

CHAPTER 5

LABOR ARBITRATION AND COLLECTIVE  
BARGAINING IN THE 1990s:  
AN ECONOMIC ANALYSIS

I. THE FUTURE OF COLLECTIVE BARGAINING AND ITS  
IMPLICATIONS FOR LABOR ARBITRATION

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The labor arbitration process derives its role from the unique system of collective bargaining that has evolved in the United States since the turn of the century. While, as others have noted,<sup>1</sup> the origins of labor arbitration can be traced back at least as far as the Anthracite Coal Commission of 1903 and the report of the Industrial Relations Commission of 1902, it was the choice of collective bargaining as the cornerstone of our national labor policy in 1935, the subsequent growth of union membership, and the endorsement of grievance arbitration by the War Labor Board that insured grievance arbitration a central role in the American industrial relations system. Indeed, it was the *particular form* of collective bargaining that evolved in the post 1930s that gave arbitration the prominent and vital role it plays in the collective bargaining system in the United States.

To understand the future of arbitration, therefore, we need to explore two aspects of the future of collective bargaining. First, how widespread will collective bargaining be? That is, will the

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<sup>1</sup>See Chamberlain & Kuhn, *Collective Bargaining*, 3d ed. (New York: McGraw-Hill, 1985), 143-145.

long period of decline in the percentage of the work force that is unionized continue and, more importantly, will the more recent decline in the absolute number of workers covered by collective bargaining continue?<sup>2</sup> Second, will the changes in the *nature* of collective bargaining that have been occurring in the first half of the 1980s alter the future role and prominence of grievance arbitration?

It is these aspects of collective bargaining that will be the central focus of my remarks. Though I will, at the conclusion, also trace specific implications for grievance arbitration, these will only be my own entries in what is sure to be a much larger debate within the profession. Thus, my look to the future is intended only to frame, rather than resolve, that debate.

Economists and industrial relations specialists should approach such questions with great trepidation given their demonstrated inability to predict the future at critical junctures in the history of industrial relations. There are two reasons why it is difficult to predict the future of collective bargaining based on past trends. The first is that union growth does not generally follow a smooth incremental path. Rather, new spurts in union growth tend to coincide with major shifts in (1) the economic and political and social environment, (2) changes in labor law or public policies, and (3) shifts in the strategies of unions. The second is that periods of significant turmoil or change often produce new sets of values, strategies, and practices that even evolve into new, accepted institutional arrangements. Since these are not simple incremental modifications of prior practices, they are difficult to envision or predict beforehand. Thus, economists in the early 1930s failed to anticipate the growth in union membership that erupted after passage of the National Labor Relations Act (NLRA) and the adoption of an industrial unionism strategy for organizing the mass production manufacturing industries. Similarly, no industrial relations experts predicted the rise of public sector unionism in the 1960s that coincided with the urban social crises, the enactment of President Kennedy's Executive Order 10988 in 1962 followed by similar and stronger bargaining legislation at the state level, and

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<sup>2</sup>As is well known, the percent of the labor force unionized has declined from a peak of approximately 35% in 1954 to less than 18% in 1985. Actual membership in unions and associations grew to a peak of 22.2 million in 1975 and has since declined to 18.3 million in 1984. See Troy & Sheffin, *Union Sourcebook* (West Orange, N.J.: Industrial Rel. Data Information Servs., 1985), 3-1.

the transformation of associations of public employees into full-fledged collective bargaining entities.

While the record of previous predictions should give solace to those who disagree with what follows, it also would be unrealistic to ignore the trends of the past decades and expect a *natural* correction or resurgence of union membership and collective bargaining to occur that will stimulate renewed demand for labor arbitration in the same fashion as it evolved in the New Deal system. Instead, to gain insight into the future we need to first understand both the forces behind the erosion of collective bargaining and union membership and the pressures that are producing changes in the institutional structure and practice of collective bargaining where it continues to exist.

For the past five years our research group has been examining the changes in collective bargaining that have been taking place and working toward the development of a stronger theoretical framework capable of both understanding why these changes are occurring and what they imply for the future of U.S. industrial relations. What follows is a general summary of our conclusions and an effort to explore their implications for the future of labor arbitration.<sup>3</sup>

#### *A Fundamental Transformation of Industrial Relations*

Our central conclusion is that the New Deal industrial relations system is undergoing a fundamental transition or transformation not only as a result of the changes in the economic and political environment of the early 1980s, but also in response to the gradual buildup since the 1960s of environmental pressures and to changes in managerial strategies. By a *fundamental* change we mean changes which alter the roles or established patterns of behavior of labor and management within and across three different tiers or levels of industrial relations activity within the firm: (1) at the workplace, (2) at the level of collective bargaining or personnel policy making and administration, and (3) at the

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<sup>3</sup>The material summarized in this paper reflects the results of a collaborative project involving faculty and graduate students from the Industrial Relations Section at MIT. It will not be possible to review the empirical evidence or the specific research projects that form the basis for the conclusions summarized in this paper. Wherever possible, however, I will cite previously published articles or books that contain more detailed analysis of the points highlighted here. The major findings, conclusions, and implications of our work are presented in Kochan, Katz, & McKersie, *The Transformation of American Industrial Relations* (New York: Basic Books, 1986).

highest level of strategic decision-making within management and labor organizations. Changes in established roles or patterns of behavior within each of these levels of activity are altering the basic principles and relationships that existed across these levels and that fit together to give the New Deal collective bargaining system its coherence and logic. We believe that we can best understand the dynamics of industrial relations practice by examining the practices within and across these levels. Thus, I will use this framework to review briefly the evolution of the New Deal system and the recent developments which challenge it.

### *The Evolution of the New Deal Model*

The passage of the NLRA signified the choice of the middle tier or level of our three-tiered framework as the central forum for joining and resolving the interests of management and labor. In return for preserving the rights of management to make strategic business decisions, workers and unions gained the right to negotiate over the *impacts* of those decisions on wages, hours, and other conditions of employment. At the workplace, management also retained the right to initiate action subject to the rights of workers to file a grievance to enforce management's obligations to adhere to the contract. As the provisions of bargaining agreements became more complex and detailed, grievance procedures and binding arbitration became tools used by unions and employers to develop uniformity and predictability in personnel administration. They also gave workers a channel for voicing their individual claims and problems on a day-to-day basis during the term of an agreement.

This model worked well from the 1930s through the 1960s because the principles and practices developed at each level of the system were well suited to the economic environment and to the strategic needs of management and labor. At the middle level, the collective bargaining process served to "take wages out of competition" as unions organized large portions of domestic product markets and standardized wages through a combination of centralized bargaining structures and/or pattern bargaining. By relying on a general wage policy that sought to tie wages to the long-term rate of growth in productivity and increases in the cost of living, unions were able to improve the relative wages of their members and share in the benefits of an expanding domestic economy. The annual improvement factor fashioned

by the United Automobile Workers was the clearest expression of the link between wages and economic growth. Thus, union strategies that increased wages through collective bargaining were compatible with their environment as long as markets continued to expand and productivity increased.

Achieving stability, predictability, and labor peace were central to the business strategies of American employers seeking to take advantage of these expanding market opportunities. At the workplace, adoption of grievance procedures ending in binding arbitration therefore served a crucial function in guaranteeing stability and labor peace during the term of the agreement. From management's perspective, the no-strike guarantee and grievance arbitration were intimately intertwined. These procedures likewise served the interests of workers and unions by replacing the arbitrary and often inconsistent or discriminatory practices of supervisors with more uniform and equitable specification of individual rights and responsibilities.

While the parties to thousands of different collective bargaining relationships adapted this general model to meet their specific needs and modified it in incremental ways from the 1940s through the 1970s, these adaptations and adjustments did not (with few exceptions) fundamentally alter or challenge the underlying principles of the system. As such, the roles of the parties at the workplace, collective bargaining, and the strategic levels of the system remained stable. Throughout this period, management maintained its essential rights to make strategic business decisions subject to their legal obligations to negotiate over wages, hours, and working conditions. Unions and companies continued to pursue wage policies that stressed comparability and standardization in order to minimize wage competition. The grievance procedure provided the means for adapting the terms of the agreement to changing conditions, to resolve differences over interpretation without resort to strikes, and to provide employees with a channel to question or challenge the administration of the contract.

#### *The Growth of a Nonunion Alternative Model*

Collective bargaining served as the major innovative force in industrial relations from the New Deal through at least the 1950s—extending well beyond the unionized sector by what was termed the “shock effect.” However, by the early 1960s a new

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nonunion model was beginning to emerge. Over the course of the next two decades, this model would grow and diffuse to the point that, by the 1980s, it would pose a major challenge to the New Deal collective bargaining system. This model emerged first in the newer growth industries among white-collar and professional employees, but then spread to capture a high proportion of the new jobs created in sectors and occupations that had been highly unionized in previous years. While this model evolved slowly and was modified through trial and error over the course of the 1960s and 1970s, its key features involved: (1) payment of wages that were competitive in the local labor market but lower than the standard union rate in the industry, (2) greater flexibility in the organization of work than is the case in typical labor agreements, (3) greater emphasis on individual and small group participation and communications, and (4) a stronger role for human resource management professionals at the strategic level of decision-making to both implement this new system and to take a proactive role in avoiding unionization. Interestingly, some of these nonunion firms developed extensive dispute resolution systems, some of which even featured grievance arbitration.

This approach was highly successful in stopping the growth in unionization among firms intent on doing so. For example, using data from a Conference Board survey, we found that unions organized only about 15 percent of new plants opened between 1975 and 1983 by firms that had at least some or all of their production employees unionized at the beginning of this period.<sup>4</sup> Furthermore, the risk of being unionized was reduced to less than one percent among firms that implemented the features of this model. As a result we estimated that the decline in union membership was twice as large in firms that adopted these policies compared with those that did not. Coinciding with the effects of these changing management strategies have been (and continue to be) structural shifts in the economy that further erode the base of unionism. Although it is difficult to provide an exact estimate of the separate or independent effects of structural (industry, occupational, regional, and demographic)

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<sup>4</sup>See Kochan, McKersie, & Chalykoff, *Corporate Strategy, Workplace Innovations, and Union Membership*, 39 *Indus. & Lab. Rel. Rev.* (forthcoming).

change, recent estimates suggest they account for between 40 and 60 percent of the decline in unionization since the 1950s.<sup>5</sup>

The culmination of these trends results in a situation in which unions are now located primarily in the oldest industries, the oldest firms competing in partially unionized industries, and the oldest facilities of partially unionized firms. Moreover, because collective bargaining continued in the 1970s to follow the patterns and wage formulas established in earlier years while the nonunion sector was growing, the union/nonunion wage differential widened—it expanded from an average of between 10 to 15 percent in the 1960s to an average of more than 20 percent in the 1970s.<sup>6</sup> These differentials were even larger for fringe benefits and for entry level wage rates.<sup>7</sup> Thus, the aggregate figures on private sector unionization mask the more serious situation implied by the recent trends and current distribution of union membership. Looking to the future, we expect union membership to continue for some time to come to be highly sensitive to both structural shifts in the economy and organizational restructuring and redeployment of investment dollars.

#### *Union-Management Responses in the 1980s*

While the expansion of the nonunion sector occurred gradually over the course of the 1960 to 1980 time period, it was not until the pressures of nonunion competition interacted with the deep recession of 1981–1982 and the changes in the political environment of the 1980s that significant changes occurred in collective bargaining, at the workplace, and at the strategic levels of industrial relations activity in unionized firms. Since these changes have been widely discussed elsewhere, in reviewing

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<sup>5</sup>See Farber, *The Extent of Unionism in the United States*, in *Challenges and Choices Facing American Labor*, ed. Thomas A. Kochan (Cambridge: MIT Press, 1985), 15–44; Dickens & Leonard, *Accounting for the Decline in Union Membership*, 38 *Indus. & Lab. Rel. Rev.* 323 (1985). New estimates, along with a comparison of estimates from previous studies, are provided in Dickens & Leonard, *Structural Changes in Unionization: 1973–81* (National Bureau of Econ. Research Working Paper No. 1882, April, 1986).

<sup>6</sup>Many studies have documented the expansion of the union/nonunion wage differential over the course of the 1970s. For a summary of the evidence see Flanagan, *Wage Concessions and Long Term Union Wage Flexibility*, 1 *Brookings Papers on Econ. Activity* 183 (1984). See also, Freeman & Medoff, *What Do Unions Do?* (New York: Basic Books, 1984), 52–54.

<sup>7</sup>For a review of the evidence on fringe benefits see Freeman & Medoff, *supra* note 6 at 61–64. For evidence on the union effects on entry level wages, see Verma, *Union and Nonunion Wages at the Firm Level: Combined Institutional and Econometric Analysis*, *J. Lab. Research* (forthcoming).

them here I will focus on the changes most important for consequences for the arbitration process.<sup>8</sup>

The most visible changes have occurred in the process and results of collective bargaining. New directions that began to appear in 1981 and that gained momentum in 1982 made the term "concession bargaining" part of our industrial relations vocabulary. These changes sparked a vigorous debate over whether these departures from the pre-1980 trends were merely temporary deviations or represented a more lasting structural shift in wage determination under collective bargaining.<sup>9</sup> Our position in this debate is that a structural shift *did* in fact occur and that it is most pronounced and will have its longest lasting effects in those bargaining relationships where both the environment and the institutional structure and process of negotiations have changed so that unions can no longer "take wages out of competition." The most significant changes in the structure and process of bargaining include: (1) decentralization of bargaining structures in a number of industries such as coal, steel, and trucking; (2) increased variability in wage settlements across firms that had previously been tied together by intraindustry or intraregion pattern bargaining; (3) reduced influence and control over negotiations by industrial relations professionals within management and increased influence of line managers and top executives; (4) more use of direct communications from management to rank and file workers; and (5) a reduction in the frequency and the economic returns to strikes.<sup>10</sup>

These changes in the structure and process of negotiations in turn produced a structural shift in the underlying model of wage determination. We can summarize the changes in the results of bargaining as follows: (1) the rate of wage growth under collective bargaining was reduced by between one to three percentage points per year below what it would have been had the settlement patterns of the 1960–1980 time period continued, (2) the biggest departures from the pre-1980 period occurred in those relationships in which bargaining was most centralized and

<sup>8</sup>For early reviews of these developments, see Katz, *Collective Bargaining in the 1982 Bargaining Round*, in *Challenges and Choices Facing American Labor*, ed. Thomas A. Kochan (Cambridge: MIT Press, 1984), 213–226; or Kochan & McKersie, *Collective Bargaining—Pressures for Change*, 24 *Sloan Mgmt. Rev.* 59 (Summer, 1983).

<sup>9</sup>For a sampling of the debate, see Freedman, *A Fundamental Change in Wage Bargaining*, 25 *Challenge* 14 (1982), and Dunlop, *Working Toward Consensus*, 25 *Challenge* 26 (1982).

<sup>10</sup>See Kochan & McKersie, *supra* note 8. A more complete discussion is provided in Chapter 5 in Kochan, Katz, & McKersie, *supra* note 3.

where pattern bargaining was most prevalent, and (3) major changes in work rules were demanded by management to increase flexibility and lower costs.<sup>11</sup> These changes are most likely to persist over time where the rise of nonunion competition from either domestic or international sources makes it difficult or impossible for collective bargaining to take wages out of competition.

Along with these visible changes in collective bargaining came intensified efforts at the workplace level of industrial relations to improve productivity and product quality through greater employee participation and incremental efforts to modify work rules in ways that increase managerial flexibility in the utilization of the work force. Although many union leaders remain skeptical about the managerial motives underlying the quality of work (QWL) movement, employee participation processes expanded in number and in scope in many union-management relationships. Not all of these, however, have survived or continued to expand to include larger numbers of workers in the bargaining unit or in the overall organization. Our conclusion, based on studies of a number of these processes,<sup>12</sup> is that the ones that are most likely to survive over time and make the most significant contribution to improving economic performance and employment security are ones in which (1) the participation process goes beyond narrow QWL or quality circle (QC) programs to address work rule and work organization issues that are significant barriers to improving productivity and quality, and (2) where cooperative efforts at the workplace are supported by policies and actions at the collective bargaining and strategic levels of decision-making which reinforce and support the trust these processes require.

The changes introduced by the most effective workplace experiments are especially important to understand for the future of arbitration since they directly challenge the centrality of the grievance procedure as the forum for worker voice and problem solving. Most of these processes start out with language stating that they will be separate from collective bargaining, will

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<sup>11</sup>Case study and aggregate evidence for these structural shifts are presented in Chapter 5 in Kochan, Katz, & McKersie, *supra* note 3. Econometric evidence using a longitudinal file of collective bargaining settlements is presented in Farber, Hirtle, Kochan, & Vroman, *Structural Shifts in Wage Determination Under Collective Bargaining: 1958-84* (Unpublished paper: May, 1986).

<sup>12</sup>See Kochan, Katz, & Mower, *Worker Participation and American Unions: Threat or Opportunity?* (Kalamazoo, Mich.: W.E. Upjohn Inst. for Employment Research, 1984).

not in any way change provisions or practices governed by the bargaining agreement, and will not interfere with the functioning of the grievance procedure. Yet we have consistently found that, over time, the most successful examples of workplace participation have expanded in scope to make changes in work organization and work rules that are covered in bargaining agreements and have introduced new means of solving problems or conflicts that heretofore could only have been channeled through the established grievance procedure.

Moreover, one of the positive effects of a successful QWL process is an improvement in the relationships among workers, supervisors, and managers. This often translates into a reduction in grievance rates. Finally, in its most advanced forms, as most clearly illustrated in the new Saturn agreement between General Motors and the United Automobile Workers, workplace reform can lead to a radical simplification in work rules and contractual provisions and a commitment by the parties to encourage consensus decision-making rather than rely on standard rules and enforcement procedures. While grievance procedures and binding arbitration are not eliminated in these new systems, the concern for flexibility and problem solving reduce the centrality of the grievance procedure and establish alternative forums and procedures for some of their traditional functions.<sup>13</sup>

Changes at the strategic level of decision-making are perhaps more limited—occurring primarily in bargaining relationships facing extreme economic pressures. Yet, where they have occurred, they represent equally fundamental departures from the principles and practices of the New Deal collective bargaining system. The common feature of changes at the strategic level is that industrial relations and human resource management considerations are now playing a more important role in strategic business decision-making. In nonunion or in union settings where unions are not powerful enough to influence the success or failure of business strategy decisions, line managers and human resource executives are central participants in decisions over issues such as investments, plant location, new technology, production sourcing, or service contracting. However, in situa-

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<sup>13</sup>See Cutcher-Gershenfeld, *New Patterns in the Resolution of Shop Floor Disputes*, Paper presented at the 1985 Annual Meeting of the Society of Professionals in Dispute Resolution, Boston, Massachusetts, October 27, 1985.

tions where unions can have a significant effect on the outcomes of these decisions or where unions perceive a major stake in these issues and are able to extract *quid pro quos* for cooperation at the workplace or in collective bargaining, union leaders are beginning to play a more active role at the strategic level of the firm.

These new roles vary considerably in the nature and degree of participation. Many go only as far as information sharing and consultation. In extreme crisis situations (most notably in airlines and trucking and in selected steel companies) more formal involvement is achieved through membership on boards of directors and employee stock ownership plans. Less visible, but increasingly common, are the negotiation of strategic bargains in which changes in traditional work rules or compensation arrangements are traded off for commitments to new investments in plant or equipment. Finally, a few unions and firms have begun to engage in joint strategic planning for new investments and the design of work systems in new or retrofitted facilities. The involvement of the United Automobile Workers in the planning of the Saturn organization illustrates this approach. Since these developments require breaking from the managerial premise that it is solely "management's job to manage" and from the business unionism principle that unions should avoid participating in managerial decisions for fear of being coopted or losing touch with their rank and file, they represent another example of the fundamental changes in collective bargaining and industrial relations that labor and management have been experimenting with over the first half of this decade.

The overriding conclusion from our research on the changes that have been taking place in industrial relations within unionized relationships is that it will be extremely difficult to return to the principles and practices that lent stability to the New Deal system in the pre-1980s. The increased exposure to global and domestic competition, the changing nature of technology in the office and the factory, the increased priority firms must give to flexibility in the use of human resources and to cooperation at the workplace to achieve this flexibility will all continue to induce changes in labor-management relations. These changes will include minimizing labor costs and linking cost increases to firms' specific economic conditions, pressing for greater flexibility and higher commitment and cooperation from their employ-

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ees, and better integrating human resource strategies to their underlying business strategies. Further, these changes will be interactive. In this context, nonunion firms and firms with only a minority of their blue-collar workers organized will either maintain or intensify their union avoidance efforts. On the other hand, more highly unionized firms that cannot achieve these changes through union avoidance will need to accept a *broader* union role at the strategic and the workplace levels in order to gain union and rank and file commitment to the human resource management and organizational principles needed to be competitive in today's world. Yet this will involve a narrower role for grievance arbitration. Finally, those firms and unions that try to return to the wage, workplace, and strategic level practices of the pre-1980s in settings where they are not protected from domestic or international competition will simply experience continued shrinkage in profitability and employment. In these sites arbitration will, of course, continue in its present form. But, as I detail later, the issues will become narrower and the tone more acrimonious.

#### *Recent Trends in Arbitration Case Loads*

In his recent paper presented to the midyear meetings of the National Academy of Arbitrators Jack Stieber noted that despite the decline in the percentage of the labor force that is unionized, the absolute number of labor arbitration cases filed with the American Arbitration Association (AAA) and the Federal Mediation and Conciliation Service (FMCS) has declined only slightly between 1978 and 1984.<sup>14</sup> Data provided from both the FMCS and the Detroit region of the AAA further suggest that private sector cases are declining both as a proportion of the total cases as well as in absolute numbers while the number of public sector cases has been increasing. A slightly different pattern in case loads has been experienced in the Boston regional office of the AAA. Again, total labor cases have declined only slightly between 1981 and 1985. However, while the number of private sector cases have basically held constant, public sector cases fell off approximately 20 to 30 percent in the wake of the tax limitations imposed in 1981 on local governments in Massachusetts.<sup>15</sup>

<sup>14</sup>Stieber, *The Future of Grievance Arbitration*, Lab. L.J. (June 1986), 366-71. The text of this paper is reprinted in Appendix E.

<sup>15</sup>Data provided by Tim Ahern, Boston Regional Office of the American Arbitration Association.

While the public sector trends in Massachusetts may be due to the unique circumstances of the state tax limitation (or they may provide a prediction of the effects of Gramm-Rudman-Hollings budget restrictions on future case loads in the federal sector), the relative stability of private sector cases again demonstrates that no large fall off in case load has yet been experienced.

Professor Stieber provides further interesting data on arbitration cases at United States Steel and Bethlehem Steel that show that despite similar employment declines of approximately 70 percent between 1969 and 1985, the number of grievance arbitration cases has held constant at United States Steel compared with a 43 percent decline in the number of cases at Bethlehem Steel. Apparently, the difference in the experience of these two companies continues today with United States Steel reporting a backlog of approximately 1,250 arbitration cases.<sup>16</sup> The difference in the experience of these two companies illustrates two important points to which I will return later in this paper. First, declines in unionized employment do not translate into immediate declines in the number of arbitration cases in situations where relations are highly adversarial. This has been and continues to be the case in the relationship between United States Steel and the United Steelworkers of America. Second, those cases that go to arbitration in these types of bargaining relationships are likely to be small tactical battles in a much larger strategic conflict over which arbitrators and the arbitration process are likely to have little influence. That is, the cases will be important for the individual grievants but are unlikely to alter the long-term evolution of the bargaining relationship. Indeed, the experience of United States Steel and the Steelworkers may be an example of the future of grievance arbitration in bargaining relationships that experience employment declines in adversarial settings.

Data from several case studies of workplace innovations we currently have underway illustrate how both the frequency of use and the role of grievance procedures change over time in settings where workplace innovations are in place. While the case data suggest that the number of grievances and arbitration cases generally decline, the magnitude and stability of the decline depend on whether or not management and labor representatives change their collective bargaining processes and their

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<sup>16</sup>*Bad Blood at Big Steel Could Lead to a Costly Strike*, Bus. Week, May 19, 1986, at 82.

strategic interactions in ways that reinforce the climate of trust and cooperation emanating from the workplace. The role of the grievance procedure also becomes more circumscribed as the parties experiment with a wider variety of forums for solving workplace problems and reduce their tactical use of the grievance procedure to solve their political problems.

The general conclusions that can be drawn from these limited data on arbitration cases are that (1) there has been a slight decline in the number of private sector arbitration cases filed and decided in recent years, however, the decline in cases is less than proportional to the decline in the number of private sector union members; (2) the more adversarial the bargaining relationship, the less the number of arbitration cases declines in response to union membership declines; and (3) the drop in private sector cases has been partially made up by a rise in public sector cases. Furthermore, where workplace innovations have been successful, grievance rates have fallen. While more comprehensive and disaggregated data are needed before any firm conclusions can be reached, the bottom line based on these data seems to be that the overall demand for grievance arbitration has declined only slightly in recent years.

#### *Implications for the Future Role of Arbitration*

These case statistics and our research suggest that the future of grievance arbitration will depend heavily on both the future scope and nature of the collective bargaining process and on how the arbitration profession chooses to adapt to these changes. As well, the future of arbitration depends on which of a number of possible scenarios dominate the future of collective bargaining. Several possible scenarios are outlined in the final chapter of our forthcoming book. Two will be discussed here in order to suggest how the future of collective bargaining will affect the role of arbitration. The first scenario assumes a continuation in the decline of union membership accompanied by an increase in the intensity of union-management conflict in those settings where unions perceive serious threats to their organizational security or survival, or both. The second assumes continued diffusion of the types of innovations in labor management relations discussed in this paper and a gradual movement toward their institutionalization as ongoing features of our industrial relations system. While we recognize that both of these

scenarios may occur in different bargaining relationships, the future of arbitration will be most affected by which scenario dominates.

If scenario one dominates—that is, union membership and the number of collective bargaining relationships continue their long-term decline—we can expect a slow, gradual, but considerably lagged decline in the demand for arbitration. To the extent that the decline in unionization coincides, as we anticipate, with an intensification of conflict and adversarialism, the lag in the fall off in the demand for arbitration will be longer. However, the importance and the contribution of arbitration to the bargaining relationships will diminish as the central issues and conflicts that will decide the eventual fate of the employment relationship are decided either in negotiations or by higher level strategic decisions of the parties. While the tactical battles of the parties may keep some arbitrators busy, their roles will be akin to rearranging the chairs on the deck of the Titanic. To stabilize the ship, much less enhance its ability to navigate through stormy seas, would require fundamental shifts in the strategic direction of the parties. Arbitration was never designed nor is it capable of performing this function.

It should be noted, however, that scenario one does not predict a continual decline in unionism below 10 percent.<sup>17</sup> Thus, the decline in the number of grievance cases should likewise not exceed more than 40 percent. Most likely the decline would be considerably less given the increases in conflict expected under this scenario. But while their case loads may hold up, experienced arbitrators are likely to become increasingly frustrated and discouraged with their roles as they see their impact on the parties and on the bargaining relationship continue to diminish. The frustration level is likely to be highest among arbitrators most committed to the clinical or problem-solving style and to the relationship-building functions of the arbitration process.

If, however, the alternative scenario gains momentum and the pace of innovations in collective bargaining expands and union membership either stabilizes or grows, the potential base for arbitration will likewise be stabilized or expanded. However, if this happens arbitration is not predestined to play as central a role in collective bargaining in the future as it did in the past. Instead, the needs of the parties for flexibility and adaptability

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<sup>17</sup>See Freeman & Medoff, *supra* note 6 at 242.

will most likely produce a varied set of processes for solving problems and resolving differences or conflicts at the workplace.<sup>18</sup> One can easily envision and predict an expansion in the demand for equally flexible third parties with multiple skills in problem solving, negotiations, mediation, strategic planning, and arbitration. Under this scenario, the eventual demand for arbitrators will depend on whether current and future members of the arbitration profession define their roles broadly enough to fill these multiple roles or leave the nonarbitration roles to the growing number of consultants and third parties trained in alternative dispute resolution (ADR) methods. The competition for these newly emerging roles is likely to be intense given the burgeoning supply of ADR enthusiasts, QWL facilitators, and consultants. Regardless of who fills these roles, the skills required and the values implicit in them sound remarkably consistent with the conception of dispute resolution favored by permanent umpires such as the late George Taylor and others who mixed mediation and arbitration as it seemed appropriate to the problem at hand.<sup>19</sup>

Finally, although a serious analysis of their prospects and implications lie beyond the scope of this paper, one can envision a variety of legislative and/or private developments which might expand the demand for arbitrator services beyond the traditional grievance arbitration arena. For example, legislation extending bargaining rights to public employees in the southern and western states that have not enacted such laws would very likely increase the demand for grievance arbitration and perhaps for interest arbitrators as well. Enactment of federal or state legislation requiring just cause prior to dismissal that incorporates a role for private arbitration as an alternative to adjudication of claims through a public agency or the courts would likewise provide a substantial increase in the demand for arbitration services. Enactment of labor law reform with a provision for binding arbitration of first contracts would similarly provide at least marginal growth in the demand for interest arbitration.

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<sup>18</sup>For a thorough discussion of the evolution and roles of these multiple forums at the workplace see Cutcher-Gershenfeld, *supra* note 13.

<sup>19</sup>A vivid picture of Taylor's commitment to this approach to the arbitration process is contained in *Early Years: Grievance Arbitration*, in *Industrial Peacemaker: George W. Taylor's Contribution to Collective Bargaining*, eds. Edward J. Shils, Walter J. Gershenfeld, Bernard Ingster, and William M. Weinberg (Philadelphia: University of Pa. Press, 1979), 29-48.

### Summary

The central message of our analysis is that if present trends in collective bargaining and union membership continue we will continue to see a slow erosion in the demand for arbitration, and a decline in its centrality and contribution to the performance of our industrial relations system. If the current innovative experiments expand, the base of collective bargaining may broaden but the demand for traditional forms of grievance arbitration will not expand as rapidly as will the demand for alternative problem-solving, planning, and conflict-resolution services. If the current and future generations of arbitrators are to match the contributions of their predecessors who established and built the profession, it is clear they will need to broaden and adapt their skills in ways that meet the contemporary needs of the parties. Those who adapt in this way will not only fulfill the legacy left to them by the giants of the past but will serve the industrial relations system in a way similar to the earlier generation by helping the parties to collective bargaining steer their way through this historic but exceedingly dangerous and uncertain transition.

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Thomas A. Kochan develops two themes in his paper: the future of collective bargaining and the demand for arbitrators in the 1990s. The rationale for combining these two labor markets is clear. The demand for labor arbitrators is closely tied to the number of workers under union contracts.

Following Kochan's paper I shall concentrate my remarks on the future demand for union workers. From my perspective Kochan makes three points: First, the decline in unionization is a major structural development related to increased competition in product and labor markets. Second, nonunion firms have become more aggressive in building an attractive alternative to

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unions. Third, the decline in unionization is a major structural development that is likely to continue into the future.

I have learned a good deal from reading Kochan's work on the topic, and I agree with the broad outline of his paper. I disagree, however, with the emphasis that he places on different causes of the union-in-decline hypothesis. I shall build upon these differences below in commenting on the Kochan paper. My discussion is organized under two headings: issues related to the functioning of labor markets *internal* to the firm and those issues related to the functioning of labor markets *external* to the firm.

### 1. The Role of Unions Within the Firm

A critical, perhaps the critical, feature of the Kochan study is his treatment of the rise of a "human resource" approach to labor relations in nonunion firms. My main reservation with his paper concerns his neglect of the central economic questions which his own analysis raises. The omission concerns the relative *efficiency*, as the term is used by economists, of the new human resource approach. Does the new approach or model dominate the old nonunion approach or model in terms of its ability to increase productivity and output in the firm? Do nonunion workers prefer the new to the old nonunion models? Is the new approach gaining market share, relative to the union approach or model, because of its relative efficiency for firms or workers, or both?

Although Kochan's approach is rooted in the labor relations literature, his model and findings can be translated into their economic model equivalents.

I would argue that one can legitimately understand Kochan as answering the above three equations in the following manner: First, the new approach was adopted because of its compatibility with the profit and goals of the nonunion firms. Second, practitioners of the new nonunion model recognize that in order to maximize profits they need to give workers a voice in their future. As a consequence, workers prefer the new model to the old. In addition, because the new model improves the economy's productivity and efficiency, while adding to nonpecuniary goals concerning the treatment of workers, these developments are seen as pluses from the perspective of society. Finally, a tentative case can be made that the new approach is gaining market share,

relative to the union approach, because of its appeal to workers as well as to firms.

*The Union Role in the Internal Labor Market*

In the past, evaluating labor relations systems in terms of their relative efficiency has been viewed by some observers as hostile to unions. But this certainly need not be the case, and increasingly economists, including myself, have adopted the standard economic methodology to evaluate labor relations systems.<sup>1</sup> The motivation for using economic analysis explicitly is driven by the dictates of market forces. Since labor and product markets are becoming more competitive, the efficiency issue can no longer be ignored.

The economic methodology is based on the simple observation that most labor markets do not work as they are described in the introductory textbooks. Most workers are employed by one firm for long periods of time. The employment relationship is sufficiently complex that it takes on the characteristics of its own internal labor market. Workers who invest in firm-specific training are no longer mobile. Similarly, workers have incomplete information. This loss of mobility and incomplete information is a source of market failure. Firms that require workers who have firm-specific training are also restricted in their options.

In economics jargon, management and workers are in a bilateral monopoly relationship with each other. The term bilateral monopoly does not require that the parties have equal bargaining power, only that both parties must deal with each other in a noncompetitive market framework.

Unions can be viewed as attempting to equalize bargaining power that is seen as tilting too far in favor of management. They accomplish this by restricting management's range of options through requiring seniority-based dismissals and promotions and by requiring the use of a neutral grievance procedure to resolve disputes. Arbitrators are the neutral agency charged with enforcing the explicit or implicit rules governing the unionized internal labor market.

In this model of the labor market, the collective bargaining framework with its use of neutral arbiters can have a potentially

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<sup>1</sup>See, for example, Williamson, Wachter, & Harris, *Understanding the Employment Relation: The Analysis of Idiosyncratic Exchange*, 6 Bell J. Econ. 250 (Spring, 1975).

positive impact on both workers and firms. Simply stated, in the presence of bilateral monopoly, unions can, depending upon their strategy, improve economic efficiency.

#### *The Nonunion Alternative*

Nonunion firms as well as union firms have internal labor markets. The difference between them involves the rules governing the decision-making process as well as the specific decisions reached in those markets.

As discussed by Kochan, during the 1960s, but picking up momentum in the 1970s, nonunion managements began to improve the attractiveness of their own internal labor markets. This was done by changing the rules to give workers more of a voice in the decision-making process and to accept some restrictions on management's freedom of action.

This change in labor relations within nonunion firms may have been motivated, in part, by a desire to remain nonunion. But the forces causing these changes have a broader base and cannot be written off as merely a defensive antiunion strategy. Unions are simply not a current threat to many nonunion firms and hence costly defensive tactics are not required. Consequently, in keeping with Kochan's findings, nonunion firms can be interpreted as adopting the human resource strategy because it is thought to increase the workers' productivity and the firms' profits.

The market failure problem within the internal labor market of firms is fundamental. It must be addressed. The system that provides the best answer to both firms and workers is likely to increase in size over time. In the Kochan framework, the nonunion alternative is clearly winning the decade.

#### *Unanswered Questions*

The above story concerning the nonunion alternative poses an important question which is only indirectly answered by Kochan's results. The unanswered question concerns the underlying appeal of the nonunion alternative. As I read the Kochan paper, he is at least implicitly suggesting an answer: Unions were the workers' preferred response to the labor relations problems of the 1930s, 1940s, and 1950s. But unions are not necessarily the preferred solution to the problems of the 1970s and 1980s.

The critical variable here is that the labor problems of the current decade may be quite different from those that existed 50 years ago. Also, it is possible to infer from Kochan's work that today's nonunion firms have learned to avoid the labor relations "mistakes" made by the now unionized firms prior to their unionization.

In addition, Kochan argues that unions were most successful and popular when they were able to secure relative wage increases without generating job losses. This could only be done in a period of increasing demand for the products of the union sector. But the period of product demand growth in most unionized firms ended by the 1960s. The employment instability in the union sector during the 1980s may be viewed as a negative by workers in their assessment of union and nonunion alternatives.

## **2. The External Labor Market and the Union Role**

The above comments have focused on issues internal to the firm. Although wages are only one part of that issue, they are not central. Yet a major impact of unions concerns their bargaining over wages and nonwage benefits. Economic analysis treats this problem differently from the internal labor market problem.

From the economists' perspective, the market failure found in internal labor markets is less of an issue in external labor markets. The ability of firms to act opportunistically in setting overall wages is limited. If a firm lowers the wages of all of its workers, it is less able to hire replacements or additional workers from the external labor market. In issues involving the external labor market, the world of Adam Smith is more important. External labor markets are simply much more competitive than internal labor markets.

### *Noncompeting Groups*

The ability of unions to raise wages above the competitive level is based on their ability, in Kochan's words, "to take wages out of competition." The antecedents of this go back to John Stuart Mill who wrote about the existence of "noncompeting groups." This point was later developed by Sir John Hicks and Alfred Marshall who described the factors which determined the degree of defenses supporting noncompeting groups.

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Certainly past economic regulatory practices that limited product market competition (such as in transportation and communications) or that restricted labor market competition (such as in construction) were key to the defenses at the boundaries. Also critical, especially in manufacturing, was the limited degree of international competition in earlier years.

In today's economy all of these defenses are being lowered, bringing wages back into competition. In addition, as discussed below, union wage practices during the 1970s might also have had an impact on this process. The higher the wage premium, the greater the profit potential for nonunion firms to compete with unionized firms in their product market. Also, the higher the premium, the greater the likelihood of capital substitution for labor.

### *The Recent History of Union Premiums*

In a recent study, Peter Linneman and I analyzed relative interindustry wages and employment over the period 1973 to 1984.<sup>2</sup> We found that union wage differentials increased significantly over that period. This follows two decades over which the union premiums remained largely unchanged. The magnitude of the 1973 to 1984 expansion in union wage premiums has been quite large, with premiums in some industries increasing by over 50 percent. The six sectors that had major increases in wage premiums were mining, durable manufacturing, nondurable manufacturing, transportation, wholesale trade, and retail trade. In each of these sectors the size of the premium increased by more than 10 percentage points. In construction, the premium increased significantly, but much of that increase was in the years immediately prior to 1973.<sup>3</sup>

These large, positive changes were not universal. The union wage premium remained largely unchanged from 1973 to 1984 in three sectors—government, finance, and services. Two of those sectors—finance and services—stand out as having both

<sup>2</sup>The methodology and results are described in Linneman & Wachter, *Rising Union Premiums and the Declining Boundaries Among Noncompeting Groups*, 76 *Papers & Proc. Am. Econ. A.* 103 (1986).

<sup>3</sup>There are several alternative methods for calculating the union wage premium. The most traditional is to choose a base group of all workers, union or nonunion, or alternatively, to choose a base group of nonunion workers. The base group used in the study is a weighted average where the various sectors are weighted according to their share of employment increases over the period. Sectors with declining employment are given a zero weight.

stable and relatively small premiums. In government, the premium was stable but large (over 20 percent).

#### *Union and Nonunion Employment*

These changes in wage premiums are closely related to changes in union employment in different industries. Our data on union employment by industry illustrate several important, but largely unappreciated, shifts in the profile of U.S. employment.

First, the decline in the share of employment in the goods-producing industries—durable manufacturing, construction, and mining—is solely located in the union sectors of those industries. Nonunion employment actually increased in each of these sectors. Only in nondurable manufacturing is the employment decline spread over both the union and nonunion sectors. This suggests that the so-called deindustrialization of America appears to be a union-specific phenomenon, at least at the one-digit level.

Second, the pattern in the goods-producing sectors is a more general phenomenon. In the service-producing sectors (i.e., transportation, retail trade, wholesale trade, finance, and services), union employment shares have also decreased with the exception of finance and services. On the other hand, nonunion employment has increased in every service-producing sector.

Third, the fact that union employment increased or remained unchanged in services and finance is important. Those were the only nongovernment sectors where union premiums remained unchanged or declined.

Fourth, we find that in nondurable manufacturing, transportation, and wholesale trade, more than one-half of the employment decline is explained by the increasing premiums. By size (as distinct from share) of impact, the largest negative premium effects are found in mining, transportation, and durable and nondurable manufacturing.

#### *Kochan's View of Relative Wages*

Kochan mentions these relative wage developments, but does not accord them much weight. But if relative wages have changed considerably, then one's perspective on changes in management strategy seems less puzzling. Management's attitude toward unions is certainly dependent on the size of union wage premiums, reflecting the perceived costs and bene-

fits of unionization. As relative union wages rose, management opposition to unions would also be expected to grow. In fact, management opposition did grow most rapidly during the 1970s when union wage premiums were increasing.

This does not suggest that relative wages are all that matter or even that they are the most important factor. It does suggest that, given the magnitude in the shift in relative wages and hence costs, important changes in collective bargaining could be expected.

### **3. The Demand for Arbitration**

As discussed by Kochan, the future demand for arbitrators will be significantly affected by two factors: their ability to carve out a role for themselves in nonunion markets and the future course of union employment.

Although the use of third-party arbitrators in the nonunion market has been restricted to a few areas, the future has greater potential. Nonunion managements, in posing an alternative to unionization, need to show their workers that they are willing to restrict their use of power in arbitrary or opportunistic ways. One possible way to do this is to buy into a third-party arbitration mode for dispute resolution. Workers in certain kinds of cases would be able to appeal to such neutral bodies for relief rather than appeal to the courts.

The evidence on union employment is less promising, although there are exceptions. In services and finance, as well as in the public sector, union employment is healthy and may expand in the future. In addition, to the extent that other sectors attempt to moderate their wage premiums (for example, through the use of two-tier wage structures), the number of arbitrable cases may increase.

### **4. Conclusion**

An interesting question is why union wage premiums increased throughout the 1970s and early 1980s. The cause of this increase is a puzzle to economists. One possible explanation is tied to the fact that the supply shocks of the 1970s meant declining real wages for the average worker and for society as a whole. Many unions, however, managed to win real wage increases through the collective bargaining process. The

increase in real wages in the union sector, coupled with a decrease in real wages elsewhere, resulted in an increase in the relative wage of union workers.

An unanswered question is whether unions and management would have agreed to those changes if they had known their potential impact on employment (from the union perspective) and on profits (from the management perspective). My guess is that the parties would have signed very different contracts if they had known *ex ante* what would develop *ex post*.

What are the implications of these results for the current period? One answer is "nothing." In the past, the parties in private sector collective bargaining have made little attempt to conduct the kind of economic analysis that has become standard in other areas. Note, for example, the difference in the treatment of sophisticated economic analysis in Title VII cases and in some interest-arbitrations in the public sector on the one hand and private sector collective bargaining on the other hand.

The use of economic evidence, however, may be in the process of changing. In part because of the success of unions in increasing premiums and the increase in the degree of competitiveness in unionized firms' labor and product market, the role of economic evidence in collective bargaining is likely to increase. In today's labor market it is difficult to talk about the future strategy of either unions or management without coming to grips with the question of relative wage premiums.