

# THE NEW ZEALAND EMPLOYMENT CONTRACTS ACT: ITS ENACTMENT, PERFORMANCE, AND IMPLICATIONS

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## INTRODUCTION

Optimal labor market legislation is a critical component of the framework that law provides to the economy. It helps determine how cooperation, coordination, and conflict are dealt with in the labor market, thereby affecting the life chances of individuals and firms. Labor market legislation cannot resolve all problems or conflicts, though it may help reduce their damage by providing a means of resolution. The New Zealand case illustrates the importance of labor market regulation, not merely as a static set of rules, but as a dynamic factor in decision-making across the economy.

## BACKGROUND

The enactment, performance, and implications of the Employment Contracts Act should be understood and evaluated in the context of the series of major reforms undertaken in New Zealand by successive governments. The reforms began in 1984 and were triggered by an exchange rate crisis. The main elements include the following:

- The removal of foreign exchange and interest rate controls, the deregulation of financial markets, and the floating of the New Zealand dollar. The Reserve Bank Act of 1989 made the central bank independent of government, with the primary aim of monetary policy being “price stability.”
- Subsidies to farming and industry were virtually eliminated, tariffs lowered (an ongoing process), and trade with Australia became fully free in 1989.
- Taxes were simplified, with the top rate of personal income tax halved (from 66 percent to 33 percent). The corporate income tax was set at the same rate. A flat-rate consumption tax was introduced (currently at 12.5 percent) with minimal exceptions to its coverage.
- The domestic air market was opened up, and ports, coastal shipping,

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and road transport were deregulated.

- Many public sector trading activities were corporatized and some (including telecommunications, railways, and various publicly owned banks) were privatized.
- The public education and health sectors were reformed, decentralized (education), and made more market-oriented (health).
- The State Sector Act 1988 placed employment in the public sector on a similar basis to employment in the private sector. The relationship between ministers and chief executives of government departments was contractualized, with chief executives having discretion over inputs (including employment and wages) while being accountable for delivery of outputs.
- The Public Finance Act of 1989 clarified expenditure controls and introduced accrual accounting. The Fiscal Responsibility Act of 1994 imposes high standards of financial disclosure, including disclosure of fiscal intentions.

In combination, the scale and impact of these reforms were massive, exceeding the extent of liberalization of any other member country of the Organisation for Economic Cooperation and Development (OECD). The Fraser Institute has rated OECD countries for "economic freedom," using a variety of measures. It has compared countries' current rating with their "initial" rating for the situation preceding economic reform (the year of the initial rating thus varying from country to country). By these measures, New Zealand shows the largest absolute and proportionate change of 23 countries, and moving to first place overall in 1995.<sup>1</sup> A recent review found: "In no other OECD country has there been so systematic an attempt at the same time (1) to redefine and limit the role of government, and (2) to make public agencies and their operations more effective, more transparent, and more accountable."<sup>2</sup>

#### BEFORE THE 1991 ACT

Prior to 1991, government institutions had played a central role in industrial relations, though the precise form varied. The Industrial Conciliation and Arbitration Act of 1894 gave trade unions special rights and protections and set up conciliation and arbitration mechanisms. In exchange, the right to strike was removed. In practice, the proscription of strike action was ignored by the stronger unions—some of which deregistered—and the courts did not challenge this.<sup>3</sup> Direct bargaining and direct action became

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1. JAMES GWARTNEY ET AL., *ECONOMIC FREEDOM OF THE WORLD, 1975-1995* (1996).

2. DAVID HENDERSON, *ECONOMIC REFORM: NEW ZEALAND IN AN INTERNATIONAL PERSPECTIVE* (1996).

3. See, for example, the historical discussion in WOLFGANG KASPER, *FREE TO WORK: THE LIBERALISATION OF NEW ZEALAND LABOUR MARKETS* (1996).

widespread.<sup>4</sup> In 1951, a serious waterfront strike was resolved by the government's use of troops. In 1968, "the Arbitration Court was humiliated when the Federation of Labour (the then peak union council in the private sector) refused to accept a nil wage order . . . and succeeded in persuading the Employers Federation to join forces in having the decision overturned."<sup>5</sup> This action led to the Industrial Relations Act of 1973, which adopted the North American distinction between disputes of right and disputes of interest and gave a clear right to strike in disputes of interest.

The industrial relations legislation and state agencies were, therefore, far from achieving stability or avoiding confrontation. However, by the 1980s, the system gave unions the following four legally based and government enforced privileges: (1) Union membership was compulsory for all those working in a defined craft area; (2) once registered, unions had the monopoly of "their" occupation or craft with all employers; (3) unions could notify a "representative sample" of employers of a claim and negotiate with that sample, the agreed award then having blanket coverage; and (4) when disputes of interest arose, there was a clear right to strike, but employers and workers were subject to compulsory arbitration in a government court.<sup>6</sup>

Industrial relations became a matter of high-level, formal legal procedures by entities—unions and employer organizations—far removed from the workplace. New Zealand had, by international standards, an unusually centralized and legalistic wage setting process that was multi-tiered. National awards, negotiated on an industry or occupational basis, set minimum rates for various jobs at the national level. Other registered collective agreements set minimum wage rates for various jobs at the enterprise level. Informal house agreements established actual paid rates and work practices for particular jobs at the enterprise or site level. In addition, the government set minimum wages, and the Arbitration Court ordered general wage adjustments until the 1980s.

Such a system was complex, cumbersome, inflexible, and remote from market forces. It also made relativities difficult to shift. As even a small manufacturing firm could find itself subject to several different national awards, any significant shift in relativities in such awards was likely to cause havoc at the local workplace. Changed relativities would lead to demands for catch-up payments from those unexpectedly losing out in the pay stakes as well as potential boundary disputes between different occupational groups. Nor could individual workplaces opt out of higher level settlements, even if such opting-out or modification of higher level awards or agreements was clearly beneficial to all parties. On a number of occasions, trade

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4. Peter Boxall, *New Zealand's Employment Contracts Act 1991: An Analysis of Background, Provisions and Implications*, 17 (4) AUSTL. BULL. LAB. 284-309 (1991).

5. *Id.* at 287.

6. The list is adapted from KASPER, *supra* note 3, at 23.

unions successfully took court cases against employers who had agreed to innovative shift arrangements with their employees, because they did not happen to conform to the standard arrangements in a national award.

Thus, in establishing union rights and seeking to formalize negotiations, the system discouraged innovation or cooperation between employers and employees at the local level. Wage fixing was, essentially, seen as a matter of controlled class warfare. Indeed, the legal requirement under the 1973 Act to notify a dispute of interest for some labor rights to apply—notably the right to strike—enshrined in law the notion of industrial relations as a form of conflict.

This system was associated with a relatively closed economy and a high level of regulation (one of the highest in the OECD). These features in turn led to widespread monopolies or cartels and to macroeconomic instability.<sup>7</sup> One commentator, speaking of both Australia and New Zealand in this period, says: “The recourse that unions had to the courts to press their claims made wages the fixed point in the system to which all other prices had to adjust. Instead of being on a Gold Standard, Australia and New Zealand were on a Labor Standard.”<sup>8</sup> The situation yielded poor productivity growth. Throughout the 1960s, 1970s, and 1980s, New Zealand’s productivity growth (annual change in GDP/person employed) lagged the OECD average, generally by at least one third.<sup>9</sup> Nor did labor relations remain harmonious. During the 1950s and 1960s, New Zealand is said to have enjoyed a low rate of industrial disputes compared with most countries.<sup>10</sup> However, days lost to industrial disputes rose during the 1970s and 1980s, and New Zealand was ranked in the OECD as having the fifth highest incidence of days lost through strikes in the five years to 1992.<sup>11</sup>

#### ATTEMPTS AT REFORM IN THE 1980S

The poor performance of the New Zealand economy, and the 1984 crisis in particular, led to debate over labor market legislation. This debate focused on two broad issues: whether real wages were too high and whether

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7. *Id.*

8. JOHN PENCAVEL, *REGULATING COLLECTIVE BARGAINING IN DEVELOPING COUNTRIES: LESSONS FROM THREE DEVELOPED COUNTRIES* (1997). Pencavel draws the comparison of a “labor standard” with a “gold standard” from the eminent British economist, John Hicks.

9. KASPER, *supra* note 3, at 4, Table 1.

10. STEPHEN EDWARDS & FRANK HOLMES, *CER ECONOMIC TRENDS AND LINKAGES* 68 (1994).

11. *ECONOMIST*, Jan. 29, 1994, at 106. Working days lost per thousand employees were considerably lower in 1991 and 1992 than in the previous three years. Thus, the effect is not due to the implementation, or threat of implementation, of the Employment Contracts Act. The level of working days lost in 1987-1990 is in line with or lower than other years in the 1970s and 1980s. Pencavel, *supra* note 8, at 4, Table 1 (reports on the relatively high level of strike action in New Zealand during the 1970s and 1980s).

the labor market was too centralized and inflexible.<sup>12</sup> Tripartite discussions led to the formation of a Long Term Wage Reform Committee in 1982 whose 1984 "statement of understanding" called for greater flexibility.<sup>13</sup> By the time the new Labour government held an economic summit in late 1984, trade union leadership was explicitly recognizing the need for greater flexibility in the labor market.<sup>14</sup> However, the government's early moves (in 1984) included the reintroduction of compulsory unionism (unionism had been made voluntary in 1983 by the previous National government), in line with an election commitment. One liberalizing initiative that it took at the same time was to abolish compulsory arbitration, and it also adopted at an early stage a policy of non-involvement in industrial disputes.

The Labour Relations Act of 1987 made some changes to the system, including the removal of union monopolies and allowing unions to compete for members; unions (but not employers) could opt out of awards; and a minimum qualifying size for registration as a union—1,000 members—was introduced. These changes perhaps represented what was acceptable to the larger unions in a trade union movement that, historically, had been close to the Labour Party.

The new opt-out procedures available to unions under the 1987 Act allowed some enterprise-level deals to be struck, but in other cases unions exercised their right to stand outside such deals.<sup>15</sup> Key wage negotiations were still a matter of rule-bound and ritualized confrontations at an aggregate level. The Act did not deal with the link between union structure and bargaining structure and, by setting a minimum union size of 1000, it did little to introduce contestability in employee representation. Indeed, the Act's reforms, combined with the economic restructuring, probably created incentives which "encouraged most unions to act cautiously with respect to major bargaining changes."<sup>16</sup>

The changes were insufficient for the labor market to be able to cope with the economic impact of the far-reaching reforms that the government had unleashed. For example, from the 1950s to the mid-1970s, the manufacturing sector accounted for a growing share of employment in New Zealand—from 4 percent to just under 26 percent. With deregulation and lower trade barriers, this number fell rapidly to some 18 percent by 1992.<sup>17</sup> Between Quarter One of 1987 and Quarter Four of 1991, employment in manufacturing fell by some 70,000—5 percent of total civilian employ-

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12. The first debate is summarized in SIMON CHAPPLE, NZIER WORKING PAPER 93/17, *THE REAL WAGE DEBATE: A CRITICAL SURVEY* (1993). A key document in the second debate is THE TREASURY, *ECONOMIC MANAGEMENT* 234-47 (1984).

13. OECD, *OECD ECONOMIC SURVEYS: NEW ZEALAND 1988/89* at 44 (1989).

14. RICHARD BLANDY & MEREDITH BAKER, *INDUSTRY ASSISTANCE REFORM AND THE LABOUR MARKET: THE NEW ZEALAND EXPERIENCE* 21 (1987).

15. Boxall, *supra* note 4, at 290.

16. *Id.* at 291.

17. EDWARDS & HOLMES, *supra* note 10, at 61.

ment.<sup>18</sup> With restructuring, surveyed unemployment rose from some 4 percent in the mid-1980s to 11 percent in 1991 (compared to an average in the Group of Seven major economies of 6-7 percent throughout the period).<sup>19</sup> It is scarcely surprising that the OECD commented, in 1989, that “despite some changes in labor market practices, it is clear that further changes would assist better labor market outcomes,”<sup>20</sup> or that the then Minister of Finance, David Caygill, could refer to the “rickety” New Zealand labor market.<sup>21</sup>

### THE 1991 ACT

In late 1990, a National Party government was elected to power, after six years in opposition. Bill Birch, who became the new Minister of Labour, described the situation as follows:

The urgent need for labour market flexibility was made a major issue by the National Party in the 1990 election. . . . I was the party's labour relations spokesman during the lead-up to the election and it was made clear that on becoming the Government we would remove compulsory unionism; remove mandatory coverage; and facilitate enterprise bargaining to encourage more flexible labour markets. . . . During 1990 I accepted regular invitations from trade unions to brief them on the National Party's intentions and by the date of the elections we had prepared detailed programmes for legislation. . . . This preparation enabled the new National Government to introduce full legislation in the form of the Employment Contracts Act before Christmas 1990.<sup>22</sup>

Given the mindset underlying the previous legislation, there arose numerous prophets of doom when the new legislation was proposed. They predicted that, without all the statutory complexity of controls and carefully specified rights and restrictions, class warfare might emerge in raw form. They anticipated harsh conflict and the disruption of business without the guiding hand of the state.<sup>23</sup> Some government officials were nervous about the radical reforms proposed and argued for minimum initial moves to be followed by an “orderly process of change” to be completed through consultation and review.<sup>24</sup> To the credit of the National government, they re-

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18. OECD, OECD ECONOMIC SURVEYS: NEW ZEALAND 1995/96 at 49 (1996) (Figure 14).

19. EDWARDS & HOLMES, *supra* note 10, at 63.

20. OECD, OECD ECONOMIC SURVEYS: NEW ZEALAND 1986/87 at 46 (1987).

21. Penelope Brook, *Reform of the Labour Market*, in ROGERNOMICS: RESHAPING NEW ZEALAND'S ECONOMY 204 (Simon Walker ed., 1989).

22. Rt. Hon. W.F. Birch, Minister of Finance, Speech to the Wellington District Law Society (June 7, 1997).

23. See KASPER, *supra* note 3, at 29, which catalogues some of these and other negative forecasts.

24. Pat Walsh & Rose Ryan, *The Making of the Employment Contracts Act*, in EMPLOYMENT CONTRACTS: NEW ZEALAND EXPERIENCES 19 (Raymond Harbridge ed., 1993).

fused to be dissuaded from substantial reforms. They may have been following the advice of Roger Douglas, the driving force behind the previous Labour government's reforms in other areas, who said, "If a window of opportunity opens up for a decision or action that makes sense in the medium term, use it before the window closes!"<sup>25</sup>

However, the new legislation did contain some significant concessions to those who argued that the employment relationship was special and needed special treatment in statute. The Act was a sufficiently radical break with the previous statutory regime to enable a new basis for cooperation to be achieved. In these terms, the Employment Contracts Act is fundamental to upgrading business and the economy. It provides a framework for the parties most immediately able to cut deals at a local level, who have both the knowledge and incentives to do so. The Act gives opportunity to both employers and employees through freedom of association; through the ability of an employer or employee to appoint a bargaining agent, or not, as they choose; through the freedom of the parties to decide on the form of a contract; and through the freedom of the parties to determine the content of the contract.

An Enterprise New Zealand Trust publication includes the following statement: "The Employment Contracts Act has allowed the parameters for flexibility in employment relationships to be set only by the limitations of the imagination of the parties to that relationship."<sup>26</sup> Of course, this does not mean that the parties will always get it right or that there will always be agreement. But management and employees at an enterprise or site level are much more likely to find the optimal arrangement than national level representatives of capital and labor, playing elaborate strategic games and without the knowledge, incentives, or ability to reflect local concerns.

### THE MAJOR GAINS UNDER THE EMPLOYMENT CONTRACTS ACT

There have been numerous studies of the impact of the 1991 Act. In summary, the main effects have been identified as the following:

- A reduction in contract size, and the virtual elimination of multi-employer contracts.<sup>27</sup> The terms and conditions of employment are no longer imposed on employers and employees from outside. When free to choose, few choose big or multi-employer contracts.<sup>28</sup>

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25. Roger Douglas, *Ten Principles of Structural Reform*, 6 POLICY 1, 4 (1990).

26. Steve Marshall, *The Impact of the Employment Contracts Act*, 5 ECONOMIC ALERT (Aug. 1994).

27. JOHN SAVAGE, WHAT DO WE KNOW ABOUT THE IMPACTS OF THE ECA? (N.Z. Institute of Economic Research Working Paper No. 96-9, 1996); Raymond Harbridge, *Trends from Research on the Effects of the Employment Contracts Act* (Industrial Relations Centre, Victoria University of Wellington, 1996). The proportion of employees on individual contracts has risen from approximately 40 percent in 1990 to 70 percent in 1996.

28. Department of Labour Collective Employment Contract Statistics Database and Contract Quarterly Bulletin (refer to Department of Labour, P.O. Box 3705, Wellington,

- Increased variation in the size of settlements.<sup>29</sup>
- A reduction in unionization.<sup>30</sup> Again, when free to choose and when trade unions do not have privileged access to the bargaining table, fewer choose to join unions.
- A reduction in work stoppages.<sup>31</sup> This has been less marked in the public than in the private sector, possibly because some large centralized contracts remain in the latter—notably the central employment contracts for primary and secondary school teachers.
- Reduction in overtime rates and workplace demarcations but increases in performance-based pay, flexible work practices, and multi-skilling.<sup>32</sup>
- A majority of employers surveyed in 1996 attributed gains in labor productivity, operational flexibility, and training to the Employment Contracts Act.<sup>33</sup>
- A gain in employment of some 17 percent from 1991 to 1996. There has been a corresponding fall in unemployment from 11 percent to 6 percent, notwithstanding a reversal of migration flows between Australia and New Zealand so that New Zealand gained from migration during the period. While the employment and unemployment trends are the product of forces across the economy, the New Zealand experience during the 1990s is unusually positive both historically and compared with other countries.<sup>34</sup>
- Disproportionately large rises in employment and falls in unemployment occurred among Maori and Pacific Islanders and the long-term unemployed.<sup>35</sup>

In view of these effects, it is scarcely surprising that surveys of employers and the general public in 1996 found that far more were positive than negative about the Employment Contracts Act, notwithstanding much initial negative publicity.<sup>36</sup> The predicted industrial unrest and disruption to business from implementation of the Employment Contracts Act—which

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29. Union density is calculated to have fallen from 40.8 percent to 24.1 percent from 1991 to 1994. Harbridge, *supra* note 27.

30. STATISTICS NEW ZEALAND, UNIONIZATION.

31. Savage, *supra* note 27; EMPLOYERS' FEDERATION, THE EMPLOYMENT CONTRACTS ACT: THE REAL WORKPLACE OUTCOMES (1996).

32. EMPLOYERS' FEDERATION, *supra* note 31.

33. STATISTICS NEW ZEALAND, KEY STATISTICS (1994 et seq., monthly publication).

34. For example, New Zealand's unemployment rate fell from one of the highest to one of the lowest in the OECD between 1991 and 1996. Similarly, employment growth appears to have been higher in New Zealand than in any other OECD country. New Zealand's rate of employment growth from 1991 to 1996 inclusive at 2.2% annum was 1.2 percentage points higher than the comparable rate for Australia despite the similarities between the two countries and their similar industrial relations systems prior to the Employment Contracts Act.

35. STATISTICS NEW ZEALAND, HOUSEHOLD LABOUR FORCE SURVEY (quarterly information release). The numbers of Maori and Pacific Islanders employed rose 28% and 40% respectively between June 1991 and June 1996.

36. EMPLOYERS' FEDERATION, *supra* note 31.



had made some officials so cautious over the proposed legislation—failed to materialize.

One area where the impact of the Employment Contract Act has been open to some dispute is productivity. At the micro level, various employer surveys indicate significant productivity advances that are substantially attributed to the Employment Contracts Act.<sup>37</sup> In addition, overall labor productivity rose by around 2 percent per annum in 1991-96, with total factor productivity rising by 2.3 percent per annum. A substantial element of growth was achieved through increased labor inputs rather than increased productivity from existing inputs. The Employment Contracts Act, by freeing up the use of labor, made hiring new employees more attractive to employers. Many of these workers were in the lower skilled category. It is therefore hardly surprising that over this period crude average productivity measures (output per labor force member) have not been as striking as the employment figures. New Zealand's experience, however, bears out the observation of Australian Professor Tom Valentine, who has undertaken extensive econometric studies of the causes of unemployment: "Wages policy and microeconomic reform—particularly increasing labor-market flexibility—play a critical role in dealing with unemployment."<sup>38</sup>

#### ECONOMIC IMPLICATIONS

The OECD, in looking at the New Zealand labor market, has suggested that the overall implications of the Employment Contracts Act for macroeconomic performance may be threefold: *First*, it should make the labor market function more efficiently by allowing relative wages to respond to skill shortages; *second*, by removing the union monopoly influence on bargaining power, it may have lowered the NAIRU—the non-accelerating inflation rate of unemployment, or the lowest rate of unemployment which does not add to inflationary pressures through labor shortages; and *third*, by allowing more responsiveness to the different labor needs of different firms, the Act may raise productivity and decrease the NAIRU.<sup>39</sup>

The OECD may have underestimated the impact of the reform by overlooking the favorable medium- to long-term dynamics that the Employment Contracts Act has unleashed. *First*, by permitting innovation and cooperation in employment, the basis for a different business culture is created. New forms of business may arise which would not otherwise have been possible or even conceived. In a rapidly changing global economy, a dynamic business culture and innovations in work arrangements will be vital to New Zealand's economic future. *Second*, by permitting wage differentials to be driven by market forces, labor inputs will be more accurately

37. THE EMPLOYER, *passim*.

38. Tom Valentine, *Wage-Policy Link to Jobs*, AUSTL. FIN. REV. Sept.15, 1993.

39. OECD, OECD Economic Surveys 1995-1996 (N.Z. OECD, Paris, 1996).

priced. This means that inappropriate substitution of capital for labor will be avoided (where low-skill labor would otherwise have been overpriced) and that inappropriate substitution of labor for capital will also be avoided (where high-skill labor would otherwise have been underpriced). The net effect is to increase the productivity of both labor and capital. *Third*, by permitting wage differentials to be driven by market forces, better signals are sent regarding the need for appropriate forms of education and training. In the late 1980s, many firms found that previously valuable capital assets shrank in value in the new economic environment. Regrettably, the same fate attended many employees—the value of old skills (or lack of skills) and career paths dwindled or vanished. The answer is not to try to shelter firms or individuals from a changing world—that was the cause of the problem in the first place—but to give them the opportunity to adjust to economic restructuring. Market-driven prices send the appropriate signals. Thus, the Employment Contracts Act enables better and more informed investment in human capital for the future.

#### *Fairness and Market Power*

The Employment Contracts Act has seen a fundamental shift in the nature of industrial relations in New Zealand, and one that benefits the majority of employers and employees. These gains are at risk from attempts to achieve greater fairness by means of top-down legislation and from weaknesses within the existing legislation that seek fairness at the expense of a contractual and cooperative approach. The move from a collective and conflict-driven approach to industrial relations to one based on cooperation is, of course, deeply disturbing to some. As the car-dealer anti-hero of a BBC television series “Minder” put it: “You don’t get what is fair in life, you get what you negotiate.”<sup>40</sup> Fairness was the intention behind the previous industrial relations regime and is the cry of some New Zealand class warriors to this day. Some fear that the Employment Contracts Act may have gone too far in transferring bargaining power to the employer, in removing protections for employees or bargaining agents, or in failing to provide means or even incentives for collective contracting. In short, while the Act is a good thing, some argue it is too much of a good thing and needs winding back in the interest of fairness or balance.

To understand the issues, we need to distinguish between, on the one hand, the case for seeking just processes in law and, on the other hand, seeking some concept of equitable or just outcomes. While we should be passionate in pursuing the first concern, the second concern—sometimes called “social justice”—in the employment field, as elsewhere, is deeply mistaken and counterproductive. Thomas Sowell recently spoke in New Zealand on *The Quest for Cosmic Justice*. He vividly illustrates the conceptual and practical

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40. *Minder* (TVNZ television broadcast, Oct. 24, 1994).

problems when, in seeking fair outcomes, we decide that “all are not to be judged by the same rules or standards within the given process; pre-existing inequalities are to be counter-balanced.”<sup>41</sup> One of the problems Sowell brings out is that “traditional justice involves the rules under which flesh-and-blood human beings interact, while cosmic justice encompasses not only contemporary individuals and groups but also group abstractions extending over generations, or even centuries.”<sup>42</sup>

This move to abstraction and applying different rules to different groups underlies the move somehow to achieve greater fairness through industrial relations legislation. The underlying view is that employees are a disadvantaged group relative to employers and thus need extra rights and protections. The source of this inherent disadvantage of employees is unclear—except to strict Marxists. In a mobile society and open economy, there are few monopolies or monopsonies outside the public sector. Employers have to compete for labor, large employers are highly sensitive to their reputation as employers, and it is usually easy for an employee to quit a job. If employers are somehow exploiting employees, this implies that a little more could costlessly be squeezed out of employers for the benefit of employees. But, in a competitive economy, no monopolists enjoy lasting economic rents with pockets waiting to be emptied. There is no more to be squeezed out. If a firm’s labor costs rise, it will have to raise prices or reduce investment, cut back on employment, and so forth. The “bit more” that employees may gain has to come from somewhere.

In short, there is no free lunch. As we have seen, the beneficial results of the Employment Contracts Act include substantial job creation. Therefore, the cost of the previous legislation—with its attempts at cosmic justice—was a massive number of jobs foregone, especially for Maori and Pacific Islanders. Their ability as “outsiders” to compete with labor market “insiders” has been greatly enhanced since the Employment Contracts Act was implemented. If we cease to think of employers as an exploitative class and employees as a class in grave and constant danger of exploitation, the Employment Contracts Act ceases to look like such a radical document. Indeed, a more accurate view is that it incorporates a number of special protections and restrictions which do not sit comfortably with a simple, contractual approach.

### *Problems with the Employment Contracts Act*

Although the Employment Contracts Act was a radical change from the previous statutory regime, it is not without problems and limitations—not quite a model piece of legislation. Part III of the Employment Contracts Act establishes personal grievance procedures, and Part VI sets up the Employ-

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41. THOMAS SOWELL, *THE QUEST FOR COSMIC JUSTICE* 15 (N.Z. Business Roundtable, 1996).

42. *Id.* at 22.

ment Court and Tribunal. As Baird has argued, the judgments of this specialist Court are predicated on the assumption that employees as a class need special protection because of a perceived “imbalance” of bargaining power.<sup>43</sup> Although the Courts frequently refer to mutual obligations in the employment relationship, the obligations that seem to exercise the courts most are those of the employer.

The effect is to create high and uncertain costs to employers entering into an employment relationship.<sup>44</sup> An employer does not enter into a contract on equal terms but rather into a relationship where his or her actions and inactions are measured by standards that are different from, and less favorable than, those of the employee. Exiting from the relationship may prove highly problematic in law for the employer, as the Employment Court in practice tends to operate not so much in terms of a bilateral contract but in terms of the right to a job vested in the employee. While particular cases may benefit particular employees, the overall effect is to discourage employment and reduce wages as the employer makes allowance for legal contingencies—the so-called “unjustifiable dismissal” provisions acting as an employment tax.

The Employment Contracts Act contains a number of sections that limit freedom of contract and treat the employment relationship as different from other contracts. Thus, there is no ability to contract out from the provisions of the Act, for instance over personal grievances. The employment contract cannot simply be a normal commercial contract, without the special rights and jurisdictions imposed by the Act. An employee who preferred contract law and more pay to obtaining special rights to the job cannot opt for the former.<sup>45</sup>

Part V of the Employment Contracts Act defines certain strikes and lockouts as illegal and others as legal. Under Section 64 certain breaches of contract by the employer or employees are made legal. Thus, the Act distinguishes employment contracts from other contracts where two principles would normally apply: (1) that a contract can—but need not—include withdrawal rights; and (2) that, subject to this first principle, breach of contract opens liability to tort. The absence of withdrawal rights and lack of tort liability encourages and protects strike or lockout action. It is a remnant of the old emphasis on conflict rather than contract and cooperation. Of course, application of tort liability would provide a clear body of contract law to breaches.

The courts have also flirted with a form of good faith bargaining. In the 1992 case of *Telecom South v. Post Office Union*, Judge Richardson at the Court of Appeal stated that “the contract of employment cannot be equated

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43. CHARLES BAIRD, *THE EMPLOYMENT CONTRACTS ACT AND UNJUSTIFIABLE DISMISSAL* (1996).

44. *Id.*

45. New Zealand’s Inland Revenue Department patrols the border between “contracts of service” and “contracts for service” to ensure that employment relationships are not disguised as some other form of relationship. The courts have sought to apply the concepts behind the personal grievance regime of the Act to fixed-term contracts and to limit independent contracting.

with an ordinary commercial contract. It is a special relationship under which workers and employers have mutual obligations of confidence, trust and fair dealing."<sup>46</sup> Judge Richardson perhaps overlooks the fact that many other relationships contain mutual obligations of confidence, trust, and fair dealing.<sup>47</sup>

The emphasis on these mutual obligations in the employment relationship sits awkwardly with the special arrangements in law for strikes and lockouts. As the Court of Appeal said in *Unkovich v. Air New Zealand*: "[T]he law allows for hard bargaining, even the use of coercive tactics which might appear to be the antithesis of trust and confidence in a subsisting relationship of employment. . . . But, even within that altered relationship, the underlying obligations . . . survive, albeit perhaps modified."<sup>48</sup> This leaves employers and unions uncertain, however, as to how far they can go in negotiations without breaching those vague "underlying obligations."

The New Zealand courts might usefully study a judgment rendered by the U.S. Supreme Court in 1981. The Court stated:

Management must be free from the constraints of the bargaining process to the extent necessary for the running of a profitable business. It must also have some degree of certainty beforehand as to when it may proceed to reach decisions without fear of later evaluations labeling its conduct an unfair labor practice.<sup>49</sup>

Although Judge Richardson's notion of "mutual obligations" sounds even-handed, employers find it difficult, if not impossible, to pursue individual employees or former employees (but not unions) for breach of contract. By contrast, except where an employer has vanished, employees have ready access to a specialized legal system to pursue personal grievances against employers for alleged failure to meet their obligations.

The upshot is that the Employment Contracts Act reflects, or is at least interpreted by the Court to reflect, a view of the employment relationship as special and the employee as requiring special protection from employers—but not vice versa. The right of the employer to opt out of any of its provisions is absent, while the Act grants special privileges in the case of some strikes and lockouts, removing the application of tort law for breach of contract by the employee.

Therefore, a number of specific improvements should be made to the Employment Contracts Act: (1) the removal of the specialized jurisdiction of the Employment Court; (2) the clarification and re-balancing of the law governing personal grievances, especially dismissal; (3) the ability to opt out, by mutual agreement, of the personal grievance procedures and perhaps other provisions of the Act; (4) the application of tort law to strikes and lockouts;

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46. [1992] 1 E.R.N.Z. 711.

47. *Telecom* [1992] 1 E.R.N.Z. 711.

48. *Unkovich v. Air N.Z.* [1993] 1 E.R.N.Z. 526.

49. *First Nat'l Maintenance Corp. v. N.L.R.B.*, 452 U.S. 666, 101 S. Ct. 2573 (1981).

and (5) the clarification and limitation of the mutual obligations of employers and employees, particularly during strikes and lockouts.

Such changes would not amount to open slather for employers. Rather, they would move employment law further in the direction of the main body of contract law. By normalizing employment law they would further encourage a contractual and cooperative approach to employment relations, framed by the law of contract.

These proposals are not based on the assumption that all employers—or employees or unions—will behave well or sensibly. What is striking about much of the anecdotal evidence concerning some employers' alleged abuse of their employees is that such behavior, if verified, would be unlawful under tort law or other New Zealand statutes, such as Section 12 of the Fair Trading Act, the Illegal Contracts Act, and the New Zealand Bill of Rights Act. Any difficulty in obtaining redress relates more to poor information and difficulty in accessing the court process than to a lack of legal protections and safeguards.

#### SUMMARY

The Employment Contracts Act has been beneficial to the New Zealand economy, employers, and employees. It points to the basic reality that the employment relationship can be handled by contract law in much the same way as other contractual relationships. In such an environment, there exists no fundamental imbalance between the economic power—or indeed interests—of employers and employees.

In his first inaugural address, Thomas Jefferson stated his view on the sum of good government: “. . . a wise and frugal government, which shall restrain men from injuring one another, which shall leave them otherwise free to regulate their own pursuits of industry and improvement and shall not take from the mouth of labor the bread it has earned.”<sup>50</sup> The experience with the New Zealand Employment Contracts Act illustrates the wisdom of this view.

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50. SAMUEL ELIOT MORISON, *THE OXFORD ECONOMIC HISTORY OF THE AMERICAN PEOPLE* (1965).