its Liberal Democrat allies after the election committed the government to limit the application of the Working Time Directive. However, in the event, these pledges were toned down significantly, with David Cameron's letter to Donald Tusk on 10 November 2015 calling instead for a cut in the total regulatory burden on business alongside a clear commitment to boosting competitiveness.

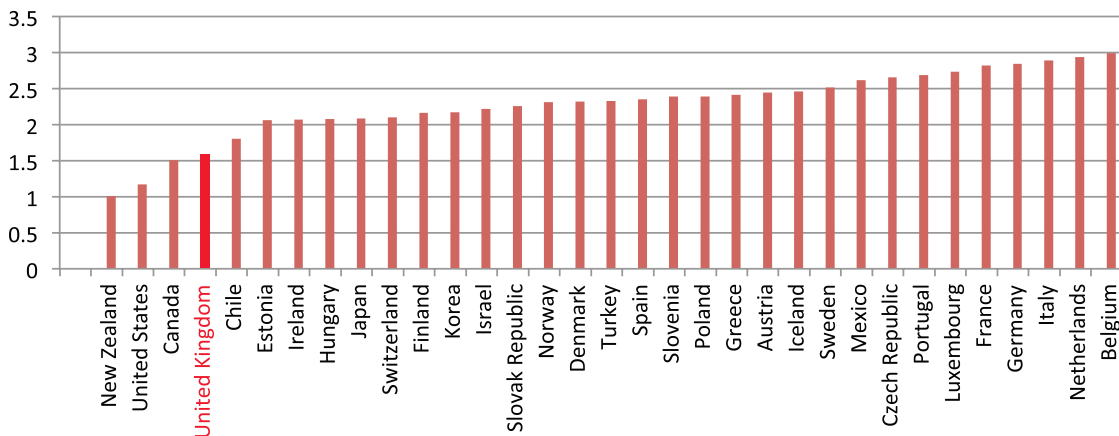
One significant uncertainty concerns what a vote for Brexit would mean for the UK's economic relationships with remaining EU members. Some supporters of Brexit advocate the UK continuing as a member of the European Single Market (ESM). The models for this arrangement would be Norway or Switzerland, which are outside the formal structures of the EU but can continue to sell goods and services to EU members. However, both countries have to continue to adhere to many EU regulations as the price of this access, somewhat undermining the argument for quitting the ESM for this kind of arrangement - at least from the point of view of easing the regulatory burden. The main alternative to the current status quo, therefore, is probably quitting both the EU and ESM in order to focus on developing economic relationships with the rest of the world and allowing the UK government to begin the process of disentangling UK from EU law.

Despite many disagreements over the details and extent of EU influence over employment regulation, most business groups are, however, against Brexit as they believe the costs on them imposed by the EU are outweighed by the benefits of access to the ESM, which account for nearly half of UK trade. Surveys and consultations show continued, albeit qualified, support for UK membership of the EU among the three main employers' organisations, the Confederation of British Industry; the Institute of Directors; and the British Chambers of Commerce. On the other hand, YouGov polling reveals a split in opinion between large, export-oriented firms and Small and Medium Sized Enterprises, which are much more evenly divided on the issue.

Politically, both main parties are divided over Europe, with labour market regulation a key fault line. Pro-Brexit Conservatives have attacked the EU over loss of sovereignty and the impact of Brussels-inspired 'red tape' on business. Both the leading Conservative Brexit

figures, the Justice Secretary Michael Gove and former London Mayor Boris Johnson, have suggested a future for the UK outside the ESM and subject to global trading rules. In his speech on 19th April Gove said this would allow the UK to cut the regulatory burden on the economy.

Although Gove did not single out employment regulation, this prospect alarms trade unions and the Labour Party. Many on the Left, including the Labour leader Jeremy Corbyn and Len McCluskey the head of the UNITE union, are suspicious of the EU in its current form as they believe it prioritises market freedoms at the expense of workers' protection. However, their increasing alarm at prospects of the free-trading, low regulation, vision of the UK's future proffered by many in the Brexit camp have recently encouraged them to side with Remain. Trade unions supporting Remain argue that EU employment directives protect workers from exploitation by unscrupulous employers, and that social partner involvement in the formulation of EU policy increases its legitimacy. Corbyn's EU speech in April warned of a 'bonfire of workers' rights' if the UK left the EU, and most of the large unions have now joined Labour in officially backing Remain.



**Table 1.** Is the UK labour market over-regulated?

Protection of permanent workers against individual and collective dismissals (years 2013-2014). Source: OECD

## 2. Summary

The implications of the Brexit referendum for labour market regulation will obviously depend on the outcome. In the event of a vote to leave the EU, it will hinge on subsequent decisions taken about the UK's future economic relationship with the remaining EU members. These are some of the likely outcomes considered by the Hearing:

- 1) A vote to Remain in the EU would be unlikely to be followed by much renegotiation of EU employment law, since both the motive and opportunity for this would have been removed.
- 2) If the UK voted to leave the EU but negotiated continued access to the European Single Market (ESM), the terms of this access likely to be imposed on the UK would probably include full adherence to EU employment regulations, implying no major change to the regulatory burden.
- 3) If, on the other hand, a post-Brexit UK focused instead on developing global trading relations with emerging markets and the Commonwealth, it would theoretically enjoy more room for manoeuvre over domestic labour market regulation and could shape these in accordance with its desired position within global production chains. However, the reality is that EU employment law is now so deeply embedded in UK case law that disentangling the two would be a very slow and costly process and would not necessarily result in better regulation or a major reduction in the overall

costs of compliance. **Therefore, a Brexit would probably make little difference to the regulatory burden on UK firms, certainly in the short and medium term.**

Other issues:

- The current cost of EU employment regulation to the UK economy is difficult to quantify fairly and accurately, although employers complain that it is a significant burden on them and that much legislation is poorly drafted and subject to further 'gold plating' by the British government.
- Some employers, in addition, argue that the UK's flexible, service-based economy is hampered by employment legislation that imposes steep compliance costs and restricts their ability to react quickly to changing market conditions.
- The net cost-benefit of the effect of EU membership on businesses also varies by size of company and sector, and business (and trade unions) have diverse views on membership of the EU and participation in the ESM. Larger, more export-oriented firms are generally prepared to cope with the accompanying regulations and accept the point of a 'social dimension' to the ESM, yet some smaller firms approach this trade-off differently and find this an unacceptable burden.

- Trade unions are generally pro-EU but have concerns about the future direction of the ESM undermining social standards. Unions argue that complaints about the 'cost' of employment regulation fails to include its beneficial impact, for instance in the areas of Health and Safety and equal treatment of workers.
- In fact, Social Dialogue at EU level over employment matters is not particularly contentious. Both employers and trade unions argue that mechanisms for 'Social Dialogue' between the two at EU level over employment regulation can work well and may even improve regulation in some cases.
- However, there are concerns from employers about the 'activism' of the European Court of Justice and European Parliament which they believe frequently exceeds their remit and contributes to bad policymaking.

### 3. Summary of the Brexit Hearing on Labour Market Regulation:

#### What is the overall impact of EU employment regulations on the UK economy and labour market?

The Hearing began with the views of some of the business groups present. Employers said they were not necessarily against all regulation stemming from Europe. Regulation is not automatically bad, as there are several areas where common rules make sense. Yet in other areas, both EU and British transposed regulation can be burdensome. Polls of businesses tend to show that many find EU employment regulation (including health and safety regulation) unhelpful. The main quoted reasons for this: it costs money; it decreases the willingness to hire; employers are often brought to tribunals which influences hiring decisions. This had most impact on young and marginalised people.

Further issues include the problem of 'gold-plating' – where British politicians use EU regulation as a scapegoat to push through costly regulations which would otherwise be politically unfeasible (e.g. working time). This negatively influences business confidence in EU membership. Furthermore, many members feel that, while they follow the rules, other businesses in the EU do not always do so. Many regulations have a disproportionate impact on small, export-driven companies. They do not have the means to track EU and British regulation, making it difficult to anticipate changes in these (e.g. Working Time Directive).

'One key problem with the EU's 'Social Dimension' is that of a democratic deficit.'

One key problem with the EU's 'Social Dimension' is the democratic deficit. As people are not really involved in voting on EU affairs, this creates a discrepancy between policy making efforts and what people want. In particular, some firms believe the EU fails to deal with the more important issues (such as trade and other outward oriented issues), and spends too much effort on inward-oriented debates.

#### What do businesses think are the main problems with EU employment regulations?

Complaints about regulation were, nevertheless, qualified by the business community's very diverse views; while regulations can be burdensome (especially for small businesses), larger companies do see the point of a social dimension in the single market. Leaving this aside, the issues businesses have tend to be more practical. Much of this has to do with the fact that the EU has become much more diverse since the 2003 enlargement. Three main concerns often emerge with CBI members, for example. First, there is a concern that Brussels is a self-sustained bureaucracy, cut off from the experiences of many of the businesses around Europe. The risk is that consequences for practical implementation are lost from sight during the long process of adapting legislation.



Secondly, there is a problem with implementation of EU Directives in UK legislation. 'Gold-plating', where civil servants add an additional layer of complexity to a regulation, is a very real issue and often happens when ministers feel very constrained in how they design legislation - simply because they wish to avoid a challenge from the European Court of Justice. Thirdly, one has to take into account that things are done differently across countries, creating unequal impact of regulation; and in the UK flexibility is very important.

Transposition of regulation is a significant factor. Businesses often end up in trouble because of technical transgression rather than challenging the spirit of regulations. Especially, regulations translated into common law often have such complicated formulations that it is unsurprising that they end up being challenged. This is not the result of business interference in the legal process, as frequently claimed, but because of the different legal system (common versus civic law).

Another concern is activism within the European Parliament. For example, while most businesses had no problems with the initial formulation of the WTD, several changes were put on the agenda by individual MEPs, despite the costly impact they would have on member states – creating uncertainty for business. One should, however, not expect a big difference, let alone a nirvana where you have far less regulation.

## What are the benefits of EU employment regulation?

The view from the trade unions was that sensible employment regulation does not hinder growth. Instead, it secures growth that is sustainable. Issues which are often presented as costs are not costs per se. For example, benefits for workers such as holidays, breaks, or health and safety provisions should not be considered as a red tape issue, but as important elements of a healthy working environment.

Much of the uncertainty and additional legal activity associated with implementation of EU regulation is the result of poor UK implementation. As UK policymakers try to minimise the impact of EU regulation when transposing and implementing these rules, they add unnecessary complexity and hence legal uncertainty. The business lobby is very successful in pressing for minimising impact (the main origin of gold-plating), yet simpler implementation of EU rules would also benefit businesses by creating less legal confusion.

With respect to the fear of enforcement and employment tribunals, unions argue that this is, in reality, a bogeyman. There are very few workers willing to take their boss to a tribunal (there are hardly any cases of a tribunal resulting from breaching the Agency Worker Directive regulations, for example). The UK has a very basic implementation of many regulations anyway - employers were usually able to sidestep regulation, and it is often very weakly enforced in practice.

It was also pointed out that the UK is already among those countries with the lightest labour market regulation (see Fig. 1), making it hard to see how it would be possible to deregulate further without seriously undermining workers' rights. Furthermore, the OECD has found it difficult to identify a clear overall causal link between the strength of employment protection and unemployment.

The original inspiration for a social dimension was the understanding that economic integration would create tensions in the social sphere (such as firm closures and widespread redundancies). The principle of a social dimension is thus to facilitate change rather than to prevent it; so not to stop job losses, but to allow workers to cope with job loss. Similarly, other values such as free movement aim to create a common floor so workers can be confident that they are treated similarly everywhere. The real problem is that the EU currently lacks a proper social dimension (especially regarding Southern-European countries).

A certain degree of social standards is therefore perhaps necessary to prevent fear of social dumping and thus facilitate opening up the Single Market. And what would be achieved by leaving the EU, other than creating regulatory uncertainty? It is politically inconceivable to repeal existing measures such as health and safety standards or parental leave. In any case, there is no alternative to implementing measures such as the Working Time Directive – as shown by Norway – if you want to remain in the Single Market. The emphasis should be on outcome-focused

regulation where the focus is less on saying what business should do, and more on what should be achieved (as happened, for example, with flexible working).

### **Can the 'cost of EU employment regulation therefore even be quantified sensibly?**

Some calculations estimate that EU social legislation costs the economy many billions of pounds a year. The flaw in these kinds of estimates is that they tend to include as costs things that UK employers would probably do anyway, significantly inflating the potential savings accruing to employers from Brexit. One could therefore question the assumptions behind a simple cost calculation. Equally, one could also point to the benefits which remain uncalculated (e.g. happy workers are productive workers etc.). Equally, however, trade union analyses of the issue tended to gloss over the fact that regulation costs firms money and therefore could destroy jobs. So how to manage this?

The British Chambers of Commerce (BCC) stopped calculating its 'Burden Barometer' in 2009 because focusing on the 'stock' of the burden made increasingly less sense as the number became extremely high. Instead the focus shifted to measuring the impact of the 'flow' of new regulations. Quantification is most useful when looking at individual measures and their potential impact, rather than at existing regulation which is not going anywhere. What is also needed, whether we are talking about measuring benefits or costs,

is a better impact assessment regime at European level (not just British level) and better communication of these impact assessments in member states.

Unions argue that it is very difficult to quantify certain things – for example the costs following from the missed opportunity to include unions and their expertise while designing rules. Hence, lacking Social Dialogue institutions presents the UK with important costs which are not taken into account.

Categorising things as costs or benefits is not a straightforward task – it involves important decisions regarding the kind of society we want. For example, maternity rights can be considered a massive cost by employers, but it can also be considered to be an important societal achievement. Perhaps cost-benefit analysis should in fact be a ‘multi goal exercise’ where you analyse the costs and benefits in respect of each goal, but where the decision regarding the trade-off between these goals is a political rather than an economic decision.

Despite the difficulties, business groups pointed out that some of the worst policy decisions are those taken without a decent assessment based on evidence (especially in labour market policies, these assessments tend to be minimal, with a quick jump towards the conclusion). Hence one should not disregard cost-benefit exercises too quickly.

### **How feasible would it be for the UK to disentangle itself from EU employment law?**

Disentangling the UK from the EU could potentially be very complicated. So would it be worth it? To some extent this depends on assessments about the degree to which the UK economy and labour market really are different from those of other EU countries.

A representative from the legal sector argued that there is no alternative in terms of disentanglement – if you want to have access to the Single Market, then you have to implement the same regulations you would hope to disentangle from. Even Norway has to comply with these, even though it would be much easier for Norway to disentangle its economy than the UK (Norway is wealthy because of immobile natural resources, the UK because of very mobile sectors). If the UK were to decide to exit the ESM nevertheless, this would primarily be a bonanza for lawyers.

If the UK chooses to leave the EU this will likely be immediately followed by new negotiations with the same EU countries for entering the Single Market as a non-EU member. However, the EU member countries will establish their negotiation position in such a way as to communicate to others that leaving the EU is a very bad idea – so one should expect a very hostile attitude to any British demand. The EU would be in serious danger of unravelling if the British leave and are therefore disinclined to encourage others to follow suit by offering attractive terms to the UK post-Brexit.

### **What is the role of Social Dialogue in formulating EU employment regulation, and does this represent a problem for the UK?**

The involvement of both trade unions and employers at the EU level in the formulation of policy ('Social Dialogue') represents a very different tradition from the UK, where governments may on occasion seek the views of either but otherwise retain autonomy in devising policy. Does this create a problem when transposing EU regulations into the UK?

Interestingly, employers at the Hearing were not necessarily against Social Dialogue. One business group said the process is sometimes useful for shaping debates between unions and employers, although achieving comprehensive agreement can be hard on the more technical issues. There are even instances where a lack of Social Dialogue may have contributed to bad policy owing to the Commission's lack of engagement with the real world. On the other hand, others cautioned that the UK's previous experience with Social Dialogue had not been positive; one business representative recalled his experience as Secretary to the National Economic Development Council (1988-1992) and said that unions saw their role on the NEDC as being to argue with Conservative Ministers rather than to debate with their CBI employer social partners

Unions argue that it should be recognised that trade unions are simply part of a wider citizenship. The Social Dialogue has been largely missing in many important EU

discussions (e.g. TTIP, TiSA, SETA). Here it were trade unions, NGOs and citizens who fought hard to get Social Dialogue on the agenda. Still there often is an imbalance, whereby many of the important social clauses welcomed by trade unions are not mandatory to the UK government – so leaving the EU or not will not make much of a difference in those instances. Nevertheless, Social Dialogue remains very useful in the context of debates on parental leave, for example. Social Dialogue offers the opportunity to educate member states who have less progressive views on such matters.

It could also be argued that the missing Social Dialogue in the UK is one explanation for earlier discussed issues such as gold-plating and the legalistic tradition in the UK. Coordination between social partners creates higher levels of confidence, reducing the need for laws and lawyers. In this sense, it is very true that one size does not fit all. This is in fact already the case in Europe – there are many areas where there is no binding EU legislation and no harmonisation (e.g. employment law in Germany is very different from the UK), and this is the way it should be. Making all countries do the same thing would also not be good in terms of 'diversification', which at system level is the best approach to deal with the risk that some policies might turn out to be bad.

### **What would Brexit mean for migrants and the UK labour market?**

A key argument for Brexit is that the UK could thereby regain control of its borders

and restrict migration. What would be the consequences for the labour market?

It was generally agreed that limiting foreign workers would reduce economic growth. Business groups pointed out that labour shortages are already developing. The hospitality industry, for example, depends heavily on workers from outside the UK. Participants in the Hearing pointed to the importance of push factors alongside the discussed pull factors – with the biggest push factor being unemployment in the home country. If the government would like to reduce the number of people coming to the UK then it should try to increase growth and employment in the other countries.

A former senior politician involved in business regulation wondered how changes in unemployment benefits could be made in a way that would be legal. Perhaps one could try to establish an immigration break, but this requires approval from the Commission and it is very difficult to enforce at the frontiers. In the end, he did not expect the government's proposals to make a real difference.

One area of puzzlement was over the fact that public opinion was concerned about the fiscal costs of immigration, even though studies find that non-UK workers contribute more than they take in benefits. So government proposals to restrict benefits would actually undermine fiscal contributions.

### **Is the UK's 'flexible', market-oriented model of capitalism compatible with the more stakeholder-oriented European models? If not, is this an argument for Brexit?**

One argument deployed by those sceptical of UK membership of the EU is that the competitive success of the UK economy hinges on flexibility in wages and employment conditions. Arguably, this is undermined by regulation originating in an EU dominated by countries adhering to the European 'Social Model', which embraces a more regulated, stakeholder-oriented system.

Some participants argued that it is very difficult to talk about an EU 'social model' as de facto diversity is already built into the institutional infrastructure. There are different regimes with different requirements, so it would be impossible to impose homogeneity. Moreover, it is not clear that arguments about a distinctive UK approach lead to a Brexit conclusion. There are good reasons to rethink whether the UK current model is as efficient as it could be. Change to the better is possible – just as the Nordics did not always look like they do now.

We also have to distinguish between the UK as an actual model of capitalism and the 'ideal' liberal market model in its pure form. As an actual model, for example, it is very reliant on foreign direct investment – the vast majority of which is attracted to the UK by our place in the ESM - and it is also reliant on importing skilled workers from elsewhere in Europe. If the UK wants to leave, it might

'...differences between the European and British social models should not be exaggerated, and are in any case no basis for a vote for or against Brexit.'

have no choice but to become fully flexible. As this would imply becoming even more a 'playground for the very rich', this is not what most politicians want.

A former senior Minister recalls that during his time in government, there was a peaceful coexistence with the European social model. The only two controversies were the Agency Workers Directive and the Working Time Directive – yet as the UK has opt-outs for both it was not really a deal buster. Therefore, differences between the European social model and the British social model should not be exaggerated, and are in any case no basis for a vote for or against Brexit.

Trade union representatives, in fact, contend that Social Europe hardly exists due to the lack of a real social underpinning to the EU's economic model. Additionally, what matters is the lack of global social underpinning - Europe is increasingly less able to introduce social elements into global treaties.

It might therefore seem strange to propose to leave the EU just as the EU seems to be liberalising and moving towards the position of the UK. This is especially visible in the Southern-European countries which are pressured to become more like the

UK, not less. Furthermore, it could be argued that the UK is massively freeriding on the skill production in other European countries. They train people and we take them in without many restrictions – why object to this?

The Brexit question also needs to be put in the context of the global economy. Most companies in goods markets depend on a complex global value chain. So what matters is how the UK is integrated in the European economic area. If the EU is not the area on which economic decisions depend, then a Brexit might not be a completely crazy idea; however, if the EU is very important in the supply chain of British firms, then Brexit could be a major factor in location with negative consequences.

Others point out that an overly simple depiction of the UK itself as permanently deregulating is not correct. One expert involved in government points to five areas where the British labour market is more regulated than it was five years ago: shared parental leave, expanded flexible working rights, public contracts, stakeholder pensions, and the apprenticeship levy. These are clearly movements in the opposite direction to the standard liberal British stereotype. Much 'home-grown' regulation is, for example, aimed at reducing the binary choice between working and caring, and is therefore likely to be extremely popular. Also, many of these regulations involve passing the costs of social goals to employers, representing a subtle shift in the UK model.

## 4. Conclusions/Policy Implications:

- Brexit might have profound long-term implications for the structure and orientation of the UK economy, and could eventually afford the government more autonomy to shape the organisation and regulation of the UK economy and labour market. However, the potentially 'liberating' effect of quitting the EU should not be overestimated, particularly in the short to medium term.
- This is not necessarily an argument for the status quo, however. Most participants at the Hearing agreed that there are significant flaws in the way employment and other policies are made in the EU. In the event of Remain, the UK government should push for a less intrusive and more context-sensitive approach on the part of the EU towards formulating labour market policy.
- In particular, EU employment policy should take more account of national differences. The structure of the UK economy and labour market is sufficiently different from that of many Continental economies to warrant concerns about moves towards further harmonisation of employment standards. In the UK flexibility and orientation towards service sectors are distinctive features of the economy which may be undermined by obtrusive moves to enforce common standards with other countries with different labour markets. This should not be exaggerated as a factor, however, and is not a reason to vote for or against Brexit.

## Participants List

First	Surname	Title
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Andrea	Broughton	Principal Research Fellow, Institute for Employment Studies
Sir Vince	Cable	Liberal Democrats; former Secretary of State for Business, Innovation and Skills
Neil	Carberry	Director for Employment and Skills, Confederation of British Industry (CBI)
David	Coats	Research Fellow, The Smith Institute; former Head of Social Affairs, TUC
Martin	Couchman	Deputy Chief Executive, British Hospitality Association
Saul	Estrin	Professor of Management & Head of the Department of Management, LSE
Jonathan	Hopkin	Associate Professor of Comparative Politics, Department of Government, LSE
Sampson	Low	Head of Policy, Unison
Adam	Marshall	Director of Policy and External Affairs, British Chambers of Commerce (BCC)
Michael	Martins	Economics Analyst, Institute of Directors (IoD)
Jeff	Masters	Policy Adviser
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