ABSTRACT

Over the last 50 years, many jurisdictions have seen increases in the level of employment protection law. At first glance one might assume that wrongful discharge laws and other forms of employment protection are good for workers. Theoretical work is ambiguous however, and empirical studies have found more sinister results. In many cases, by increasing the costs of letting workers go, employers become more reluctant to make new hires. This is shown in a variety of times and places, through various means. Additional work is needed, however, in both the theory and empirics of employment protection law literature.
For most of recent history in the United States and western Europe, the relationship between employer and employee went mostly unregulated. Workers and owners were assumed to each have equal bargaining power over the contracting of labor. Workers were free to leave a job while owners were free to fire laborers as they each saw fit. In an era of artisanal, high-skilled work, this arrangement made sense. Owners provided workers with job security not out of the kindness of their heart, but because training new workers in high-skill and small-scale production was prohibitively costly. This doctrine, known as employment-at-will (the will of either employee or owner to end the relationship) was carved into American case law in *Payne vs. Western and Atlantic Railroad* (1884). The Tennessee Supreme court ruled that firing for any reason was legal, famously stating that “All [employers] may dismiss their employees at will, be they many or few, for good cause, for bad cause, or even for cause morally wrong, without hereby being guilty of a legal wrong”. By and large, the pre-industrial experience was the same in Europe.

With the growth of industry in the 19th and early 20th century, however, the relationship between employee and owner changed. As businesses increased in scale, workers became increasingly specialized in their labor. Work became simplified and more repetitive, and the nature of job protection changed. Workers became substitutable, as less firm-specific human capital was required to perform a given task. At the same time, training new workers required fewer resources. These effects combined to drastically damage job security. As a result, a number of countervailing employment protection measures found their way into the American job market. [Although not directly applicable to employment protection laws, it is worth noting the rise trade unions in the United States; over the first half of the 20th century, union membership increased dramatically along with the industrialization of the economy. In many ways, unions achieved a leveling of the playing field by increasing job security as

1 A common misconception, Payne was actually not an employee of Western & Atlantic Railroad. Rather, he was a merchant who sued the railroad for adopting a policy of dismissal for anyone “who trades with L. Payne” (Hogler, 1989). Claiming the policy ruined his business, the court nonetheless ruled that the railroad had the right to fire no matter the cause.
well as increasing bargaining power of workers through collective bargaining.]

If pre-World War II employment protection could be attributed to the growth of unions, it must be recognized that union membership has largely receded in the postwar period. Instead, employment protection has been gained through court fiat and legislative action. Collectively, these actions constitute the literature on employment protection laws. Employment protection legislation (EPL), generally speaking, provides job security to those working. Counterintuitively, however, the laws are generally found to reduce aggregate employment. The overall effect on welfare then is ambiguous, and this is possibly the largest question the current literature hopes to answer.

This paper is going to review three major avenues of employment protection laws (EPLs for short), and the economic effects of such laws. First, however, some of the theoretical underpinnings used commonly will be presented. Then, the paper will discuss EPLs in the United States, focusing on impacts in the post-war period. Third, the paper will discuss EPL in the European Union (EU). Lastly, the paper will return to the United States to review the Americans with Disabilities Act (ADA). The paper will close with some thoughts on the future of EPL research; where more research is needed and some interesting (current) extensions to the literature.

I. Theoretical impacts of employment protection laws

Lazear (1990) is perhaps the most commonly cited paper in the theoretically modeling the effects of EPL, and is one of the earliest papers doing so. Lazear considers a 2 period model where a contract is signed in period 1 and work is performed in period 2. Without any constraints, the wage will settle at some market-clearing wage $W^*$. If a severance pay $Q$ is mandated in the case that the worker is let go before working in period 2 (this event occurs with probability $P$), then it is necessarily the case that the worker earns

$$ W' = W^* + Q $$

In Europe, union membership has declined as well, the process only being slower and with more lag.
The higher wage is attractive to workers and unattractive to employers. To return to equilibrium, workers will pay a fee to sign contracts until the after-fee wage is equal to the un-mandated wage (in expectation)

\[(2) \quad PW^* = -\text{Fee} + PW^* + (1-\text{P})Q.\]

or

\[(3) \quad \text{Fee} = Q.\]

Lazear thus finds that mandated employment insurance can be offset entirely by efficient bargaining. This main result has two implications. First of all, if workers in the real world really can bargain efficiently, then there may be a welfare gain from employment protection because of the reduction of risk on the parts of workers. On the other hand, a failure to efficiently bargain might lead to a reduction in welfare. A worker, for example, may simply not have wealth equal to Q, or may be unable to borrow in order to pay the fee to obtain work. If workers cannot pay a fee equal to Q for legal reasons or credit constraints, then involuntary unemployment is likely to occur; mandated severance can be thought of as a tax on employment, which comes with an associated dead-weight loss.

It is worth mentioning as well Blanchard and Katz (1997). The authors' paper works with matching models as a framework to test the effects of firing restrictions on employment. The authors note three possible effects: decreased firing and hiring, decreases in productivity (because employees are kept on longer than they would be otherwise), and lastly that workers already hired have increased bargaining power, leading to higher wages. The authors conclude that the net welfare effects are ambiguous. If decreased productivity is accounted for with decreased wages, then (again, as in Lazear, 1990) aggregate employment might not be affected. If workers are willing to take lower wages to gain employment protection, overall welfare may be higher.

II. Exceptions to Employment-At-Will in The United States

Starting in the early 1970's, state courts began adopting exceptions to the longstanding doctrine
of employment-at-will. Adopted state-by-state, these exceptions fit into three categories.

Public Policy Exception

First established in the state of California in 1959, the public policy exception is today the most widely accepted exception, being law in one form or another in 43 of 50 states (Muhl, 2001). In the case of Peterman Vs. The International Board of Teamsters, Peterman (an employee) was instructed to give false information when subpoenaed for an investigation into the actions of the teamsters\(^3\). Later cases broadened the scope of the public policy exception (see Palameteer v. International Harvester Company\(^4\)). In general the doctrine prevents employers from firing workers for any action that goes against public policy.

Implied-Contract Exception

The implied-contract exception is recognized in 41 states, making it almost as widely accepted as the public policy exception. Most commonly cited is the formative case of Toussaint v. Blue Cross Blue Shield of Michigan\(^5\). The exception is defined broadly to protect employee from dismissal for bad cause in the case where it can be implied that the firm promised to dismiss only for good cause. Although exact interpretation varies from state to state, the implied-contract exception has proven quite robust. Expectations of continued employment have been found to be implied simply through seniority, a history of promotions, or even industry practices (see Pugh v. See's Candies).

The Good Faith Exception

Lastly, the good-faith exception prevents dismissal without just cause. Perhaps the most

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\(^3\) Peterman was hired by the Teamsters Union as a business agent. During an investigation into teamster corruption, Peterman was called to testify in front of the Assembly Interim Committee on Governmental Efficiency and Economy. Peterman refused the directives of his employer to lie, and was promptly fired the day after giving his testimony. The California appellate court stated that “public policy”, loosely defined, covered any action with “tendency to be injurious to the public or against the public good”.

\(^4\) The Illinois court rejected the “mutuality theory” of employment which held that employee's right to end employment put them on equal footing with employers. The majority opinion stated that public policy “strike[s] at the heart of a local citizen's rights … and responsibilities”.

\(^5\) Blue Cross' employee manual of company policy stated that management intended only to dismiss for “just cause”. The appellate court of Michigan ruled that this created an “implied-contract”, even though the company never explicitly told that he could be fired only for just cause. This has had a large impact on the writing of employee manuals, in an attempt not to create any implied-contract with employees.
sweeping of exceptions, the exception generally protects employees from being fired without “just cause” (economic necessity or poor performance). The case of *Fortune v. National Cash Register Company* ruled that it was illegal to fire an employee before an employee was due to collect commissions.\(^6\)

Taken together, the three major exceptions can be thought of as added expected firing costs, if an employer thinks that there is some positive probability that a costly lawsuit will ensue. When a firm decides that it wants to fire an employee, it may nonetheless be unable to do so because of one (or more) of the exception discussed. In studying whether or not aggregate employment was reduced by the adoption of any exception, the variation in timing serves as a great benefit to researchers. The fifty different states serve as a natural quasi-experiment, helping to control for natural variation of employment over the period in question (the 1970's to 1990's) as well as the different regions, and any other unobserved characteristics.

*Dertouzos & Karoly (1992)*

Dertouzos and Karoly do some of the earliest work in evaluating state-level anti-discrimination law. In their book *Labor-Market Responses to Employer Liability*, the authors devote a section to the direct and indirect costs of employment protection laws\(^7\). The authors find extremely strong results, concluding that adoption of the most liberal tort versions of can cause a reduction in aggregate employment of “2 to 5 percent” (page 64). Later authors, discussed shortly, improve upon these early findings, although exactly how effects of such a strong magnitude are found remains unclear.

*Autor, Donohue and Schwab (2006)*

The authors here undertake perhaps the most comprehensive and robust estimation of the effects of EPL on employment rates. The authors relay on Lazear (1990) for their theory. They hypothesize

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6 In the case at hand, the employee was let go, but asked to stay on in order to help with a pending sale. After the sale was made, the plaintiff (Fortune) was offered 75 percent of his commissions due. He sued, and won 100 percent of back pay. The court found that the plaintiff had been denied the full “benefit of his bargain”.

7 Much of the book is actually spent trying to explain employment protection introduction to a state, based on state characteristics. Given that the literature always takes this occurrence as a random event, the authors makes a very important critique!
that increases in wrongful discharge laws have increased expected costs associated with firing employees. Given frictions in the economy, the authors conclude this is likely to reduce aggregate employment.

The timing of implementation is important, and the authors decide in their model specification to use the two years prior to adoption as the “pre period” and the period 13 to 36 months after adoption as the “post period”, allowing for a year of adjustment\(^8\). The basic model is given by:

\[
\ln(\text{employment}) = \alpha + \beta_1 \text{Treat}_{st} + \beta_2 \text{Post}_{st} + \beta_3 \text{Treat}_{st} \text{Post}_{st} + \epsilon_{st}
\]

Where the coefficient of interest is \(\beta_3\), the difference between pre and post rates. Autor, et. al. run the regression separately for men and for women to see if the effects are felt differently between genders. The implied-contract exception leads to significantly lower employment for both men and women, while the signs for the good-faith and public-policy are mixed (and never significant). When the authors regress the log of hourly wage on the same data, the results are all mixed and insignificant. This finding is very important. There may be power in the argument of sticky-wages, insofar as changes in EPLs (which can be thought of as a sort of mandated benefit to not be wrongly discharged) lead to changes in employment but not in hourly wages.


David Autor's 2003 paper in *JLE* analyses a different dependent variable affected by exceptions to employment-at-will. In his discussion of EPL, Autor notes that the implied-contract exception makes it much more difficult to fire employees. So, for workers that are easily substitutable with each other, a firm may use a temp agency in order to easily let go of that employee if the firm should wish. Autor notes that firms generally hire employees with different levels of firm-specific human capital for different tasks. For example, a receptionist is unlikely to very specialized to his or her specific employer; the nature of receptionist work is general and doesn't greatly change depending what firm

\(^{8}\) It's ambiguous exactly when the law comes into effect, given that these exceptions often arise out of court cases. To chose timing, the authors use the first major appellate-court decision. This matches with others' assessment in the court literature (see Morriss, 1995).
the receptionist is working at. Moreover, a receptionist let go is easily replaced. A computer
programmer, on the other hand, is likely to have lots of firm-specific human capital\(^9\). Their work is
extremely firm-specific. Such an employee cannot be readily converted into temp, because suddenly
losing the employee might be very costly to the firm.

The author regresses temp employment rates in states over time on common law exceptions,
using employment and an index of labor force demographics as controls:

\[
\ln(THS_{jt}) = \alpha + \delta \cdot (\text{common law exception}_{jt}) + \lambda \cdot (\ln \text{nonfarm emp}_{jt}) \]
\[
+ \zeta \cdot (\text{Lab force dem}_{jt}) + \mu_j \text{ (state dummy)} + \tau_t \text{ (year dummy)} + \epsilon_{jt} \text{ (error)}
\]

The author makes the assumption that one may treat the adoption of exceptions as random\(^{10}\), and that
adoption in one state didn't have any spillover effects to other states.

The findings are consistent with the theoretical predictions. Because temporary help services
can't work around the public-policy or good-faith exceptions, they're expected to have null effects on
employment. Indeed, regressions find significantly positive results for the adoption of the implied-
contract exception (causes an increase in temp services), while the signs are mixed and insignificantly
measured for the good-faith and public-policy exceptions. The average effect of implied-contract
implementation is not small; the reported coefficient on delta is .137, meaning that the implied-contract
exception leads to an almost 14% increase in temp employment. Autor concludes that the welfare
effects are ambiguous, however, as calculating the tradeoff between those harmed and those benefited
is extremely difficult.

It's worth noting that not all anti-discrimination law comes at the state level. Donohue and

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\(^9\) There are exceptions to this, most notably the use of “permatemps” by many companies (including computer
programmers in Silicon Valley). In fact, Microsoft settled out of court in 2000 when several thousand temporary
enployees sued, claiming that they were in fact being “recycled” (fired and then rehired to avoid pension and other
liabilities). For more information see *Vizzaino v. Microsoft*.

\(^{10}\) This assumption may be a stretch (see Dertouzos & Karoly, 1992). It could be the case that lower employment makes
lawmakers more likely to enact employment protections, as a sort of knee-jerk response to enact popular policy.
However, given 1) the lag in implementation and 2) the fact that many of these exceptions were introduced via court
cases, it's unlikely that the assumptions made are too strong to be realistic.
Heckman (1991) address this in an earlier paper. However, it's much more difficult to examine the country as a whole, because there aren't any meaningful controls. In the cases of state-level EPL, the other 49 states can act as controls for a given state moving in or out of a specific doctrine.

III. Employment Protection in Europe

In Europe, employment protection legislation developed around roughly the same time as in the United States (the post-war period, generally). However, there are key differences. First of all, worker protections are generally stronger in Europe than in the United States. Secondly, there is much greater variation in worker protections within Europe, when comparing different countries. An excellent summary is provided by Kuhn (2000)\textsuperscript{11}. For example, in the United States, employers do not need to justify firings through economic necessity, unlike in Germany, France, and the Netherlands. And although no termination notice is required in the United States, some notice is required in every country surveyed (from as little as a week for low-seniority, young workers in the Netherlands to up to 9 months for some in Belgium). The variation in policies creates a perfect setting for testing what the costs of adopting employment protection really are.

Blanchard and Wolfers (2000)

The authors do a very good job explaining “Eurosclerosis”- a term coined in reference to the sclerotic labor markets that constituted many western European countries during the 1970's and 1980's. The authors identify and bring together two different popular explanations to explain the lessened rates of hiring and job creation over the 1970's-1990's. One central concept is that of institutions- the legal and bureaucratic systems set up to ensure workers are given adequate notice, severance, etc. during times of worker displacement. From previous work (Lazear, 1990), it's been shown that adding firing costs can lead to reductions in both firing and hiring- thus a sclerotic job market. Another important idea the authors touch on, however, is the addition of aggregate shocks to the economies over the

\textsuperscript{11} A chart on pages 56-59 shows, at a glance, major similarities and differences within some major countries, including the United States and many countries that make up the European Union.
period of interest\textsuperscript{12}. Specifically, institutions and shocks interact to cause more damage together than they would cause apart. Aggregate shocks often require large changes in business practices at the firm level. However, institutions hamper firing- which in turn hampers hiring- so firms are least capable of adjusting to new economic reality. Although the authors' conclusions are overly optimistic\textsuperscript{13} (especially in the face of the latest global recession), their model nonetheless accurately predicts how changes in institutions within the European Union led to changes in aggregate employment. Blanchard and Wolfers (2000) is not, at its core, much different than previous work by Nickell (1997). It's just that the authors now have a superior dataset\textsuperscript{14}.

\textit{Bentolila and Bertola} (1990)

Bentolila and Bertola provide a somewhat different perspective on EPL. It's worth mentioning because the authors show that it is possible for general welfare to be higher under a sclerotic regime of high firing costs. Using a competitive model of firms and workers, the authors are able to produce a “ratcheting effect” under very reasonable assumptions. By assuming that firms discount future gains and losses, the authors demonstrate how marginal workers are brought on during good times; the firm knows that it might be over-hiring, but discounts away the high costs associated with firing marginal workers. When push comes to shove, however, the high firing costs then actually prevent worker displacement. The result is employment “ratcheted up” by EPL. Higher employment rates, in them of themselves, do not imply increased welfare. It's likely the case that employment over the frictionless levels lead to decreased wages. If workers are very risk-averse, however, they may collectively prefer somewhat smaller wages in order to safeguard their employment.

Although the authors admit that their work is only in partial equilibrium, and thus may not be a

\textsuperscript{12} The authors keep most of the discussion centered around the run-up in oil prices in the 1970's, including the 1973 Oil Embargo which affected European countries to different degrees.

\textsuperscript{13} The authors claim that “the future looks bright” for Europe. By assuming favorable macroeconomic conditions and an absence of future shocks- a terrible assumption- most of the problems stemming from a sclerotic labor market (worker mismatch, over or under hiring in certain sectors, for example) will \textit{eventually} work their way through the economy.

\textsuperscript{14} Blanchard and Wolfers also make some slight changes to their model specification. For earlier work that substantively the same, see Nickell (1997).
perfect model of the real economy, the results are important philosophically. If, from a policy standpoint, we are willing to accept depressed corporate profits, the gains of keeping employed even in bad times may result in a net welfare increase. If one cares more about workers than owners, and if workers are sufficiently risk-averse, then “Eurosclerosis” may not really be so bad.


In more recent work, Blanchard takes on a much more conciliatory tone in discussing the future of Europe. According to the author, the successes of Europe in the post-war period can be attributable to “playing catch-up”; that is, adopting superior technology from the rest of the world and enjoying comfortable gains in output\(^1\). However, further gains require improvements in innovation. Noting that in the very recent future, union membership has dropped in many European countries, Blanchard makes the case that innovation and deregulation are primed in the economy. His argument lies in that unions are likely to have less bargaining power, in setting wages as well as within the political economy. If businesses are able to loosen laws surrounding EPL, then labor markets can be made more efficient and productive. This relationship is brought into question by more recent research (see Acharya, Baghai, and Subramanian, 2010\(^\text{16}\)). So, Blanchard makes a weak case, especially in light of the very recent history within the Euro zone.

IV. The Americans With Disabilities Act (1990)

In 1990, George H. W. Bush signed into law the Americans With Disabilities Act (ADA). The law makes it illegal to discriminate in hiring, promoting, compensating, or firing an employee based on a disability\(^1\). Passage of the act was overwhelmingly popular, although some business groups spoke out against the ADA as introducing prohibitive costs to small business.

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15 Also known as “capital-deepening” in the literature of economic development.
16 The Acharya, et. al. examine how changes in worker dismissal laws affect innovation (measured in patents received)
17 There was, at time of passage, and still is, some debate as to what it means to be disabled. Congress defined it as “a physical or mental disability that prevented a major life activity”. Owning to the continued confusion over the definition of “major life activity”, the 2008 ADA Amendments Act provided further directives, in fact enumerating a (non-exhaustive) list of major-life activities.
The ADA has several provisions, but the most important implications arise from the firing provision- that firms may not discriminate in firing based on disability- and the equal pay provision- that firms cannot discriminate on wages based on disability. By outlawing firing of individuals for being disabled, the expected firing costs associated with disabled workers increase dramatically\textsuperscript{18}. By mandating equal pay, involuntary unemployment may be created if the mandated wage is above the disabled workers reservation wage, but the unmandated wage is below. Disabled workers are a relatively small share of the workforce, so the economic impact of the ADA has received less study than more general EPL in the United States and Europe. Still, two papers by Acemoglu and Angrist (2001) and DeLeire (2000) demonstrate clearly the unintended consequences of the ADA.

\textit{DeLeire (2000)}

The author, without theoretical underpinnings, simply makes the case intuitively that the ADA increases expected firing costs associated with disabled workers. Over the whole cycle of employment, it thus becomes more expensive in expectation to hire disabled workers. DeLeire constructs a simple probit model based on disability status, year, and an interaction between the two\textsuperscript{19}:

\begin{equation}
\text{Probability(employed)} = \alpha + \delta \times \text{(Disabled?)} + \lambda \times \text{(Post 1989?)} \\
+ \zeta \times \text{(Disabled x Post 1989?)} + \epsilon_{jt} \quad \text{(error)}
\end{equation}

The results are large and significant for all three coefficients. Not surprisingly, $\delta$ is reported to be around -0.3, meaning that disabled people are 30 percent less likely to work. $\lambda$ is also negative, owing to the fact that there was a recession in the early part of the 1990's. The real coefficient of interest, $\zeta$, is reported to be -.072, meaning that disabled persons were 7.2\% less likely to be working after the passage of the ADA. Wages are not affected very drastically. This replicates findings in the United States and Europe- EPL having a much stronger effect on employment than wage- and also may be

\textsuperscript{18} As Acemoglu and Angrist (2003) note, it's even possible for non-disabled workers to sue, claiming disability (which is not as exactly defined as workers statuses such as gender or age). Further, even if the plaintiff loses, the court costs may still be crippling to a small or medium sized firm.

\textsuperscript{19} The author doesn't ever explicitly give the form of the probit estimation, so this is a recreation based on tables from the paper.
related to the fact that disabled persons were, *ex ante*, already earning far less than non-disabled workers on average.

*Acemoglu and Angrist (2001)*

The authors improve upon the DeLeire paper by incorporating a standard competitive labor market with two different inputs of interest, those being disabled workers (D) and non-disabled workers (L). Both disabled and non disabled workers can now sue, claiming discrimination on the grounds of a disability. It is assumed that, from the perspective of the employer, this happens randomly at different exogenous probabilities for disabled workers and non-disabled workers. Further, the reasonable accommodation clause introduces the possibility for adjustment costs for hiring workers. Because this is a competitive market, workers will each be paid their marginal products of labor (see figure below):

\[
\frac{\partial F(L, e \cdot D)}{\partial L} = w_a + \beta \cdot s \cdot f_a - [1 - \beta \cdot (1 - s)] \cdot h_a,
\]

\[
\frac{\partial F(L, e \cdot D)}{\partial D} = w_d + \beta \cdot s \cdot f_d - [1 - \beta \cdot (1 - s)] \cdot h_d + c.
\]

where c is net costs of accommodation, h\(_a\) and h\(_d\) are hiring costs for non-disabled and disabled workers respectively, beta is the discount rate over time, e measures the relative efficiency of disabled workers, and \(f_a\) and \(f_d\) are the associated partials of \(F(L, e \cdot D)\). The authors use this main result to generate a number of important predictions (summarizing pages 923-925):

1. As h\(_d\) is a hiring subsidy, it is possible for the ADA to raise both employment and wages of disabled workers.
2. The ADA has not, then, had a seemingly large impact on h\(_d\). More than raising the costs of *not hiring* (through threats of lawsuit for being passed over for a job), the ADA has raised the costs of hiring (for wrongful dismissal related to a disability).
3. Equal pay provision may create involuntary unemployment if disabled workers are less efficient (e < 1) than non-disabled workers.
4. ADA may have spillover effects to the non-disabled workers, in both wages and employment levels.
For their data, Acemoglu and Angrist use data collected from the Current Population Survey, March 1988-1997. From wages and hours worked data, the authors find sharp reductions for disabled men and women after passage of the ADA. Most telling of all is the fact that the number of disabled workers receiving disability income from the government rose roughly a third between from 1988 to 1996, after passage of the ADA.

In sum, the Americans with Disabilities Act should be viewed as a misguided attempt to help disabled workers. A key problem with the ADA is exactly how it's structured to allow lawsuits. Lawsuits brought by disabled workers who feel that they've been discriminated against hiring are relatively unlikely, compared to lawsuits over wrongful wrongful displacement or failure to provide reasonable accommodation. The latter are likely to make employers more wary of hiring disabled workers, while the former should increase the hiring of disabled workers. If subsequent amendments to the ADA are passed (major amendments were passed in 2008), they should encourage the former at the cost of the latter.

V. Conclusion

We find that employment protection has generally negative results for aggregate employment. This result is somewhat paradoxical; policy-makers' actions to protect employment end up doing the opposite. As perhaps in the case of rent (or more generally, price) controls, frictions are introduced which cannot be entirely undone through efficient bargaining. Exactly how efficient bargaining fails hasn't been entirely explained. It may due to the sticky-wage hypothesis, credit-constraints amongst workers, some combination of the two (or even some other yet to be discovered reason). Either way, this creates inefficiency and, more likely than not, welfare losses for average workers. It is difficult to find if there is research into the popularity of EPLs, but anecdotal evidence appears to validate their popularity. Unfortunately, those that benefit from EPL are easy to identify (current workers), while those hurt are difficult to see (those who would have been hired in the future, but now aren't). This
makes it difficult, given the political economy, to equate marginal benefits to marginal damages. Better educating policy-makers may not be adequate to correct imbalances, if the repeal of EPLs are unpopular with a given electorate. Instead, educating the public, or putting the decision in the hands of those not elected may be the only solution if employment protection should be reduced. Of course, if it's decided that employment protection must stand for the sake of some, then efficiency losses will simply have to be tolerated.

Future Research

There are several areas where employment protection research is either under-researched, or is likely to gain prominence in the near future.

A current, and increasingly important extension of the EPL literature will be the issue of age discrimination in the workplace. In the case of high-skill labor, there is often a need for relatively current skills. In the United States, the combination of an aging workforce and need for newer skills creates a “perfect storm” for age discrimination against older workers. In the near future, the composition of the US workforce is likely to become more skewed towards older workers. The proportion of workers age 16-24, as well as the proportion of those aged 25-39 are both expected to decline. The greatest increase, on the other hand, will be those aged 65 and older (Toossi, 55-56).

Previous work within the field of EPL does exist. Johnson & Neumark (1997) study self-reports of age discrimination of older workers. However, they use a much older cohort, specifically men who were older between 1966 and 1980. Shuster and Miller (1984) review a bevy of court cases involving claims of age discrimination, but again are looking at an older data set. The period of interest is more current, as only recently has the graying of the workforce become so prominent. If data for the US is still forthcoming, authors might be interested to look at the case of those European countries that have already gone through substantial aging in their workforce composition.

Another area of interest is in the outfall from the current financial crisis. The finances of many countries have been called into question, in some cases necessitating foreign intervention into credit
markets. In the case of Greece, which was given loans from the International Monetary Fund, financial help was given contingent on certain labor-market reformations. Although Greece's reforms don't directly alter EPL in the country, there may be pressure (on Greece or other countries in the EU) to reduce employment protections into order to ultimately increase employment and aggregate output. I have not yet seen empirical work looking at any affects of the financial crisis on EPL (or visa versa), but there is certain to be strong interest among policy-makers if there is a causal effect going either way.

Finally, developing countries have been largely ignored in the literature. Most likely this is because developing countries have nowhere near the employment protection that is granted in the United States and Europe. In that sense, there may be little to study. The theory still needs to be developed to predict how EPLs will change as countries develop. If workers become higher skill, then development of employment protection might come in the same way it developed in the US over the 20th century. On the other hand, governments may recognize the sclerotic effect that EPL has on hiring and firing. Governments then may work to hold back EPL so that firms can maintain agility to respond to changes in aggregate demand. Developing countries are often pitted in competition against one another to keep wages down. This will probably also work to keep employment protection to a minimum.

Empirically, developing countries can offer natural experiments, however, if EPL changes during the course of development. This would be analogous to much of the research done in the EPL literature pertaining to the United States.
Worked Cited


Blanchard, Olivier and Lawrence Katz. “What We Know and Do Not Know About The Natural Rate of Unemployment”. *Journal of Economic Perspectives*, volume 11(no 1).


Figures

Figure 1; count of states over time having adopted various exceptions to employment-at-will. From Autor (2003), page 5.

Figure 2; ratio of disabled persons employment rate to non-disabled persons employment rate, 10 years 1986-1995. From DeLeire (2000).