

**Hayek on Labour Unions**  
by  
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*It is probably... impossible in our time for a student to be a true friend of labour and to have the reputation of being one (Hayek [1959] 1967, p. 294).*

**Introduction**

As this epigraph implies, unions have a much better reputation than they deserve. Even today (2004) a majority of the general public thinks that labour unions are the best friend that any working man or woman could have. That is simply wrong, and in his writings on unions, from *Monetary Nationalism and International Stability* ([1937] 1972, pp. 21-2) wherein he first noted the inflationary dangers of collective bargaining, through *1980s Unemployment and the Unions* (1980), which Arthur Seldon characterized as the summation of Hayek's teaching on unions ([1980] 1984, p. 9), Hayek explained why. He argued that while unions benefited some workers it was always at the expense of other workers and that as a whole, unions have made workers significantly worse off than they would otherwise have been. Moreover, he saw unions as they were (and, in large measure, as they still are) in Britain and the US as major threats to the free economy as well as the free society in general. He endorsed voluntary unionism on grounds of freedom of association properly understood, but he saw actual unions in both countries as wholly involuntary organizations to which politicians had granted both immunity from the ordinary rule of law and power to wield coercive authority mainly against workers who preferred to be union free. The malign consequences of coercive unionism examined by Hayek fall into two broad categories: effects on the economy and conflicts with the rule of law. In both, Hayek saw immense problems which could only be solved by major reforms of public policy.<sup>1</sup>

In what follows I will first discuss what Hayek meant by “coercive” unionism and what he saw as the sources of the unions’ coercive powers in Britain and the US. Some rule-of-law issues will be addressed here. Next, in turn, I will consider his views on voluntary unions, the economic consequences of coercive unionism, and the threats of coercive unionism to the free society and the market economy. Then I will cover Hayek’s views on coercive unionism and the rule of law as it relates to freedom of association, freedom of contract, and strikes and picketing. I will follow with a discussion of his views on profit sharing as an alternative to collective bargaining and on codetermination or industrial democracy. I will close by commenting on the extent to which the situation has changed since 1980.

### **Coercive Unionism**

In *The Constitution of Liberty* (1960) Hayek outlined his views concerning the proper scope of government. He argued that the principle function of a just government is to provide the protective services of the classical night watchman state. Later, in *Law, Legislation and Liberty I* (1973) he characterized these protective services as those necessary to enforce the “rules of just conduct” among people. I have characterized these rules of just conduct as the rules of voluntary exchange (Baird 1995). These rules are general (applicable to all situations) and abstract (not designed to accomplish specific purposes). They set the environment within which people remain free to pursue their own purposes. To enforce such rules government must have some coercive power. According to Hayek, coercion is evil, but some coercion, exercised exclusively by government for the sole purpose of preventing people from trespassing against each other, is necessary.

In addition to limited government, Hayek's view of the rule of law requires that government apply and enforce the rules of just conduct uniformly over all people and to itself. People wielding governmental authority may grant no special privileges to, and impose no special burdens on, anyone. Equality before the law, what Hayek called *isonomia*, is the *sine qua non* of the rule of law (1960, Part II). Moreover, the private use of coercive force, except in self defense, is always contrary to the rule of law.

Now, unions are not governments. They are private organizations of private individuals. They should never be able to deal with any people except on the basis of voluntary exchange. Yet, in Britain and the US politicians have granted unions the unique privilege of using coercion to get what they want.

Public policy concerning labor unions has, in little more than a century, moved from one extreme to the other. From a state in which little the unions could do was legal if they were not prohibited altogether, we now have reached a state where they have become uniquely privileged institutions to which the general rules of law do not apply. They have become the only important instance in which governments signally fail in their prime function – the prevention of coercion and violence (1960, p. 267).<sup>2</sup>

What sort of coercion and violence did Hayek have in mind?

The unions cannot achieve their principal aims unless they obtain complete control of the supply of the type of labor with which they are concerned; and, since it is not in the interest of all workers to submit to such control, some of them must be induced to act against their own interest....

It is the techniques of coercion that unions have developed for the purpose of making membership in effect compulsory, what they call their ‘organizational activities’ (or, in the United States, ‘union security’ – a curious euphemism) that give them the real power (ibid., pp. 273-4).

In Britain if a union, through strikes and threats of strikes, could get employers of a particular kind of labor to agree not to hire any union-free workers, the instrument of coercion would be to present recalcitrant workers with a “choice”: join up or don’t work. In the US the same sort of coercive choice was imposed through the “union security” provisions of the National Labor Relations Act (1935). In 1947 that Act was amended, and subsequent decisions of the US Supreme Court reduced compulsory union membership to the compulsory payment of union dues. It remains true in the US that unions can coerce workers to support them as a condition of continued employment.

However, unions do not stop there. Sometimes individual workers who wish to become or remain union-free are threatened with beatings and worse. Sometimes the threats become reality. Sometimes the families of recalcitrant workers are also victims of threats and attacks.<sup>3</sup> And all of this has been considered proper. How could this be?

All this has become possible because in the field of labour relations it has come to be accepted belief that the ends justify the means, and that, because of the public approval of the aims of union effort, they ought to be exempted from the ordinary rules of law. The whole modern development of unionism has been made possible mainly by the fact that public policy was guided by the belief that it was in the public interest that labour should be as comprehensively and completely

organized as possible, and that in the pursuit of this aim the unions should be as little restricted as possible ([1959], 1967, p. 281).

Muddled thinking and widespread belief in the “myth” that unions have benefited the working class and that those benefits would vanish in the absence of unions, leads public opinion to several false conclusions.

[T]he fact that it is a natural aim of the unions to induce all workers to join them has been so interpreted as to mean that the unions ought to be entitled to do whatever seems necessary to achieve this aim. Similarly, the fact that it is legitimate for unions to try to secure higher wages has been interpreted to mean that they must be allowed to do whatever seems necessary to succeed in their effort. In particular, because striking has been accepted as a legitimate weapon of unions, it has come to be believed that they must be allowed to do whatever seems necessary to make a strike successful. In general, the legalization of unions has come to mean that whatever methods they regard as indispensable for their purposes are also to be considered legal (1960, p. 274).

This unthinking support of labour unions is based on confused notions of social justice.

The struggle for the recovery of Britain may mean a struggle against those long regarded as the ‘good’ people, whose ‘social conscience’ led them to try to impose some ideal design on the distribution of incomes. These are the politicians in all parties, in the trade unions, supported by well meaning, but muddled people in high places ([1980], 1984, p. 47).

The principal source of the coercive powers enjoyed by British unions was the 1906 Trades Dispute Act which, unlike US legislation in the 1930s, didn't actually grant any coercive powers. Instead the 1906 act simply immunized labor unions and labor union leaders from any prosecution for acts of coercion and violence. This may sound a bit exaggerated, but it is not. Even Sidney and Beatrice Webb, staunch supporters of British unions in the late 19<sup>th</sup> and early 20<sup>th</sup> centuries regarded the Trade Disputes Act as "nothing less than monstrous" (Hanson 1984, p.70). As Hayek pointed out in 1960 (p. 268) and Hanson repeated in 1984 (p. 70), A. V. Dicey , the renown British constitutional lawyer, condemned the 1906 law for having made "a trade union a privileged body exempted from the ordinary law of the land" (ibid., pp. 69-70). From 1906 until the Thatcher reforms of the 1980s (despite a feckless attempt by the Heath government in 1971 to make some changes) unions could, with impunity, use threats of force and violence and actual force and violence against employees and employers as well as customers and suppliers of strike targets to achieve whatever they wanted as long as it was in the context of a labour dispute.

Hayek cites the sources of American unions' coercive powers as the Clayton Act of 1914, and the Norris LaGuardia Act of 1932 together with the Supreme Court decision in *Hunt v. Crumboch* (325 US 821 [1945]). Curiously he failed to cite the most important piece of legislation in this regard: the National Labor Relations Act of 1935 as amended in 1947 (Hayek 1960, p. 268). The Clayton Act was an attempt by Congress to make unions exempt from antitrust laws. It didn't work because the 1921 Supreme Court decision in *Duplex Printing v. Deering* (254 US 443) prevented the exemption from applying to most union activities. The Norris LaGuardia Act overrode the *Duplex*

decision as far as antitrust was concerned. In addition it made it impossible for federal courts to grant injunctions against any sort of union activities in labour disputes, authorized mass picketing, even by non-employees, during strikes, and made union-free agreements between workers and employers unenforceable (Baird, 1995, Section III). *Hunt v. Crumboch* was an especially egregious Supreme Court decision wherein the Court granted union leaders the privilege of driving an employer out of business simply because they did not like the employer (Baird 2000, Section III).

The National Labor Relations Act (NLRA), was and is the principal legislative source of union exemptions from the rule of law in the US. Its doctrines of exclusive representation and mandatory good faith bargaining are the main culprits. Union security, which as we saw above was cited by Hayek, really derives from exclusive representation. Briefly, exclusive representation is the provision in the NLRA that prohibits individual workers from deciding whether they will or will not be represented by a union. Instead, the question is decided by majority vote. A union that is certified by such a vote represents all workers who were eligible to vote. Workers who voted against the union as well as workers who didn't vote must accept the representation "services" of the winning union. Individuals are forbidden to represent themselves. Moreover, once a union is certified it is presumed to have majority support indefinitely. There are no regularly scheduled future elections wherein workers can reconsider the issue. For example, the United Auto Workers union is the exclusive bargaining agent for all American General Motors assembly line workers even though all of the workers who voted for the union back in the 1930s and 1940s are now dead or retired. Current workers never got a chance to vote.

Although Hayek did not explicitly discuss exclusive representation in American unionism, he clearly condemned the principle twice in *The Constitution of Liberty*.

Legislation has frequently gone so far as to require not only that that a contract concluded by the representatives of the majority of the workers of a plant or industry be available to any worker who wishes to take advantage of it, but that it apply to all employees, even if they should individually wish to be able to obtain a different combination of advantages (1960, p. 275).

Later, while discussing how to constrain union coercion he wrote:

It would be necessary ... to rescind all legal provisions which make contracts concluded with the representatives of the majority of workers of a plant or industry binding on all employees and to deprive all organized groups of any right of concluding contracts binding on men who have not voluntarily [as individuals] delegated this authority to them (ibid., p. 278).

Mandatory good faith bargaining forces employers to bargain with certified unions on matters of wages and salaries and other terms and conditions of employment. The only sure defense an employer has against a charge of failure to bargain in good faith with a union is an unambiguous record of making compromises during the bargaining process. In Britain a union could force an employer to give into union demands by threats and acts of violence. In America, the law itself explicitly forces employers to give in. For example, union security is a mandatory subject of bargaining. The law compels employers to bargain with certified unions on whether workers who are not union



members, but who, under exclusive representation, are represented by those unions, shall be forced to join the union or at least pay union dues.

Hayek never discussed mandatory good faith bargaining. Perhaps he was unaware of this feature of American law. In any case the idea is completely foreign to Hayek's conception of the rule of law. Under the common law of contracts, if any party to a contract were forced to bargain and forced to make concessions, the contract would be null and void. To be legitimate a contract must emerge from a process of voluntary exchange. This is one example of what Edwin Vieira, an American labour lawyer, calls "the apartheid of [American] labor law" (1986, p. 35).

To perfect the exemption of American unions from the rule of law, the Supreme Court in *United States v. Enmons* (410 US 396 [1973]) exempted unions and their leaders from federal prosecution for any threats or acts of violence and coercion as long as the threats and acts were committed in the context of a labour dispute wherein unions were seeking "legitimate union objectives" such as higher wages and collective bargaining contracts. In so doing the Court enacted its own Trades Disputes Act.

### **Voluntary Unionism**

Hayek begins his discussion of the legitimate functions of unions in *The Constitution of Liberty* (1960) with a rather startling statement:

It can hardly be denied that raising wages by the use of coercion is today the main aim of unions. Even if this were their sole aim, legal prohibition of unions would however, not be justifiable. In a free society much that is undesirable has to be tolerated if it cannot be prevented without discriminatory legislation (1960, p. 275).

The problem with unions, then, is not what they try to do even when those efforts are coercive. The problem, Hayek suggests, is that the unions are not subject to the rule of law. Their coercive acts go unpunished. In a free society that which is undesirable must be dealt with by a consistent application of the rules of just conduct and punishment of those who break those rules. No special, discriminatory legislation is justified.

Hayek then opines, “as truly voluntary and non-coercive organizations, [unions] may have important services to render. It is in fact more than probable that unions will fully develop their potential usefulness only after they have been diverted from their present antisocial aims by an effective prevention of the use of coercion” (ibid., p. 276). This is in keeping with Hayek’s view of the competitive market process as a “discovery procedure” ([1968] 1978). No one can know what activities voluntary and peaceful unions might discover to be beneficial to their voluntary members and others. Unions have never had to embark on that journey of discovery.

Nevertheless, Hayek suggests some broad types of possibly useful activities for voluntary unions. Among these are a role in the discovery of preferred mixes of direct wages and fringe benefits in compensations packages, and discovery of majority opinion concerning “the differentials between the remuneration for different jobs and the rules for promotion” (1960, p. 276). He also guesses that unions may be useful in setting up rules concerning “self-government” among employees (ibid., p. 277). Then he says, “There is ... the oldest and most beneficial activity of the unions, in which as ‘friendly societies’ they undertake to assist members in providing against the peculiar risks of their trade” (ibid.). I have doubts regarding his first three conjectures, and I join him in the fourth. But that is not the point. Anyone can make a list. Only the market can reveal

outcomes. Part V of the 1984 edition of *1980s Unemployment and the Unions* consists of an edited version of an article Hayek wrote in October 1978 for *The Times*. In that article he reiterated his 1960 conjecture that voluntary, peaceful unions would have useful things to do. Here they are limited to activities “with respect to the internal organizations of enterprises – questions on which the arrangements of large organizations depend ([1978] 1984, p. 61). This suggestion is no more helpful than his earlier ones.

My expectation is that whatever useful functions would be discovered for peaceful, voluntary unions they would be carried out at the level of the individual firm, not whole industries, much less for the entire economy. Hayek was not so sure. He said, “We shall leave the question open, however, as to whether any of the above arguments justify unions of a larger scale than that of the plant or corporation” (1960, 277). I find this curious because, as we will see below, Hayek favored the application of antitrust laws to unions. If antitrust laws are used to prohibit two or more firms from colluding together, consistent application of the laws would also prohibit the employees of two or more firms from colluding together. My position is that antitrust law ought not be applied to either firms or unions (Baird, 2000).

Before his discussion of the legitimate functions of voluntary unions Hayek noted that such unions could not aspire to raise wages above market levels.

[S]trictly voluntary unions, because their wage policy would not be in the interest of all workers, could not receive the support of all. Unions that had no power to coerce outsiders would thus not be strong enough to force up wages above the level at which all seeking work could be employed, that is, the level that would establish itself in a truly free market for labor in general (1960, pp. 270-1).

The only way any union can enforce an above-market wage is to exclude union-free workers from employment at the high wage. To do that, the unions must have coercive power. Truly voluntary unions, working within the rule of law, would have no such power. No union-free workers would consent to be shut out of high wage employment, and their competition with unionized workers would lower the wage to the market level.

Hayek was even more forthright in his endorsement of voluntary unionism in his *1980s Unemployment and the Unions*.

I do not, of course, deny the trade unions their historical merits or question their right to exist as voluntary organizations. Indeed, I believe that everybody, unless he has voluntarily renounced it, ought to have the right to join a trade union. But neither ought anyone to have the right to force others to do so ([1980] 1984, p. 51).

The phrase “unless he has voluntarily renounced it” raises another question. In America prior to the Norris LaGuardia Act (1932) it was legal for an employer to include a union-free (unionists called them “yellow dog”) provision in his offer of employment. Any worker who accepted such an offer of employment would thereby consent to abstain from any sort of union activity. As I have argued elsewhere, such agreements are perfectly consistent with the doctrine of freedom of contract (1995). I infer from the quote above that Hayek would agree with me. However, in *The Constitution of Liberty* Hayek unequivocally condemned the “yellow dog contracts” as an agreements in restraint of trade (1960, p. 278). I will return to this issue below. Here I simply point out that Hayek must have changed his mind on this issue by 1980.

## **Economic Consequences of Coercive Unionism**

The malign economic effects of coercive unionism examined by Hayek fall into four broad categories: unions disrupt and impair the coordination of economic activities through the competitive market process; they increase the extent and duration of unemployment; they cause inflation and exacerbate the business cycle; and they lower productivity which results in lower standards of living for working people.

### **Discoordination of Economic Activities**

Part II of *1980s Unemployment and the Unions*, is a clear and persuasive exposition of Hayek's long-held understanding of how markets achieve coordination of the diverse economic activities of all market participants without any central direction. Relative prices and relative wages, and their profit and loss implications, are central to that coordination process. In brief, within the context of voluntary exchange, all market participants attempt to do the best they can for themselves. They formulate production and exchange plans on the basis of the bid and ask prices they expect to encounter in the market. Each person formulates his own bid prices for those goods and services (including labour) he is interested in buying and his own ask prices for those goods and services (including labour) he is interested in selling. Each person also has expectations regarding the bid and ask prices of other market participants. As people attempt to carry out their plans they will discover the extent to which their expectations and planned actions are consistent with what others are willing to do. Buyers who expected to encounter lower ask prices than they do, will decide to buy less than they had planned. Buyers who expected to encounter higher ask prices than they do, will decide to try to buy more than they had planned. Sellers who expected to encounter higher bid prices

than they do will decide to sell less. Sellers who expected to encounter lower bid prices than they do will decide to try to sell more. All the while, market participants will adjust their own bid and ask prices to make them more consistent with newly discovered production and exchange opportunities. Gradually, as expectations come to correspond to reality, more and more coordination of production and exchange activities is achieved. Since market conditions are almost always changing, coordination is a moving target. Nevertheless, freely determined prices and wages move markets toward coordination, a state where the plans and actions of all market participants are mutually consistent. Note that no one has to have knowledge of the underlying reasons other market participants do what they do. All that is necessary is that prices are free to convey the implications of those actions.

In Hayek's words:

Each individual can rarely know the conditions which makes it desirable, for him as well as for others, to do one thing rather than another, or to do it in one way or another. *It is only through the prices he finds in the market that he can learn what to do and how.* Only they, constantly and unmistakably, can inform him what goods and services he ought to produce in his own interest as well as the general interest of his community or country as a whole. The 'signal' which warns him that he must alter the direction or nature of his effort is frequently the discovery that he can no longer sell the fruits of his effort at prices which leave a surplus over costs. The signaling apparatus works as much for the employed worker as for the professional or business man. ...

For anyone earning his living in the market, which means most of us, the most valuable contribution he can make at any time will depend on thousands of continually changing conditions of which he can have no direct knowledge. It is nevertheless possible for him to make whatever decisions are most advantageous both to himself and the community at large because the open market conveys to him, through its prices, the information he requires to make the right decisions and choices. The prices are thus the indispensable signals that communicate to him the effects of events with which he cannot himself be directly acquainted ([1980] 1984, pp. 28-29, emphasis in original).

Coercive unionism cripples this coordination process. Specifically when above-market wage rates are imposed in unionized employments by the ability of unions, through coercion, to shut out competing workers, those wages will not tell the truth about the relative scarcity of workers who can do the job. Too few workers will enter those employments. Instead, many workers who should be employed therein, based on what they can do and the willingness of consumers to pay employers to hire them to do it, will be diverted to lower valued uses of their abilities. This will depress wages in those employments again resulting in prices that do not send the right signals to market participants. Relative wages and relative prices will be distorted. They will tend to discoordinate the economy rather than coordinate it. Hear Hayek on union-caused discoordination in Britain when it was considered the “sick man of Europe.”

The effect of the present system of wage determination in Britain is that the country no longer has an internal price structure to guide the economic use of

resources. This is almost entirely due to the rigidity of politically determined wages. If it is no longer possible to know the most efficient use of the natural talents of the British people, it is because relative wages no longer reflect the relative scarcity of skills. Even their relative scarcity is no longer determined by objective facts about the real conditions of supply and demand, but by an artificial product of the arbitrary decisions of legally tolerated [labour] monopolies (ibid., p. 54).

### *Unemployment*

Hayek held that unemployment is always a pricing problem. It emerges when “there is a discrepancy between the distribution of labour (and the other factors of production) between industries (and localities) and the distribution of demand among their products” (1975, p. 19). Given the pattern of consumer demands for goods and services, suppose there is an excess demand for labour where consumer demand for goods and services is strong and an excess supply of labour where consumer demand is not so strong. Ordinarily this would result in higher wages in the former and lower wages in the latter. This pattern of relative wages would attract additional workers into the production of goods and services for which consumer demand is strong and induce some workers employed where consumer demand is less strong to leave those employments. The additional supply of workers seeking employment in the former will tend to lower wages there. The decrease supply of labour in the latter will tend to increase wages there. The process continues until all labour is employed in accordance with the pattern of consumer demands. Higher consumer demand becomes translated into additional production, and lower consumer demand becomes translated into less production. Any discrepancy



between the allocation of labor among employments and the pattern of consumer demands is gradually remedied by changing relative prices and wages.

The only way such a discrepancy can endure is if there is a “distortion of the system of *relative* prices and wages” (ibid., emphasis in original). To the extent that the markets in which there is an excess demand for labor are unionized, additional workers are prevented from seeking employment there. The high wages become permanent. Thus the high consumer demand is absorbed by the high wages rather than translated into additional production. If the markets in which there is an excess supply for labour are also unionized, the initial wage decrease will be prevented so employers have no recourse but to lay off workers. Result: durable unemployment. If the markets with excess supply of labour are not unionized unemployment there can be avoided, but only by a substantial decline in wages. If declines of that magnitude are illegal because of minimum wage laws, or, if because of the welfare state, people would be paid more not to work than to work at such low wages, the result again is durable unemployment. Unions always support increases of legal minimum wages and higher unemployment benefits.

In Hayek’s words:

The normal cause of recurrent waves of widespread unemployment is ... a discrepancy between the way in which demand is distributed between products and services, and the proportions in which resources are devoted to producing them. Unemployment is the result of divergent changes in the direction of demand and the techniques of production. If labour is not deployed according to demand for products, there is unemployment ([1980] 1984, p. 55).

It is the continuous change of *relative* market prices and particularly wages which can alone bring about that steady adjustment of the proportions of the different efforts to the distribution of demand, and thus a steady flow of the stream of products. It is this incessant adaptation of relative wages to the ever-changing magnitudes, at which in each sector demand will equal supply, which the trade unions have set out to inhibit (*ibid.*, p. 18, emphasis in original).

The reason why I believe that the licence to use coercion conceded to unions some 70 years ago [in the Trade Disputes Act] should be withdrawn is precisely that their actions have become the chief cause of unemployment. [One way they do this] is the obvious one of an increased demand for some product being absorbed by an increase of the wages of the workers already employed in it rather than by an influx of additional workers, leaving out in the cold those in the industries from which demand has turned ([1978] 1984, p. 62).

The chief significance of the comprehensive systems of unemployment compensation ... is that they operate in a labor market dominated by the coercive action of unions and that they have been designed under strong union influence with the aim of assisting unions in their wage policies. ... Such a system, which relieves the unions of the responsibility for the unemployment that their policies create and which places on the state the burden not merely of maintaining but of keeping content those who are kept out of jobs by them, can in the long run only make the employment problem more acute (1960, p. 302).

Hayek acknowledged another way in which union-imposed wage distortions cause unemployment. Excessive wage rates imposed by union duress will cause

employers to change the capital-labour mix in ways that permit them to reduce labour costs while maintaining output. “At wages higher than those which would prevail in a free market, employers must, in order to be able to pay them, use the limited amount of capital that is available in a manner which will require fewer workers for a given output” ([1978], 1984, p. 62).

### *Unions, Money, Inflation and Keynes*

Hayek often cited a perverse de facto division of responsibility between monetary authorities and trade unions in Britain. The unions would arbitrarily set high money wage rates in key industries, and, because by itself this would result in extensive unemployment, the monetary authorities would inflate the money supply enough to raise money prices which in turn would lower real wages sufficiently to avoid the extensive unemployment.

What we have achieved is a division of responsibilities under which one group can enforce a wage level without regard to the effects on employment, and another agency is responsible for providing whatever amount of money is needed to secure full employment at that wage level. So long as this is the accepted principle, it is true that the monetary authorities have no choice but to pursue a policy resulting in continuous inflation, however little they may like it. But the fact that in the existing state of opinion [the sanctity of unions] they cannot do anything else does not alter the fact that, as always, it is monetary policy and nothing else which is the cause of inflation ([1959] 1967, p. 282).

The US also experienced this phenomenon on a limited scale, especially in the 1970s, but unions here were much less pervasive than in Britain so it was much less of a problem. Nevertheless we had our own discussions of the extent to which this “cost-push” process could account for US inflation. Most US economists concurred with Hayek (and Friedman) that cost-push could not account for inflation in the absence of ratifying monetary policy.

Keynesian economics, of course, only strengthened the link between unions and the monetary authorities in causing inflation. Keynes always understood that unemployment was a result of real wages that were too high, but he simply assumed that money wages could not be reduced because of unions and other causes of wage “rigidities.” His solution to the problem of unemployment was to increase aggregate money demand through expansionary monetary policy. Of course, this “solution” is possible only to the extent that workers underestimate the resulting inflation.

The essential point is that it must be once more realized that the employment problem is a wage problem and the Keynesian device of lowering real wages by reducing the value of money when wages have become too high for full employment will work only so long as the workers let themselves be deceived by it. It was an attempt to get round what is called the ‘rigidity’ of wages which could work for a time but which in the long run has only made this obstacle to a stable monetary system greater than it had been. What is needed is that the responsibility for a wage level which is compatible with a high and stable level of employment should again be squarely placed where it belongs: with the trade unions ([1958] 1967, p. 298).

The final disaster we owe mainly to Lord Keynes. His erroneous conception that employment could be directly controlled by regulating aggregate demand through monetary policy shifted responsibility for employment from the trade unions to the government. This error relieved trade unions of the responsibility to adjust their wage demands so as to sell as much work as possible, and misrepresented full employment entirely as a function of government monetary policy. For 40 years it has thus made the price mechanism ineffective in the labour market by preventing wages from acting as a signal to workers and to employers. As a result there is divided responsibility: the trade unions are allowed to enforce their wage demands without regard to the effect on employment, and government is expected to create the demand at which the available supply of work can be sold at the prevailing (or even higher) wages. Inevitably the consequence is continuous and accelerating inflation ([1980] 1984, p. 57).<sup>4</sup>

However, Hayek did not recommend that this “disaster” be remedied by restrictive monetary policies. He thought such an effort would be far too dangerous: “A monetary policy that would break the coercive powers of the unions by producing extensive and protracted unemployment must be excluded, for it would be politically and socially fatal” (1960, pp. 281-2). The only solution, according to Hayek, is to remove the unions’ privileges, to subject them to the rule of law. This would be difficult, but the unions would come to see that it is the least bad of their alternatives.

[I]f we do not succeed in time in curbing union power at its source, the unions will soon be faced with a demand for measures that will be much more distasteful

to the individual workers, if not the union leaders, than the submission of unions to the rule of law: the clamor will soon be either for the fixing of wages by government or for the complete abolition of the unions (ibid., p. 282).

Of course Hayek would be opposed to either government wage setting or the complete abolition of (voluntary) unions. However, I think Hayek was, at least in 1960 when he wrote these words, too optimistic about the unions' distaste for government wage fixing. American, if not British, unions supported government interference in the 1970s through "incomes policies" and explicit wage fixing. During that period of time the unions had a lot of confidence in their ability to manipulate public policy in their interests. And the complete abolition of (coercive) unions was not then, and is not now, politically possible.

Hayek thought that Keynes' notion of "aggregate demand" was meaningless but dangerous. Thinking in such aggregate terms diverts attention away from what, as we saw above, was, in Hayek's mind, really important: the distribution of individual demands relative to individual supplies and relative prices.

If the composition (or distribution) of the demand for the various products is very different from that of their supply, no magnitude of total demand will assure that the market is cleared. The wider the difference between the composition of the demand and that of the supply, the more the achievement of a correspondence between the whole of demand and the whole of supply can be brought about *only* by a change in the relative quantities, *and* this, in turn, only by a change in the relative prices of the different products and services, including wages ([1980 1984, p. 16 emphasis in original).<sup>5</sup>

Moreover, trade unions exacerbate the difficulty.

Aggregate demand may well exceed the aggregate price of all goods and services offered, yet this will not create full employment if in the sectors in which demand exceeds supply the already employed obstruct the entry of additional workers by claiming all the surplus as gains for themselves (ibid., p. 17).

Finally, Hayek joined his critique of unionism with his monetary theory of the business cycle.<sup>6</sup> As discussed elsewhere in this volume, the basis for that theory is the role of relative prices (including wages) and interest rates in the coordination of economic activities. The introduction of newly created money and bank credit distorts relative prices sending incorrect signals to market participants who then misallocate resources. The new money does not change the underlying real supplies and demands, but makes it appear that some supplies and demands have changed. In particular, lower interest rates send the false signal that people want to consume less now and more in the future. In response, producers produce less for current consumption and instead undertake too many investments designed to yield consumer goods in the future. In the meantime real demand for consumer goods doesn't decrease, and the spending boom part of the cycle gets underway. Eventually, unless money inflation is accelerated to keep ahead of expectations, real supply and demand conditions will become revealed, and a correction of the misdirections of resources will get underway. This is the bust part of the cycle.

What role do unions play in this story? When discussing unions Hayek emphasized that wages are distorted by inflation and so they will misdirect labour. When

monetary authorities resort to inflation in order to avoid unemployment, the new money increases particular wage rates. “The artificial demand brought about by increasing the amount of money is simply misleading: it attracts workers into employments which cannot be maintained except by accelerating inflation” ([1980] 1984, p. 21). Moreover, after Hayek had developed his trade cycle theory and had turned his attention to the union problem he came to see that unions were the principal influence leading monetary authorities to inflate.

[T]he most common cause [of unemployment] is that, because of excessive credit expansion, over-investment has been encouraged and too many resources have been drawn into the production of capital goods, where they can be employed only so long as the expansion continues or even accelerates. And credit is expanded to appease trade unions that fear their members will lose their jobs, even though it is they themselves who forced wages too high to enable the workers to find jobs at those excessive rates of pay (ibid., pp. 55-6).

### ***Lower Productivity and Lower Standards of Living***

According to Hayek, “It is a complete inversion of the truth to represent unions as improving the prospect of employment at high wages. They have become in Britain the chief cause of unemployment and the falling standard of living of the working class” ([1978] 1984, p. 62). Misallocation of labour due to the unions’ interference with the signaling functions of relative prices and wages reduces the productivity of the workforce by preventing labour from being allocated according to its most highly valued uses. Many



workers are excluded from where they would be most productive and forced into employments where they are less productive, or they are excluded from any employment.

It is the wages maintained by the closed shops whose barriers prevented the rest from earning as much as they might have done which keeps the productivity of the majority of British workers low. Once the opportunity to earn more in a particular trade becomes the exclusive property of those already employed there, successes of individual enterprises are likely to be taken out by its present staff in the form of higher wages rather than leading to additional employment ([1980] 1984, p. 19).

Britain has been brought to her present plight, not because of the lack of skill or industry of the individual worker, but because government and labour organizations, in order to appease groups of workers, have tried to relieve them of the necessity for adjustments by removing the inducements (and rewards) of changing their jobs (ibid, p. 35).

High productivity in an economy requires that individual decisionmakers within their respective enterprises not only attempt to allocate each resource to its most highly valued use, it also requires that as little as possible of each resource is used to produce any amount of any output.

[R]educing costs means setting free resources which could produce more elsewhere. In any particular instance, the primary aim must therefore always be to use as few resources as possible for a given output.... The secret of productivity

which makes it possible to employ many at high wages is for each producer to do his job with the use of as few resources as possible. ...

It has come to be thought in Britain [due to unions] that a prime task of economic policy was the protection of *existing* jobs. This fundamental reversal of the truth has developed into a sort of anti-economics which has misrepresented the chief social goal to be the use of as *large* a quantity of resources as possible (ibid. pp 34-5, emphasis in original).

One common manifestation of this phenomenon is union-imposed workplace rules that stipulate the types and amounts of labour that must be devoted to each task. I recently gave a lecture at a convention hotel in Las Vegas. I had prepared a PowerPoint presentation, but I was tardy in requesting the organizers to provide a data projector. When I did, it was too late. I offered to bring my own projector and set it up myself. That, I was told, was impossible because in this union-impaired hotel only in-house equipment could be used and only union workers could set it up and operate it.

Hayek discussed yet another way by which unions have lowered the overall productivity of labor: through their influence on investment and the composition of the capital stock. Hayek recognized what is today called the holdup problem. Specific capital goods, those which when once acquired and set up by employers have few, if any, alternative uses, present unions with opportunities to expropriate most of the returns from the productivity of those capital goods. The cost of acquisition of capital equipment is its purchase price minus any immediate resale value it may have. If it is specific capital it has few if any other uses, and thus its resale value will be very low. This means almost all the purchase price is a sunk (unavoidable) cost. Under these circumstances it is rational

for an employer to continue to operate as long as after-tax revenue is any amount over variable costs, which include labour costs. If a union drives up labour costs so that there is only a penny left over out of after-tax revenue after the other variable costs are covered, that penny would be the only return to capital. Specific capital has nowhere else to go, so the penny is better than nothing. Of course employers recognize this danger. That is why most of them try to avoid unionization. Where that is not possible, employers attempt to minimize their purchases of highly specific, relative to less specific, capital equipment, or they simply reduce their investment spending in general.

It is true that any union effectively controlling all potential workers of a firm or industry can exercise almost unlimited pressure on the employer and that, particularly where a great amount of capital has been invested in specialized equipment, such a union can practically expropriate the owner and command the whole return of his enterprise (1960, p. 270).<sup>7</sup>

Because unions are most powerful where capital investments are heaviest, they tend to become a deterrent to investment – at present probably second only to taxation (ibid, pp. 272-3).

Personally, I am convinced that this power of union monopolies is, together with contemporary methods of taxation, the chief deterrent to private investment in productive equipment which we have allowed to grow up. We must not be surprised that private investment dries up as soon as uncertainty about the future increases after we have created a situation in which most of the gain of a large, risky and successful investment goes to the unions and the government, while any loss has to be borne by the investor ([1959] 1967, p. 286).

Low productivity diminishes the flow of incomes that arise from production and exchange. It decreases the average real standard of living.

It is more than doubtful ... whether in the long run these selfish practices [of unions] have improved the real wages of even those workers whose unions have been most successful in driving up their relative wages – compared with what they would have been in the absence of trade unions. It is certain, and could not be otherwise, that the average level of attainable real wages of British workers as a whole has thereby been substantially lowered. Such practices have substantially reduced the productivity potential of British labour generally. They have turned Britain, which at one time had the highest wages in Europe, into a relatively low-wage economy ([1980] 1984, p. 53).<sup>8</sup>

The logical implication of this observation is that, at least in the long run, unions don't benefit the workers they represent. They benefit only union leaders who, in effect, are paid very handsomely to make the rest of us worse off.

The myth that unions benefit the working class dies hard. Yet the evidence is quite clear. "Real wages have often risen much faster when unions were weak than when they were strong; furthermore, even the rise in particular trades or industries where labor was not organized has frequently been much faster than in highly organized and equally prosperous industries" (1960, p. 271-2). The best discussion of this question is in Reynolds (1991).

## **Unions Threaten the Free Society and the Market Economy**

Apart from their malign economic effects, Hayek saw labour unions as a threat to the free society. In *Law, Legislation and Liberty* Vol. III (1979), while discussing the role of special interest groups in unlimited majoritarian democracies Hayek pointed out that the methods commonly employed by labour unions are especially damaging.

It was a misfortune that these [special interest group] problems became acute for the first time in connection with labour unions when widespread sympathy with their aims led to the toleration of methods which certainly could not be generally permitted .... One need merely ask what the results would be if the same techniques were generally used for political instead of economic purposes (as indeed they sometimes already are) in order to see that they are irreconcilable with the preservation of what we know as a free society (1979, p. 89).

Government employee unions have indeed carried the methods of coercion into the determination of public policy in the US. The principles of exclusive representation, union security and mandatory good faith bargaining in government employment, in effect make government employee unions an unconstitutional fourth branch of government.<sup>9</sup>

Hayek was also concerned that the actions of labour unions were leading inexorably to the crippling of the market economy and the emergence of central economic planning.

It is scarcely an exaggeration to say that, while we still owe our current living standards chiefly to the operation of an increasingly mutilated market system, economic policy is guided almost entirely by a combination of the two views

whose object is to destroy the market: the planning ambitions of doctrinaire socialist intellectuals and the restrictionism of trade unions and trade associations ([1980] 1984, p. 40).

[Unions] are using their power in a manner which tends to make the market system ineffective and which, at the same time, gives them a control of the direction of economic activity which would be dangerous in the hands of government but is intolerable if exercised by a particular group....

Unionism as it is now tends to produce that very system of overall socialist planning which few unions want and which, indeed, it is their best interest to avoid (1960, pp. 272-3).

### **Freedom of Association**

Unions claim that they are based on workers' freedom of association. The International Labour Organization (ILO) proclaims that freedom of association is the most basic right upon which union legitimacy rests. Hayek didn't see it that way. The unions and the ILO have a warped understanding of freedom of association. Correctly understood, freedom of association has both a positive and a negative dimension. The former is the principle that each person is free to associate (for legal purposes) with any other person or persons who are willing to associate with him. The latter is the principle that each person has a right to refuse to associate with any person or persons who want to associate with him. If there is no effective right to abstain from unwanted association the right to choose one's associations is meaningless. The unions and the ILO do not recognize the right of workers to abstain from association with unions. Their appeal to freedom of association as justification for coercive unionism is pure hypocrisy.

The unions have of course now become the open enemies of the ideal of freedom of association by which they once gained the sympathy of the true liberals.

Freedom of association means the freedom to decide whether one wants to join an association or not. Such freedom no longer exists for most workers. The present unions offer to a skilled worker only the choice between joining and starving, and it is solely by keeping non-members out of jobs that they can raise the wages of particular groups of workers above the level they would reach in a free market ([1978] 1984, p. 61).

Hayek began Chapter 18 in *The Constitution of Liberty* with a section titled “Freedom of Association.” In it he argues that unions have transformed that principle into a right to coerce.

Most people ... have so little realization of what has happened that they still support the aspirations of the unions in the belief that they are struggling for ‘freedom of association,’ when this term has in fact lost its meaning and the real issue has become the freedom of the individual to join or not join a union. The existing confusion is due in part to the rapidity with which the character of the problem has changed; in many countries voluntary associations of workers had only just become legal when they began to use coercion to force unwilling workers into membership and to keep non-members out of employment. Most people probably still believe that a ‘labor dispute’ normally means a disagreement about remuneration and the conditions of employment, while as often as not its

sole cause is an attempt on the part of the unions to force unwilling workers to join (1960, p. 268).

In a later section of the same chapter, titled “Constraining Coercion,” Hayek argued that to do so, “The essential requirement is that true freedom of association be assured and that coercion be treated as equally illegitimate whether employed for or against organization, by the employer or by the employees” (ibid. p. 278).

In sum, according to Hayek, just as appeal to freedom of association was the means by which unions made their claim to legitimacy, appeal to freedom of association correctly understood is the essential means by which unions can be transformed from involuntary into voluntary (and therefore legitimate) organizations.

### **Freedom of Contract**

Then, continuing in the same section, Hayek gets into what I consider to be a bit of logical trouble. He was so adamantly opposed to the closed shop as it evolved under the unions’ illegitimate privileges and immunities granted by the Trades Disputes Act in Britain and the National Labor Relations Act in the US that he failed to recognize that closed shop agreements between a truly voluntary union and a willing employer would be consistent with true freedom of association. Here is Hayek’s argument:

[T]he unions should not be permitted to keep non-members out of any employment. This means that closed- and union-shop contracts ... must be treated as contracts in restraint of trade and denied the protection of the law. They differ in no respect from the ‘yellow-dog contract’ which prohibits the individual worker from joining a union and which is commonly prohibited by the law (ibid.).



He implies that “yellow dog” contracts (which I prefer to call “union-free” contracts) are properly prohibited by the law. I disagree. A job offer made by an employer to an employee has several components. The compensation package stipulates a direct wage or salary along with a set of other benefits of various descriptions. Hayek certainly would not argue that an employer should be prohibited from offering any compensation package he chooses. He certainly would argue that the prospective employee has the right to accept or reject the compensation package. Similarly, the job description itself (the stipulation of the time, place and manner of the employee’s expected actions on the job) is another part of the job offer. Hayek certainly would not argue that an employer should not be able to make such stipulations. Again, he would argue that the prospective employee must be free to accept or reject the offer. It seems to me that if an employer wants to include a union-only agreement in the job offer that is his right. The prospective employee would have a corresponding right to accept or reject the job offer. Any job offer will consist of some things a prospective employee likes and other things he doesn’t like. He must settle the tradeoffs in his own mind before he exercises his right to accept or reject the job offer.

Now, in the absence of any special privileges or immunities for unions or employers, I think the principle of freedom of contract (which is part of the freedom of association), implies that a willing employer has a right to agree with a truly voluntary union to hire only union members as employees. I wouldn’t expect many truly free employers to do so, but I think they should be free to do so. If such agreements work in a free market setting, they will be adopted by other employers and other unions. If they don’t work they will not be adopted. The market will sort it all out. Hayek endorsed the

principle of letting the market sort things out in other settings. He was not logically consistent when he advocated government interference in market arrangements in this setting.

I will go even further. The problem with exclusive representation in American labour law is not exclusive representation itself. It is that the law compels exclusive representation. In the absence of the National Labor Relations Act, I see no reason why an employer should not be free to agree with a voluntary union that the question of union representation will be decided by majority vote among the employees. Certainly in the case of a brand new enterprise, where all prospective employees know that there will be such a vote, such an arrangement should not be prohibited. In an established enterprise the terms of each individual worker's hiring contract would determine whether he could be bound by any post-hiring vote among his colleagues on the issue of union representation. Again, I would not expect many truly free employers would choose to enter such agreements.

My position on this issue is, of course, that taken by Milton Friedman (1962, pp. 115-6). Friedman argued that American right-to-work laws (which, in the twenty-two states that have adopted them, prohibit a union from agreeing with an employer to require union membership or the payment of union dues as a condition of continued employment) were, by themselves, illicit interferences by government in the freedom of contract. He went on to state that the problem that should be remedied is the monopoly power that the National Labor Relations Act grants to certified unions. Friedman did not explicitly say that without such monopoly power, the right-to-work laws would be moot, but they certainly would be. If unions represented only their voluntary members, they

would have no argument to justify any sort of compulsory membership or support. In any case, there is no place for right-to-work laws in a truly free labour market.

Hayek goes on, in the same section, to claim that his position on closed shop and union-free contracts (that both should be prohibited) is consistent with the principle of freedom of contract correctly understood.

It would not be a valid objection to maintain that any legislation making certain types of contracts invalid would be contrary to the principle of freedom of contract. We have seen before (in chap. xv) that this principle can never mean that all contracts will be legally binding and enforceable [sic]. It means merely that all contracts must be judged according to the same general rules and that no authority should be given discretionary power to allow or disallow particular contracts.

Among the contracts to which the law ought to deny validity are contracts in restraint of trade. Closed- and union-shop contracts fall clearly into this category (1960, pp. 278-9).

Here, again, I disagree. Closed- and union-shop contracts in the context of special privileges and immunities for unions clearly are illicit. But the best solution is to eliminate those special privileges and immunities. If that cannot be done, then, as a second best, measures like American right-to-work laws could be used to protect individual worker rights.

The term “contracts in restraint of trade” is a work of art. It means different things to different people. In particular that term has played a mischievous role in the sad history of antitrust regulations. One person’s contract in restraint of trade is another’s

innovative arrangement to cope with market realities. As Dominick Armentano (1982) has shown, American antitrust laws have more often been used to protect particular competitors than to protect the process of competition and consumers. I infer from Hayek's condemnation of contracts in restraint of trade in the context of unions that he would support the application of antitrust laws to unions. Again, I disagree. As I have argued elsewhere (Baird, 2000) antitrust laws should be repealed. That together with repeal of the monopoly-granting privileges of the National Labor Relations Act would allow the market to sort out efficient from inefficient organizational architectures.

Finally, Hayek agreed with the position I have taken above concerning right-to-work laws as second-best alternatives.

Though there ought to be no need for special 'right-to-work laws,' it is difficult to deny that the situation created in the United States by legislation and by decisions of the Supreme Court may make special legislation the only practicable way of restoring the principles of freedom (1960, p. 279).

Of course right-to-work laws do not really restore principles of freedom. They are actually an infringement on the freedom of contract made necessary to partially offset even greater infringements on freedom of association and contract. What we ought to do is abolish all such infringements.

### **Strikes and Picketing**

If a strike is defined as a collective withholding of labour services by workers who find the terms and conditions of employment offered by an employer to be unacceptable, then there is a legitimate right to strike. I call this the voluntary exchange right to strike. In the

absence of an unexpired fixed-term employment contract, any individual worker has a right to withhold his labour from an employer who doesn't offer satisfactory terms. If every worker has such a right they all can individually choose to exercise the right simultaneously. Even if a worker has an unexpired fixed-term contract with an employer, he cannot be forced to continue on the job. If he walks off the job the employer's only recourse is to sue him for breach of contract and let other employers know that he is an unreliable employee.

Neither the right of voluntary agreement between workers nor even their right to withhold their services in concert is in question (1960, p. 269).

I am even prepared to agree that *everybody* ought to have the *right* to strike, so far as he does not thereby break a contract....But I am convinced that nobody ought to have the right to *force* others to strike ([1980] 1984, p. 5, emphases in original).

When unions (and compliant politicians) claim that there is a right to strike, they mean something very different from the voluntary exchange right to strike. They assert that union leaders, or union members by majority vote, can force workers who do not want to strike to withhold their labour. In addition, they claim the right to prevent employers from hiring replacement workers during strikes and to prevent suppliers and customers from continuing to do business with struck firms. In other words they claim the right to prevent people who do not support a strike from exercising their voluntary exchange rights with strike targets. Unions exercise these extraordinary rights claims through picket line intimidation and violence.

The present coercive powers of unions ... rest chiefly on the use of methods which would not be tolerated for any other purpose and which are opposed to the protection of the individual's private sphere. In the first place, the unions rely – to a much greater extent than is commonly recognized – on the use of the picket line as an instrument of intimidation. That even so-called 'peaceful' picketing in numbers is severely coercive and the condoning of it constitutes a privilege conceded because of its presumed legitimate aim is shown by the fact it can be and is used by persons who themselves are not workers to force others to form a union which they [the non-employee strangers] will control .... (1960, pp. 274-5). [A]ll picketing in numbers should be prohibited, since it is not only the chief and regular cause of violence but even in its most peaceful forms is a means of coercion (ibid, p. 278).

The US Supreme Court addressed these picket line questions in its decision in *American Steel Foundries v. Tri-City Central Trades Council* (257 US 184 [1921]). The Court noted that even peaceful picketing can be intimidating so it limited the number of pickets to one per entrance. Moreover, the Court ruled that only actual employees could be pickets. No strangers bussed in from union headquarters could participate. Both parts of the decision were overruled by Congress in 1932 with the enactment of the Norris-LaGuardia Act.

Hayek claimed that even the voluntary exchange right to strike “though a normal right, can hardly be regarded as an inalienable right” (1960, p. 269). There are certain employments (he did not give an example) where “workers should renounce this right” by entering “long-term obligations,” and “any concerted attempts to break such contracts

should be illegal” (1960, p. 269). Twenty years later Hayek gave an example – enterprises on which the law has “conferred a monopoly” ([1980] 1984, p. 51). He was thinking of private enterprises, but I think his point applies most obviously to the military, the police, and firefighters. In the US the military cannot be unionized, but police and firefighter unions have gone on strike with impunity in several states and localities. Hayek’s suggestion that strikes against private firms with government-granted monopoly power are especially harmful because consumers have no alternative sellers to whom to turn, applies to almost all strikes by government employee unions. Government employing agencies almost always have monopoly power. Private sector alternatives are often simply outlawed. Hayek had nothing explicit to say about unionism in the government sector. He probably thought his arguments against private sector unionism applied a fortiori to the government sector.

As an aside, most Americans accept the common sense idea that strikes by police and firefighters ought to be prohibited. So unions representing those government employees have argued, often successfully, that strikes should be replaced by compulsory arbitration over the terms and conditions of employment. This is incompatible with a basic democratic value: there should be no taxation without representation. The terms and conditions of government employment are matters of public policy paid for by taxpayers. Unelected arbitrators should not be able unilaterally to determine the taxes that taxpayers must pay.

### **Profit Sharing and Codetermination**

Hayek thought that collective bargaining, as it had evolved by 1972 in Britain, created so many problems that it simply had to be replaced by some “alternative method of wage

determination which, while offering the worker as a whole a better chance of material advance, at the same time restores the flexibility of the relative wages of particular groups” (1972, p. 117). He came up with a specific solution.

The only solution of this problem I can conceive is that the workers be persuaded to accept part of their remuneration, not in the form of a fixed wage, but as a participation in the profits of the enterprise by which they are employed. Suppose that, instead of a fixed total, they could be induced to accept an assured sum equal to, say, 80 percent of their past wages *plus* a share in profits which in otherwise unchanged conditions would give them on the average, their former real income, but, in addition, a share in the growth of output of growing industries. In such a case the market mechanism would again be made to operate and at the same time one of the main obstacles to the growth of social product would be removed (ibid., emphasis in original).

He recognized that such a proposal “raises many difficult problems” (ibid.), but he did not discuss any specific examples. I think union leaders, whose incomes depend on sustaining the illusion that employers and employees are natural enemies, would fight this idea every time and in every venue in which it was proposed. Given Hayek’s distaste for schemes imposed by government, I doubt that he would support any legislation aimed at forcing this outcome. It would have to be adopted, by willing employers and employees, one enterprise at a time. Still, given the success of several different sorts of profit sharing plans in American union-free enterprises, the idea cannot be dismissed as an impossible dream.



Hayek's profit sharing proposal must not be confused with the insidious institution, particularly popular among muddled thinkers even today, called codetermination. This idea calls for government to require that workers (and, often, other "stakeholders") be given a role equal to the role of owners and their agents in controlling most aspects of businesses. Efficiency in the allocation of resources depends crucially on decisionmakers in firms being accountable to the owners of the firms and that the criterion for success is the maximization of long-term owner value through voluntary exchange. To maximize long-term owner value it is necessary for decisionmakers to seek to serve the interests of customers, and this requires striving for cost minimization and timely adaptations to changing market conditions. If diverse groups of stakeholders, with diverse objectives, all have part control over an enterprise, decisionmaking therein degenerates into a political process based on a strife of interests. Even if decisionmaking is done democratically, as advocates of "industrial democracy" would have it, choices among three or more alternatives could result in cyclical majorities – i.e., no one alternative can beat all of the others by majority vote – and this would give rise to battles of varying degrees of civility and totally unpredictable outcomes (Barry 2002).

Hayek was clear in his condemnation of industrial democracy and codetermination. After discussing some legitimate functions for voluntary unions he asserted that codetermination was not one of them.

An entirely different matter ... is the claim of unions to participation in the conduct of business. Under the name of 'industrial democracy' or, more recently, under that of 'co-determination,' this has acquired considerable popularity, especially in Germany and to a lesser degree in Britain. It represents a curious

recrudescence of the syndicalist branch of nineteenth-century socialism, the least-thought-out and most impractical form of that doctrine. Though these ideas have a certain superficial appeal, they reveal inherent contradictions when examined (1960, p. 277).

### **In Conclusion**

The Thatcher reforms of British labour law by the Employment Acts of 1980 and 1982 and the Trade Union Act of 1984 went a long way toward removing the most egregious privileges and immunities British unions had enjoyed since the 1906 Trade Disputes Act, but there is still a way to go before British unions become truly voluntary. In the US, labour law has changed very little since the 1959 amendments to the National Labor Relations Act (which attempted to give rank-and-file members more control over union leaders). All the worst privileges – exclusive representation, union security and mandatory good faith bargaining – plus the court-granted immunity to prosecution for acts of violence during labour disputes remain. As Hayek said about the economic myths that sustain coercive unionism, “A departure from such a condition can come only from a truer insight into the facts, and whether this will be achieved depends on how effectively economists do their job of enlightening public opinion” (1960, p. 273). But it is not just economists who should attempt to enlighten public opinion on unionism. The rule-of-law issues raised by Hayek imply that historians, legal scholars, and philosophers also have a continuing role to play. To be a true friend of labour, one cannot be a friend of coercive unionism.

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## Endnotes

- 1 Although Hayek made frequent references to labour unions in several essays, his thinking on this issue is most completely represented in just three sources: “Unions, Inflation and Profits,” ([1959], 1967), Chapter 18 of his *Constitution of Liberty* (1960) and the monograph he wrote for the Institute of Economic Affairs in 1980, *1980s Unemployment and the Unions*. The IEA published a second edition of this monograph in 1984 which consisted of Hayek’s original essay and a postscript by Charles G. Hanson which addressed the Thatcher union reforms of the early 1980s.
- 2 I do not know how unions were treated by the law in Britain in the latter part of the 19<sup>th</sup> Century, but it is clearly not the case that in the US the legitimate functions of unions were ever proscribed or prosecuted (Baird, 1984).
- 3 For thorough documentation of union violence in the US see Thieblot et. al, (1999).
- 4 See also Hayek’s “Full Employment, Planning and Inflation” ([1950] 1967, pp. 271-2).
- 5 See also Hayek’s *A Tiger by the Tail* (1972, p. 118)
- 6 What is now called the Austrian theory of the trade cycle was first explicated by Ludwig von Mises in *The Theory of Money and Credit* (1912). Hayek developed that theory in the 1930s.
- 7 See also Hayek’s “Unions, Inflation and Profits” ([1959] 1967, pp. 285-6).
- 8 See also *The Constitution of Liberty* (1960, p. 271).
- 9 This argument is fully developed by Robert S. Summers (1976)