

About Suffering and Law in the Labour Market

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In this article, I begin with the question, what should be the agenda of political economy and of law and economics? I argue that the agenda should include humanistic economic questions, such as how to protect weak workers and how to minimize suffering. Humanistic economics is especially important when we discuss legal questions. Then, I discuss this article's central question: How should power gaps be handled in the labour market? I examine the various answers to this question and discuss the fundamental controversies in political economy. In particular, I examine the solution of a free market vis-à-vis the social-democratic solutions of labour legislation—especially the minimum wage law, encouragement of organized labour, and transfer of wealth through tax laws.

*Hunger allows no choice
To the citizen or the police;
W. H. Auden¹*

*In its majestic equality, the law forbids rich and poor alike to sleep under bridges,
beg in the streets, and steal their loaves of bread.
Anatole France²*

People are competing with each other for jobs. Some of them do not have special skills. People may find themselves forced to choose between a starvation-wage job, i.e., wages insufficient to provide the ordinary necessities of life (but still keeps them from starvation), and real starvation. They may find themselves subject to abuse and degrading treatment at work while facing the alternative of sleeping on the street. How should the state law handle this? How should we approach this problem? What do the different bodies of knowledge have to say about this, and which of them should be consulted?

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1. W.H. Auden, *September 1, 1939*, POETS, <https://poets.org/poem/september-1-1939> (last visited Nov. 23, 2020).

2. ANATOLE FRANCE, *LE LYS ROUGE* (1894). “*la majestueuse égalité des lois, qui interdit au riche comme au pauvre de coucher sous les ponts, de mendier dans les rues et de voler du pain.*”

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I. INTRODUCTION

The main question discussed in this article is, how should the law deal with the power gaps between the employer and employee in the capitalist labour market? In particular, I focus on the low wage problem of workers. I present two polar remedial strategies. The first is non-intervention beyond the enforcement of contracts, as opposed to intervention through labour legislation and/or encouragement of organized labour and/or wealth transfers that enrich the poor through taxation and distribution of benefits such as negative income tax or social services. The second is a Marxist solution for abolishing private property.

The question I discuss is very close to the following questions: How to protect the weak worker? How to regulate the labour market? How to divide work? What should be the limits of the free market? The key significance of this article is the presentation of major disputes in political economy, while sometimes translating one theory into the language of another theory. Many of the economic disputes I present are those that are overlooked by

economics schools.

In addition to presenting the disagreements, I present a series of advisory lessons, such as a recommendation to encourage trade unions and to recognize the significant right to a solidarity strike (a second-order strike), which can surprisingly increase distributive justice and the efficiency of the division of labour.

A. Roadmap of the Article

The article is structured as follows: In Section B, I discuss what the agenda of political economy and of law and economics should be, and I support a humanist economics agenda that investigates how to minimize human suffering (Section I.B). I discuss how to approach the question—as an imaginary dialogue between a socialist and a capitalist equipped with their best arguments (Section I.C); I also investigate what a capitalist labour market is (Section I.D). Next in Part II, I analyse the basic game taught in economics schools, a game where one field owner employs many workers. I discuss what exploitation is and how the workers in the aforementioned game are exploited. I present some potential power gaps in the labour market; I question how to deal with these power gaps in particular relation to low wages.

Then in Part III, I present the capitalist argument that the state should not interfere in the private labour market beyond contract enforcement, fraud prevention, theft prevention, etc., and that labour relations should be based on the principle of the freedom of contract (Section II.A). I present the various justifications for this: efficiency, liberty, and fairness (Section III.B). The primary rationale is that if both parties enter into a voluntary deal, it shows that they both expect to gain from the deal, so they should not be interrupted by the government.

Finally, in Part IV, I present various social-democratic answers. First, I explore the solution of cogent labour laws; I primarily analyse the minimum wage law. I recommend discussing minimum wage debate in conjunction with unemployment benefits and minimum income assurance, and I thus conduct the analysis (Section IV.A). I then examine the solution of organized work (Section IV.B). Next, I examine the solution of redistribution through tax laws, particularly, the solution of negative income tax (Section IV.C); I also discuss how much money to transfer from the rich to the poor through tax laws (Section IV.C.1). I discuss a combined mechanism of minimum wage and negative income tax; a mechanism that sets both, a negative income tax and a minimum wage, so that the employer cannot respond to negative income tax by lowering the wage below the minimum wage, but the mechanism also greatly reduces the firm's incentive to dismiss its employees (Section IV.C.2).

B. On the Importance of the Question, or: What Should be the Agenda of Political Economy and of Law and Economics?

Before I delve into the question, I discuss its importance and the agenda on which it is based.

Adam Smith said:

Political economy considered as a branch of the science of a statesman or legislator, proposes two distinct objects: first, to provide a plentiful revenue or subsistence for the people, or more properly to enable them to provide such a

revenue or subsistence for themselves; and secondly, to supply the state or commonwealth with a revenue sufficient for the public services. It proposes to enrich both the people and the sovereign.³

Thus, a student of the Smithian political economy would ask, for example, how the crown should allow citizens to provide for their needs, and how the crown should secure income for itself. Or, in a more Smithian style: What makes some countries more successful in allowing their citizens to provide themselves with the products they need and others less successful? Moreover, we can imagine other political economy goals, such as minimizing human suffering caused by poverty, reducing poverty, protecting the weak, or reducing gaps; choosing other goals will invite other questions.

Choosing the issues that political economy studies will invite controversy over the agenda. The philosopher Joseph Agassi emphasized that one of the most important questions is “what should be the agenda?,” and that the technique of elected parliaments in authoritarian states is the control of the agenda.⁴ A humanist economics agenda would propose to discuss how to protect the weak. Kenneth Arrow pointed out that economists are now almost exclusively using the utilitarian philosophy.⁵ The utilitarian philosophy aims to maximize happiness—as much happiness as possible for as many people as possible.⁶ This philosophy sees moral action as an act that brings about human happiness and justifies its basic principle on the basis that what people want in life is to be happy; given human equality, the moral principle should be to maximize total human happiness. One of the founding fathers of the Law and Economics movement, Richard Posner, considers the economic analysis of law as transforming utilitarianism into a scientific theory.⁷ Smith was not a utilitarian, but a natural freedom advocate. This can be seen in his lack of support in antitrust laws, since they violate natural freedom; although, Smith acknowledged the great damage caused by monopolies, and therefore argued that it was wrong to encourage monopolies.⁸

3. ADAM SMITH, *THE WEALTH OF NATIONS* 5 (Andrew Skinner ed., Penguin Books 1999) (1776).

4. JOSEPH AGASSI, *OUR AGENDA AND ITS RATIONALITY*, in *THE MYSTERY OF RATIONALITY: MIND, BELIEFS AND THE SOCIAL SCIENCES* 7–15 (Gérald Bronner & Francesco Di Iorio eds., 2018). JOSEPH AGASSI & ABRAHAM MEIDAN, *BEG TO DIFFER THE LOGIC OF DISPUTES AND ARGUMENTATION* (2016).

5. 1 KENNETH J. ARROW, *COLLECTED PAPERS OF KENNETH J. ARROW* viii (1983).

6. John Stuart Mill, *Utilitarianism*, in *SEVEN MASTERPIECES OF PHILOSOPHY* 329 (Steven M. Cahn ed., 2016) (1861).

7. Richard A. Posner, *The Present Situation in Legal Scholarship*, 90 *YALE L.J.* 1113, 1115 (1981).

8. See SMITH, *supra* note 3, at 91–93.

A monopoly granted either to an individual or to a trading company has the same effect as a secret in trade or manufactures. The monopolists, by keeping the market constantly understocked, by never fully supplying the effectual demand, sell their commodities much above the natural price, and raise their emoluments, whether they consist in wages or profit, greatly above their natural rate.

The price of monopoly is upon every occasion the highest which can be got. The natural price, or the price of free competition, on the contrary, is the lowest which can be taken, not upon every occasion, indeed, but for any considerable time together. The one is upon every occasion the highest which can be squeezed out of the buyers, or which, it is supposed, they will consent to give: the other is the lowest which the sellers can commonly afford to take, and at the same time continue their business.

The exclusive privileges of corporations, statutes of apprenticeship, and all those laws which restrain, in particular employments, the competition to a smaller number than might otherwise go into them, have the same tendency, though in a less degree. They are a sort of enlarged monopolies, and may

I continue the critique of Arrow that economists today exclusively use the utilitarian philosophy by presenting an example of a specific discussion that emerges from the moral approach that actions should be judged according to how they improve one's moral qualities. *The Book of Education*, a 13th century's Jewish theological book that discusses each of the 613 commandments, explains "the commandment to allow the wage-worker to eat from the attached [produce] upon which he is working" by these words, "[i]t is from the roots of the commandment [that it is] to teach the Children of Israel to have a nice soul and goodwill."⁹ Maimonides, in his book *The Guide for the Perplexed*, wrote about a commandment that protects refugees' rights:

Mercy is also the object of the law, "Thou shalt not deliver unto his master the servant that is escaped from his master" (Deut. xxiii. 15); but it teaches besides a very useful lesson, namely, that we must always practise this virtue, help and protect those who seek our help, and not deliver them unto those from whom they flee; and it is not sufficient to give assistance to those who are in need of our help; we must look after their interests, be kind to them, and not hurt their feeling by words.¹⁰

I argue that the fact the theoretical-economic framework, or at least the culture of economists, does not take such considerations into account is a serious limitation, and we should mitigate it. The utilitarian discourse can also include the benefits of pity cultivation in society.

In health economics, disregard for virtue or the benefit of maintaining compassion in society can lead to conclusions that completely contradict common sense. When we ignore the considerations of preserving the moral virtues of society, we may arrive to absurd conclusions regarding the right to receive medical care, especially regarding the rights of elderly people, or regarding financing expensive drugs or regarding organ trafficking. If, for instance, a cost-benefit balance that excludes virtue considerations leads to the conclusion that a particular drug package should be funded by the state, then a cost-benefit balance that also takes into account the ill-treatment of patients destroys society and

frequently, for ages together, and in whole classes of employments, keep up the market price of particular commodities above the natural price, and maintain both the wages of the labour and the profits of the stock employed about them somewhat above their natural rate.

Such enhancements of the market price may last as long as the regulations of police which give occasion to them.

The market price of any particular commodity, though it may continue long above, can seldom continue long below its natural price. Whatever part of it was paid below the natural rate, the persons whose interest it affected would immediately feel the loss, and would immediately withdraw either so much land, or so much labour, or so much stock, from being employed about it, that the quantity brought to market would soon be no more than sufficient to supply the effectual demand. Its market price, therefore, would soon rise to the natural price. This at least would be the case where there was perfect liberty.

Id. Despite all of this, Smith did not propose to take any active legal measure to fight monopolies that were not created by the law.

9. *Mitzvah*, in SEFER HACHINUC 576 (translated by Sefaria, 2018). There is a debate about who is the true author of this canonical book.

10. MOSES MAIMONIDES, THE GUIDE FOR THE PERPLEXED 341 (Micheal Friedlander trans., George Routledge & Sons 1919) (1881).

rescuing them fosters compassion and friendly feelings, will lead to the conclusion that a larger drug package should be funded by the state. A perception that only economic considerations should be considered contradicts the words of one of the two fathers of utilitarian theory, John Stewart Mill, as expressed in his book *Principles of Political Economy*:

It must be kept in mind that Political Economy deals only with the phenomena of material wealth; it does not supply ethical or political grounds of action. It is quite conceivable that a legislator, in coming to a decision, may have to balance economic gains against moral or political losses, and may choose to give up the former to prevent the latter.¹¹

I would like to point out a possible change in the utilitarian agenda of economists. The utilitarian philosopher asks how to promote as much happiness as possible to as many people as possible. In contrast, the Popperian philosopher would ask how to minimize suffering.¹² Therefore, the mechanism design economists are asking how to provide the incentives that will lead to achieving the optimal result (and some would also add: What are the incentives that lead to information flow to the central planner?).¹³ We prefer another approach, to ask: How to provide the incentives that will lead to the prevention of negative results? Or, how to prevent the games that may lead to adverse results. In my article with Joseph Agassi, we argue:

We suggest that the most significant achievement of game theory is not in the design or in the applications of games but in the suggestions of what games it is unwise to play. Here we follow Popper, who said, politically, preventing pain or suffering has priority over creating pleasure. Obviously, in game theory, prevention is also much easier than application, because every game requires some conditions for its very applicability, and these are never too clear and seldom parts of game theory are proper.¹⁴

The proposed agenda of humanistic economics says that political economics is interested in minimizing suffering. If one accepts this agenda, those who discuss the labor market, particularly labor law, should ask questions such as: How to minimize the suffering of the weak workers? How much is needed to protect them? And, how to deal with power gaps? Adopting a humanistic approach is especially important when economists turn to

11. JOHN STUART MILL, *PRINCIPLES OF POLITICAL ECONOMY* 621 (New York, D. Appleton & Co. 1894).

12. KARL R. POPPER, *THE OPEN SOCIETY AND ITS ENEMIES* 157–69 (4th ed. 1963) (focusing on minimizing suffering).

13. Eric Maskin claimed in his Nobel lecture:

Because mechanism designers do not generally know which outcomes are optimal in advance, they have to proceed more indirectly than simply prescribing outcomes by fiat; in particular, the mechanisms designed must generate the information needed as they are executed. The problem is exacerbated by the fact that the individuals who do have this critical information – the citizens in the public good case or the buyers in the asset-selling example – have their own objectives and so may not have the incentive to behave in a way that reveals what they know. Thus, the mechanisms must be incentive compatible.

Eric S. Maskin, *Mechanism Design: How to Implement Social Goals*, 98 AM. ECON. REV. 567, 568 (2008).

14. Uri Weiss & Joseph Agassi, *How Game Theory Encourages Peace* (2020) (unpublished manuscript) (on file with author).

legal questions. The jurist's imperative is "seek judgment, relieve the oppressed, judge the fatherless, plead for the widow."¹⁵ Under the humanistic approach the law minimizes injustice and arbitrariness. When economists function as jurists, a legal agenda that prevents injustice is certainly important.

The Law and Economics movement transforms political economy from the theory of the legislator and statesman (as Smith described it) to the theory of the judge, legislator, statesman, and in particular, the judge.¹⁶ However, a dominant approach in law and economics supports not assessing justice considerations. A significant portion of law and economics scholars replace justice considerations with efficiency considerations.¹⁷ From their point of view, efficiency answers all things. Richard Posner discerns the rules in common law as efficient and as ones that should be efficient.¹⁸ Posner rightly views law and economics as a continuation of American legal realism.¹⁹ American legal realism did not recognize the ability to reach legal conclusions through legal rules Posner suggests reaching conclusions through economic theory, which he regards as the scientification of utilitarianism.²⁰

The next step in the economic analysis of the law is Kaplow and Shavell's theory,

15. *Isaiah* 1:17 (King James).

16. SMITH, *supra* note 3.

17. Posner even claimed:

Once the concept of corrective justice is given its correct Aristotelian meaning, it becomes possible to show that it is not only compatible with, but required by, the economic theory of law. In that theory, law is a means of bringing about an efficient (in the sense of wealth-maximizing) allocation of resources by correcting externalities and other distortions in the market's allocation of resources.

Richard A. Posner, *The Concept of Corrective Justice in Recent Theories of Tort Law*, 10 J.L. STUD. 187, 201 (1981).

18. See generally RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* (7th ed. 2007); RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* (1st ed. 1973).

19. Posner claimed:

The scholarly movement that is today's counterpart to Legal Realism as the foremost alternative to doctrinal analysis is economic analysis of law, or, as it is sometimes called, 'Law and Economics.' It too has both normative and positive aspects. The normative branch of the economic analysis of law can be viewed as a direct descendant of Legal Realism, by way of Guido Calabresi; the positive branch comes from outside the law, from the work of economists such as Ronald Coase and Gary Becker. Calabresi's brand of normative economic analysis of law shares with Legal Realism a desire to perform radical surgery on the common law; for example, Calabresi wishes to do away with fault as the basic guide to allocating liability in accident cases. The positive analysts such as myself resemble traditional doctrinal analysts in believing that there really are rules of law—that the law is not wholly a matter of judicial discretion, as the more extreme Legal Realists believed. We use economics to inquire to what extent the common law is a coherent system of rules concerned with promoting efficiency.

Posner, *supra* note 7, at 1120.

20. Posner claimed:

With qualifications not important here, economics can be described as scientific utilitarianism. Someone who uses economics to expose the inner logic of the common law or to propose reforms designed to make the law more efficient is therefore taking up where Ames and Prosser left off; he is using a similar methodology but one that is more powerful because it is informed by modern advances in economic thinking.

Posner, *supra* note 7, at 1115.

which states that since tax laws can compensate those who are offended by the efficient rule, the efficient rule must always be enacted independently of the considerations of distributive or corrective justice.²¹ That is, jurists should be completely blind to the considerations of justice when choosing the legal rule. For them, when the legislators come to the legislature, it is necessary to ask what is the law that will maximize the general pie measured in units of money, and this is the super criterion under which the law should be determined.²² Otherwise, they are missing out on the Pareto improvements: improving the condition of at least some players without undermining any players. Kaplow and Shavell claimed, “We have demonstrated that any method of policy assessment that is not purely welfarist violates the Pareto principle.”²³

The explanation for this is as follows. Suppose a law leads to a 100-size general pie, and another law leads to a 90-size general pie. Kaplow and Shavell argue that the law leading to a 100-size general pie should be favoured independent of whether the other law leads to more or less affirmative and distributive justice.²⁴ According to them, if we consider that judicial considerations lead to the preference of the other law, then what is needed is not to legislate it, but to compensate those who are affected by the preference of one law over another.²⁵ Since the pie created in one law is greater, one can also give those who would enjoy what they were entitled to under the other law; and retain the excess!

Kaplow and Shavell’s theory has magic, but its magic rests on delusion. They are wrong. They ignore the fact that such compensation is often (and especially in cases of corrective justice such as tort law) impossible or impractical because it is impossible to know whom the casualties requiring compensation are and how much money the victims are compensated. The question arises: What to do when it is impossible or impractical to compensate the victims of the more efficient legal rule?

One option is to give up the efficient law in favour of the fair law, and the other is to enact it, nonetheless. The theory that the efficient rule should be passed independently of other considerations, even if compensation is not possible, is a continuation of the theory that underlies the Kaldor-Hicks criterion: When it is possible to compensate those affected by the wealth-maximizing distribution, in case the injured are compensated, the wealth-maximizing distribution is the best one, even when there are no compensators.²⁶ According to the Kaldor-Hicks index, if it is possible to move from one division to another, and if everyone benefits from this transition, the transition should be preferred.²⁷ So far, this is easy to agree with. This transition is desirable even when mutual improvement is made due to the compensation. This is also easy to agree with. However, this theory actually holds: since what is important is maximizing the pie, the transition that would have created mutual

21. See Louis Kaplow & Steven Shavell, *Any Non-Welfarist Method of Policy Assessment Violates the Pareto Principle*, 109 J. POL. ECON. 281, 284–85 (2001) (concluding that everyone is made worse off when policy evaluations provide weight to “principles independent[] of their effect on individuals’ utilities”).

22. *Id.*

23. *Id.*

24. *Id.*

25. *Id.*

26. N. Kaldor, *Welfare Propositions of Economics and Interpersonal Comparisons of Utility*, 49 ECON. J. 549, 550–51 (1939); J. R. Hicks, *The Foundations of Welfare Economics*, 49 ECON. J. 696, 698–701, 711–12 (1939).

27. Kaldor, *supra* note 26; Hicks, *supra* note 26. See generally W.J. Baumol, *Community Indifference*, 14 REV. ECON. STUD. 44 (1946).

improvement should have been supported if we had compensated the injured, even when the compensation is not actually paid.²⁸ Their theory was criticized and rejected by Kenneth Arrow.²⁹ According to him, not only is it ethically difficult, but it also may lead to a contradiction: sometimes, x will be better than y , and sometimes, y will be better than x .³⁰ This theory, which has been rejected in other branches of economics (other than ‘industrial organization’),³¹ is still used in law and economics. This theory is equivalent to the following theory: “If we had compensated the casualties, the rule would have been desirable, and therefore it would be desirable even if we did not break them.” This theory is rather absurd and must be rejected, particularly in law, as it is contrary to the basic command of the jurist: “seek judgment, relieve the oppressed, judge the fatherless, plead for the widow.”³² In other words, the use of the above measure in law and economics is absurd in light of the role of the law—the protection of the weak.

The proposed agenda in this article—seeking ways to protect the weak—would be lauded by economists such as Frederick Hayek, one of the great prophets of twentieth-century capitalism. According to Hayek, spontaneous order should be preferred and social planning should be avoided.³³ Hayek had two main arguments. First, social planning is doomed to fail since the social planner does not have enough information required for planning success.³⁴ According to the first welfare theorem, when resources are allocated through the free market then, in the absence of friction such as transaction costs or information gaps, exchanges that create mutual improvement will not be missed.³⁵ In contrast, the social planner does not know the preferences of the citizens.³⁶ Therefore, social planning is likely to lead to absurdities. For example, if Ann lives in Apartment A and Bob lives in Apartment B and both desire to exchange apartments, which would have easily been possible if the rules of the game were to allocate resources through the free market, taxes imposed on buying and selling apartments can sometimes prevent their exchange. Second, social planning is likely to lead to tyranny because it requires a state apparatus.³⁷ This approach sometimes leads to absurdities as well, such as private prisons. Under the guise of a minimal state ideology, the state encourages “private” tyranny foci.

28. Arrow wrote: “Voting can be regarded as a method of arriving at social choices derived from the preferences of individuals. Another such method of more specifically economic content is the compensation principle, as proposed by Mr. Kaldor: in a choice between two alternative economic states x and y , if there is a method of paying compensations under state x such that everybody can be made better off in the state resulting from making the compensations under x than they are in state y , then x should be chosen in preference to y , even if the compensation is not actually paid.” Kenneth J. Arrow, *A Difficulty in the Concept of Social Welfare*, 58 J. POL. ECON. 328, 330 (1950) (footnote omitted).

29. *Id.*

30. *Id.*

31. For the place of Kaldor Hicks efficiency in industrial organization, see Stephen Martin, *The Kaldor–Hicks Potential Compensation Principle and the Constant Marginal Utility of Income*, 55 REV. INDUST. ORG. 493 (2019). For the place of Kaldor Hicks efficiency in law and economics, see generally Jules Coleman, *The Normative Basis of Economic Analysis: A Critical Review of Richard Posner’s The Economics of Justice*, 34 STAN. L. REV. 1105 (1982).

32. *Isaiah* 1:17 (King James).

33. See generally Friedrich A. Hayek, *Planning, Science and Freedom*, 148 NATURE 580 (1941).

34. *Id.*

35. See generally MAS-COLELL ET AL., MICROECONOMIC THEORY (1995).

36. Hayek, *supra* note 33.

37. *Id.*

According to Hayek's philosophy, the intervention of the state to protect the poor would lead to much more suffering.³⁸

The discourse of humanistic economics is especially important in light of the social role that economists play today, especially in the design of legal institutions. They replace other value designers, such as philosophers, writers, clerics, intellectuals, and jurists. Percy Bysshe Shelley said, "The poets are the unacknowledged legislators of the world."³⁹ I wonder, how true is this concerning the economists today? I think it is easy to agree that those involved in the design of values should consider human suffering. I would like to criticize those economists, especially from the Chicago school, whose agenda does not consider human suffering. It should be noted that eminent economists such as Smith and Keynes were humanists.⁴⁰ Economic theory on the labour market is developing at an unbearable level of inattention to the weak and the need to minimize their suffering. W. H. Auden said, of painters, following a visit to the museum:

About suffering they were never wrong,
 The old Masters: how well they understood
 Its human position: how it takes place
 While someone else is eating or opening a window or just walking dully along;
 How, when the aged are reverently, passionately waiting
 For the miraculous birth, there always must be
 Children who did not specially want it to happen, skating
 On a pond at the edge of the wood:
 They never forgot
 That even the dreadful martyrdom must run its course
 Anyhow in a corner, some untidy spot
 Where the dogs go on with their doggy life and the torturer's horse
 Scratches its innocent behind on a tree.
 In Breughel's Icarus, for instance: how everything turns away
 Quite leisurely from the disaster; the ploughman may
 Have heard the splash, the forsaken cry,
 But for him it was not an important failure; the sun shone
 As it had to on the white legs disappearing into the green
 Water, and the expensive delicate ship that must have seen
 Something amazing, a boy falling out of the sky,
 Had somewhere to get to and sailed calmly on.⁴¹

38. FRIEDRICH AUGUST HAYEK, THE CONSTITUTION OF LIBERTY: THE DEFINITIVE EDITION (2020).

39. Percy Bysshe Shelley, *A Defence of Poetry*, POETRY FOUND., <https://www.poetryfoundation.org/articles/69388/a-defence-of-poetry#:~:text=Shelley's%20%E2%80%9CDefence%20of%20Poetry%E2%80%9D%20is,aesthetic%20judgments%20of%20his%20contemporaries.&text=Language%2C%20Shelley%20contains%2C%20shows%20humanity's,appreciation%20of%20unity%20and%20beauty> (last visited Nov. 21, 2020).

40. See, e.g., ADAM SMITH, THE THEORY OF MORAL SENTIMENTS (2010); SMITH, *supra* note 3; JOHN MAYNARD KEYNES & PAUL A. VOLCKER, THE ECONOMIC CONSEQUENCES OF THE PEACE (1920); JOHN MAYNARD KEYNES, THE GENERAL THEORY OF EMPLOYMENT, INTEREST, AND MONEY (2016). Ditz claimed, "Smith's ideology, affirming laissez faire, free enterprise, capitalism is indeed congruent with Weber's 'Protestant Ethic'. Keynes's ideology in contrast expresses secular hedonistic humanism." Gerhard W. Ditz, *Smith and Keynes: Religious Differences in Economic Philosophy*, 49 BIJDRAGEN 58, 86 (1988).

41. W. H. Auden, *Musée des Beaux Arts*, POEMS <https://poems.com/poem/musee-des-beaux->

Auden was delighted that the great painters see human suffering, decode it, and portray it as coexisting with happiness and boredom, with the indifference of happy and bored sufferers. Although it is wrong to place demands on economists that they cannot meet and considering that human suffering is a demand that is almost impossible to meet, it is a matter of degree. The norm among orthodox economists of almost completely ignoring the suffering of disadvantaged workers needs to change. At the very least, economists should not be short-sighted by refusing to wear available glasses like the insights offered in other social sciences and arts.

The following is an example of the tremendous effects in cases where economists take the humanistic approach. Kenneth Arrow is one of the greatest humanist economists. One of Arrow's major contributions is that he transformed the economic theory of healthcare, an inversion with tremendous positive results for the lives of a large number of people, especially the weak.⁴² In general, until Arrow's innovation, economists saw no difference between healthcare and another product/service.⁴³ Just as the free market requires the distribution of resources without any state intervention, it must also regulate health services. The humanist's feelings rise against this because they believe "neither shalt thou stand against the blood of thy neighbour,"⁴⁴ and also because the mere abandonment of a sick person to death and torment will corrupt society. A free-market economist would say something like, "[r]ight, but the responsibility of charity is of the church and not of the state."⁴⁵ Kenneth Arrow, in a formative article, points out some of healthcare's specific characteristics.⁴⁶ The first characteristic is the externalities—implications for third parties, which the parties to the contract do not consider.⁴⁷ For example, when a person is ill, he/she may spread diseases. A second feature is the high cost of medical care, which is why people purchase insurance in advance.⁴⁸ However, it is in the insurance company's best interest

arts/#:~:text=About%20suffering%20they%20were%20never,beChildren%20who%20did%20not (last visited Nov. 21, 2020).

42. See generally Kenneth J. Arrow, *Uncertainty and The Welfare Economics of Medical Care*, 53 AM. ECON. REV. 941 (1963) (evaluating the economic problems of medical care that are explained as resulting from uncertainty).

43. Krugman claimed: "Um, economists have known for 45 years—ever since Kenneth Arrow's seminal paper—that the standard competitive market model just doesn't work for health care: adverse selection and moral hazard are so central to the enterprise that nobody, nobody expects free-market principles to be enough." Paul Krugman, *Health Care is Not a Bowl of Cherries*, N.Y. TIMES (June 28, 2009, 3:04 PM), <https://krugman.blogs.nytimes.com/2009/06/28/health-care-is-not-a-bowl-of-cherries/?mtref=www.google.com&assetType=PAYWALL>.

44. *Leviticus* 19:16 (King James).

45. "If only 'every church and synagogue would take in 10 welfare families' each, [Ronald Regan] said, the problem could be weathered until it passed." Chris Roberts, *The Great Eliminator: How Ronald Reagan Made Homelessness Permanent*, SF WEEKLY (June 29, 2016, 6:00 PM), <https://www.sfweekly.com/news/the-great-eliminator-how-ronald-reagan-made-homelessness-permanent/>. Milton Friedman said about poverty:

One recourse, and in many ways the most desirable, is private charity. It is noteworthy that the heyday of laissez-faire, the middle and late nineteenth century in Britain and the United States, saw an extraordinary proliferation of private eleemosynary organizations and institutions. One of the major costs of the extension of governmental welfare activities has been the corresponding decline in private charitable activities.

MILTON FRIEDMAN, *FREEDOM AND CAPITALISM* 190–91 (1962).

46. See generally Arrow, *supra* note 42 (describing healthcare's specific characteristics).

47. *Id.*

48. *Id.*

that doctors subject patients to as few expensive treatments as possible. There is a conflict of interest between the patient and the doctor or the insurance company, and information gaps about what the patient needs. In other words, the person who determines in real time what is needed for the patient is in conflict with the patient. Therefore, the reasoning of the free market may fail. In fact, because of the information gaps and the conflict of interest, there are unquestionable benefits of regulating health care according to the principles of ethics, rather than the principles of the market. This is actually the other side of the coin, the problem of defensive medicine; tort law encourages doctors to prefer to make mistakes for which they will *not* pay compensation, over making mistakes for which they will pay compensation.⁴⁹ The logic of incentives can distort doctors' choices, and thus there is an advantage in regulating medicine by way of ethics rather than by way of incentives.

Arrow's theory was later developed by his student, Nobel laureate George Akerlof.⁵⁰ In one of the finest models of economic theory, Akerlof showed that asymmetrical information could make the entire health market fail; when someone buys health insurance, they signal to the insurance company that they may be a sick person, making the deal unprofitable for the insurance company.⁵¹ He claimed:

It is a well-known fact that people over 65 have great difficulty in buying medical insurance. The natural question arises: why doesn't the price rise to match the risk?

Our answer is that as the price level rises the people who insure themselves will be those who are increasingly certain that they will need the insurance; for error in medical check-ups, doctors' sympathy with older patients, and so on make it much easier for the applicant to assess the risks involved than the insurance company. The result is that the average medical condition of insurance applicants deteriorates as the price level rises—with the result that no insurance sales may take place at any price.

...

This adds one major argument in favor of medicare. On a cost benefit basis medicare may pay off: for it is quite possible that every individual in the market would be willing to pay the expected cost of his medicare and buy insurance, yet no insurance company can afford to sell him a policy—for at any price it will

49. Kessler and McClellan claimed:

"Defensive medicine" is a potentially serious social problem: if fear of liability drives health care providers to administer treatments that do not have worthwhile medical benefits, then the current liability system may generate inefficiencies much larger than the costs of compensating malpractice claimants. To obtain direct empirical evidence on this question, we analyze the effects of malpractice liability reforms using data on all elderly Medicare beneficiaries treated for serious heart disease in 1984, 1987, and 1990. We find that malpractice reforms that directly reduce provider liability pressure lead to reductions of 5 to 9 percent in medical expenditures without substantial effects on mortality or medical complications. We conclude that liability reforms can reduce defensive medical practices.

Daniel Kessler & Mark McClellan, *Do Doctors Practice Defensive Medicine?*, 111 Q.J. ECON. 353, 353 (1996).

50. George A. Akerlof, *The Market for "Lemons": Quality Uncertainty and the Market Mechanism*, 84 Q. J. ECON. 488, 492-94 (1970).

51. *Id.*

attract too many ‘lemons’. The welfare economics of medicare, in this view, is *exactly* analogous to the usual classroom argument for public expenditure on roads.⁵²

The theory of information problems in the insurance market has influenced the discourse on health care reform at least in the United States.⁵³ Hayek argued that information problems would fail any planning⁵⁴ and therefore, spontaneous order should be chosen without trying to protect the weak in the way of planning. For Arrow and Akerlof, the information problems are in themselves the justification for state intervention in the health market. One of the lessons could be that we can only know at the end of the debate the answer to issues such as how the state law should protect the weak in the market. Information problems can sometimes negate planning and can sometimes require it.

Moreover, the controversy over the question of what the free market boundary should be is not merely a dispute over traditional economic questions. It is not just a dispute about the state’s intervention in the nails market. The following questions are also included: What should be the plea-bargaining limit? To what point does a person’s right to sell organs extend? To what extent is the freedom to reach surrogacy agreements? What should be the limit of the free market for sexuality? What should be the limit of the free market for marriage? (In fact, even the ban on bigamy is a restriction on the freedom of contract.) It makes perfect sense to give different answers in different markets. Just as it is wrong to discuss the question as to what the free market boundary should be, when there is only a free market of prostitution before us, so too it is wrong to discuss this question when there is only a free market of greeting card sales before us. Thus, even the answer to the question of what should be the free labour market boundary can depend on the strength gaps that characterize the specific labour market.

As a summary of this Section, I note that I support the humanist economy agenda. Such an agenda would consider the weakest sections of society. For a humanist economics agenda, it is appropriate to adopt Popper’s recommendation to ask how to minimize suffering, rather than ask how to maximize happiness, as utilitarianists do.⁵⁵ It is important to make these changes, because, as Arrow pointed out, economic theory nowadays adopts the utilitarian philosophy almost exclusively.⁵⁶ Moreover, the economic theory of law uses welfare measurements that look after profit maximization, as opposed to maximizing happiness which works against the weak (since the indices do not consider that a dollar for the poor is more important than a dollar for the rich).⁵⁷ A humanist economics agenda is

52. *Id.*

53. *See, e.g.*, Paul Krugman, *Health Economics 101*, N.Y. TIMES (Nov. 14, 2005), <https://www.nytimes.com/2005/11/14/opinion/health-economics-101.html> (discussing the role information plays in health care discourse). *See also* David Brooks, *Do Markets Work in Health Care?*, N.Y. TIMES (Jan 13, 2017), <https://www.nytimes.com/2017/01/13/opinion/do-markets-work-in-health-care.html> (“Proponents of market-based health care rely less on theory and more on data.”).

54. Hayek, *supra* note 33, at 582.

55. Popper said: “The piecemeal engineer will, accordingly, adopt the method of searching for, and fighting against, the greatest and most urgent evils of society, rather than searching for, and fighting for, its greatest ultimate good.” POPPER, *supra* note 12, at 158.

56. ARROW, *supra* note 5.

57. THOMAS RICHARD HARRY, *THE GATHERING OF THE CLAN: AN INDEPENDENT POLITICAL OPTION FOR AMERICA* 45 (2009). *See generally* Matthew D. Adler & Eric A. Posner, *Implementing Cost-Benefit Analysis When Preferences Are Distorted*, 29 J. LEGAL STUD. 1105 (2000).

especially important in law and economics if one agrees that the fundamental purpose of law is to protect the weak from injustice and arbitrariness. Regarding the extent to which a humanistic economy agenda is necessary, we can learn from Arrow's humanistic approach, an approach that led to a revolution in the theory of health economics, which saved a large number of people. Thus, in discussing labour market regulation, it is important to ask questions such as: How to protect the weak worker? Or: How to deal with power disparities in the labour market?

C. How Does this Article Approach the Question?

How should state law deal with the power gaps between the employer and the employee in the capitalist labour market? Before I answer the question itself, I discuss my approach. I shall approach it as an imaginary dialogue between a capitalist and a socialist speaking both languages of modern economic theories, including game theory and law and economics. Both theories can eliminate the historical errors from the approaches in which they have emerged. In doing so, I try to equip each of them with the best considerations and arguments that we can raise. One of the problems in the current economic debate is that while Smith's economic theory has been presented in the language of modern economic theory, socialist theory has not been similarly presented. Thus, the outcome of the argument is predetermined. Moreover, the transfer of economic theory to the framework of a modern economy is not merely an act of translation, rather, a very intervening one; it sometimes corrects mistakes or adjusts itself to the new environment. If an imaginary argument between the socialist and the capitalist is presented today, it would be presented between a fossilized socialist and a capitalist who is free from fundamental mistakes in his theory (for example, the theory of the free market has been updated to deal with market failures). The current text in economics books is on the one hand unhistorical, and on the other hand, if they relate to the socialist, they refer to the historical socialist.⁵⁸ The turning point I propose is significant, since I argue that there is much to be learned from socialist economists—especially on the problems created by the capitalist system—although the interesting things that socialists have said have been accompanied or even been coined by nonsense. There is a criterion that all scientists agree on in the discussion, and it is transparency.⁵⁹ In this article I try to contribute to the transparency of the debate. The article is deliberately written in such a way that it could contribute to the democratic discourse, as opposed to the technocratic discourse; to the fundamental questions that economists sometimes see as part of economics (when they give their advice) and sometimes see as part of philosophy (when they are criticized on the lack of the discussion of fundamental questions). The article is written in the style of an introductory article, one that tries not to rely on the former knowledge of the reader and presents important disagreements.⁶⁰

58. *E.g.*, JOSHUA GANS ET AL., PRINCIPLES OF MICROECONOMICS 12–14 (2011).

59. “Both scientists and philosophers of science have recently emphasized the importance of promoting transparency in science.” Kevin C. Elliot, *A Taxonomy of Transparency in Science*, CANADIAN J. PHIL. 1, 1 (2020).

60. It can serve, for example, as an introduction to a course in labour law.

D. What is a Capitalist Labour Market?

In this article, I discuss the capitalist labour market and how to deal with the power gaps created in it. However, what is a capitalist labour market after all?

The question of what a capitalist production method is, is controversial. According to the Marxist conception, the method of production becomes capitalist when one owner employs a large number of workers.⁶¹ We can read it in Marx's words, as per his book *The Capital*:

Capitalist production only then really begins, as we have already seen, when each individual capital employs simultaneously a comparatively large number of labourers; when consequently the labour-process is carried on on an extensive scale and yields, relatively, large quantities of products. A greater number of labourers working together, at the same time, in one place (or, if you will, in the same field of labour), in order to produce the same sort of commodity under the mastership of one capitalist, constitutes, both historically and logically, the starting-point of capitalist production. With regard to the mode of production itself, manufacture, in its strict meaning, is hardly to be distinguished, in its earliest stages, from the handicraft trades of the guilds, otherwise than by the greater number of workmen simultaneously employed by one and the same individual capital. The workshop of the medieval master handicraftsman is simply enlarged.⁶²

Thus, according to the Marxist view, material conditions shape the method of production. The industrial revolution made machinery more productive than domestic production, and therefore those who engaged in domestic production would lose competitiveness.⁶³ However, machines are an expensive commodity, and therefore they have caused one owner to employ many workers. In other words, production without machinery cannot compete with production with machinery, and the machinery belongs only to the wealthy. This is also one of the key things to change according to the Marxist approach: to transfer the means of production to the workers of production.⁶⁴ According to the Marxist approach, because the industrial revolution took place under production conditions, this led to a capitalist revolution in the relations of production, which also led

61. KARL MARX, *CAPITAL: A CRITIQUE OF POLITICAL ECONOMY* 353 (Frederick Engels ed., Samuel Moore & Edward Aveling trans., Charles H. Kerr & Co. 1908).

62. *Id.*

63. See, for example, those words of Friedrich Engels:

This industrial revolution was precipitated by the discovery of the steam engine, various spinning machines, the mechanical loom, and a whole series of other mechanical devices. These machines, which were very expensive and hence could be bought only by big capitalists, altered the whole mode of production and displaced the former workers, because the machines turned out cheaper and better commodities than the workers could produce with their inefficient spinning wheels and handlooms. The machines delivered industry wholly into the hands of the big capitalists and rendered entirely worthless the meagre property of the workers (tools, looms, etc.). The result was that the capitalists soon had everything in their hands and nothing remained to the workers. This marked the introduction of the factory system into the textile industry.

Frederick Engels, *The Principles of Communism*, MARXIST INTERNET ARCHIVE, <https://www.marxists.org/archive/marx/works/1847/11/prin-com.htm> (last visited Dec. 26, 2020).

64. *Id.*

to the legal revolution.⁶⁵ It was the capitalist change in the conditions of production that gave rise to the liberal law, which in turn gave birth to liberal labour laws and the liberal constitutional conception, a concept that placed central freedom of property and freedom of contract, and made the freedom of negotiations the central freedom.

The Marxist legal approach is Hegelian (i.e. a romantic one).⁶⁶ The law reflects and validates the status quo, but the law does not change the reality. The Marxist approach denies the ability of the law to protect the stranger, the orphan, and the widow.⁶⁷ Marxism, therefore, does not seek to repair the world through changes in legislation, but through changes in the relations of production and bargaining relations, which would occur mainly through revolution rather than through legislative changes. Marx criticized social

65. Marx and Engels wrote:

By freedom is meant, under the present bourgeois conditions of production, free trade, free selling and buying

But don't wrangle with us so long as you apply, to our intended abolition of bourgeois property, the standard of your bourgeois notions of freedom, culture, law, &c. Your very ideas are but the outgrowth of the conditions of your bourgeois production and bourgeois property, just as your jurisprudence is but the will of your class made into a law for all, a will whose essential character and direction are determined by the economical conditions of existence of your class. The selfish misconception that induces you to transform into eternal laws of nature and of reason, the social forms springing from your present mode of production and form of property – historical relations that rise and disappear in the progress of production – this misconception you share with every ruling class that has preceded you. What you see clearly in the case of ancient property, what you admit in the case of feudal property, you are of course forbidden to admit in the case of your own bourgeois form of property

Does it require deep intuition to comprehend that man's ideas, views, and conception, in one word, man's consciousness, changes with every change in the conditions of his material existence, in his social relations and in his social life? What else does the history of ideas prove, than that intellectual production changes its character in proportion as material production is changed? The ruling ideas of each age have ever been the ideas of its ruling class

The ideas of religious liberty and freedom of conscience merely gave expression to the sway of free competition within the domain of knowledge.

Karl Marx et al., *Manifesto of the Communist Party, 1848, Chapter II: Proletarians and Communists*, MARXIST INTERNET ARCHIVE, <https://www.marxists.org/archive/marx/works/1848/communist-manifesto/ch02.htm> (last visited Nov. 22, 2020).

66. Marx claimed:

The criticism of the German philosophy of state and right, which attained its most consistent, richest, and last formulation through Hegel, is both a critical analysis of the modern state and of the reality connected with it, and the resolute negation of the whole manner of the German consciousness in politics and right as practiced hereto, the most distinguished, most universal expression of which, raised to the level of science, is the speculative philosophy of right itself.

Karl Marx, *Introduction to A Contribution to the Critique of Hegel's Philosophy of Right*, MARXIST INTERNET ARCHIVE, https://www.marxists.org/archive/marx/works/download/Marx_Critique_of_Hegels_Philosophy_of_Right.pdf (last visited Nov. 22, 2020). See also Timothy M. Hyden, *A Critique of Marxist Legal Theoretical Constructs*, 28 *STUD. IN SOVIET THOUGHT* 345–55 (1984). Regarding Hegel, see generally GEORG WILHELM FREDRICH HEGEL, *HEGEL: ELEMENTS OF THE PHILOSOPHY OF RIGHT* (Allen W. Wood ed., 1991).

67. According to Marx, “Already as the resolute opponent of the previous form of German political consciousness the criticism of speculative philosophy of right strays, not into itself, but into problems which there is only one means of solving — practice.” Marx, *supra* note 66.

democrats for their attempt to restrain the effects of the price mechanism—that is, the determination of prices by “market forces” or such other metaphors—as an “invisible hand” rather than abolishing it.⁶⁸ Thus, while social democrats want the state to intervene in free competition to curb its wild effects, and the state will intervene, by regulation, in the labour relations between the firm and the workers, the Marxist approach holds that the solution is not to prevent the effects of the mechanism by regulation, but to replace the mechanism in a revolutionary way.⁶⁹

The Marxist idea, like Hegel, belittles legal and political documents. Hegel is the founding father of *realpolitik*.⁷⁰ The real-political approach is that an international agreement is not worth the paper it is written on, since the strong will dictate the relationship independently of the agreement, and the strong will act according to their own interest, independently of the agreement.⁷¹ Stalin expressed this view by asking, “How many divisions does the Pope have?”⁷² The Marxist approach is materialistic. This approach perceives the development of the material situation, especially technological, as a key to historical, cultural, and personal development. The material situation affects the legal perception, and also the literary perception. For instance, the Marxist literary philosopher, György Lukács, believed that the historical novel should not deal with the greatest known personalities in history as major heroes, since in the Marxist approach, the individual does not influence history.⁷³

As noted, Marx considers capitalism as a method of production in which one person employs many workers.⁷⁴ He considers it as the description of a factual situation, whereas the law confirms rather than creates it.⁷⁵ On the other hand, Adam Smith proposed a theory that was a recommendation; in particular, a recommendation to reduce the state’s role.⁷⁶ For Smith, a good liberal law—in particular, a law that protects property as it is protected in England during his lifetime—is a sufficient condition for prosperity: “That security which the laws in Great Britain give to every man that he will enjoy the fruits of his own labour is alone sufficient to make any country flourish.”⁷⁷ Of course, in order for the law

68. Marx said:

Trades Unions work well as centers of resistance against the encroachments of capital. They fail partially from an injudicious use of their power. They fail generally from limiting themselves to a guerilla war against the effects of the existing system, instead of simultaneously trying to change it, instead of using their organized forces as a lever for the final emancipation of the working class that is to say the ultimate abolition of the wages system.

Karl Marx, *Value, Price and Profit XII. General Relation of Profits, Wages, and Prices*, MARXIST INTERNET ARCHIVE (1910), <https://www.marxists.org/archive/marx/works/1865/value-price-profit/ch03.htm>.

69. *Id.*

70. Popper, *supra* note 12. Joseph Agassi, *Legal-Rational Authority*, WILEY-BLACKWELL ENCYC. SOC. THEORY 1–3 (2017).

71. Erik Ringmar, *The Relevance of International Law: A Hegelian Interpretation of a Peculiar Seventeenth-Century Preoccupation*, 21 REV. OF INT’L STUDIES 87, 87 n.1 (1995).

72. WINSTON CHURCHILL, *THE SECOND WORLD WAR* 105 (1948).

73. See generally GEORG LUKÁCS, *THE THEORY OF THE NOVEL: A HISTORICO-PHILOSOPHICAL ESSAY ON THE FORMS OF GREAT EPIC LITERATURE* (1971).

74. MARX, *supra* note 61.

75. *Id.*

76. SMITH, *supra* note 3, at 556.

77. *Id.*

to provide the assurance that Smith speaks of, requires both the laws and a minimum of the rule of law. This is a significant meta-legal difference between the Marxist approach and the liberal approach of Smith. Smith argued that what brings the desired result is the law.⁷⁸ To achieve a free market there must be a law that will guarantee property. Moreover, Smith supported non-interference by the state in the market beyond the protection of property rights, enforcement of contracts, prohibition of fraud, and imposition of taxes required for the supply of public goods, etc.⁷⁹

Game theory can also contribute to the dispute between the liberal and the Marxist-Hegelian approach over the question of the importance of international law and agreements. In my article with Joseph Agassi, we argue that game theory leads to the refutation of the realpolitik approach in both international relations and law.⁸⁰ The challenge for legal realism is that the law can prevent bad games, such as prisoner's dilemma games,⁸¹ and the challenge for political realism in international relations is that in repeatable relationships reputation can replace courts as an enforcement mechanism.⁸² In his Nobel lecture, Robert J. Aumann provided insight for the idea that the repeat of the game could eventually replace courts.⁸³

To conclude, according to the Marxist approach, production becomes capitalistic when a single landlord employs many workers.⁸⁴ It is the law that legitimizes the status quo. In contrast, Smith's theory of free trade is a recommendation.⁸⁵ It is a recommendation as to what the legal rules of the game should be. It is the law that can lead to economic prosperity.

II. THE PROBLEM OF BARGAINING GAPS IN THE CAPITALIST LABOUR MARKET

In this Part, I discuss the power gaps in the capitalist labour market. Let us consider the following example, which is taught in the introductory course in economics schools:

- A field owner has 10 plots.
- To process each plot, one worker is required.
- The first plot yields 1,000.
- The second plot yields 900.
- The third plot yields 800.
- . . .
- The ninth plot yields 200.
- The tenth plot yields 100.

I emphasize that these are unskilled workers, such that each of them can replace another worker. As far as the owner of the field is concerned, there is no problem in swapping the worker who processes the tenth plot and the worker who processes the first plot.

78. *Id.*

79. SMITH, *supra* note 3, at 556.

80. Uri Weiss & Joseph Agassi, *Game Theory for International Accords*, SSRN (March 8, 2020), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3533335.

81. *Id.*

82. *Id.*

83. See Robert J. Aumann, *War and Peace*, 103 PROC. NAT'L ACAD. SCI. 17075, 17076 (2006) (discussing how enforceable contracts can enable cooperation and predictable outcomes through agreement).

84. MARX, *supra* note 61, at 353.

85. SMITH, *supra* note 3, at 556.

In the usual discussion students ask: What is the average contribution of each of the employees to the employer? What is the marginal contribution of each employee to the employer and what will be the wage? Before I turn to these questions, I present the terms: *Average contribution* is the sum of contributions divided by the number of contributors (employees). What, then, is the average contribution of each employee to the employer? The average contribution is 550.⁸⁶ *Marginal contribution* is how much the employer has gained (earned) from the last employee, in other words, how much would they lose if they had one less employee? In this case, the marginal contribution is 100. Thus, if the employer were to give up one of the workers—even the worker who processes the plot with the highest yield, their yield would be reduced by 100. If they are forced to give up the employee who processes the best plot, they would divert the worker who processes the worst plot.

What would be the wage? If the employer employs ten workers, we know that the wage is not more than 100. Thus, no employee earns more than 100. If the employees' salary is more than 100 each, then the employer would prefer to employ less than 10 employees (and if one employee earns more than 100, the employer would prefer to dismiss him). We know that the wage will equal at least the wage that would make the worker indifferent to accepting or not accepting the employment. Therefore, the wage will range between the marginal contribution and the wage of indifference. Thus, we see that the *average* contribution is 550, the *marginal* contribution is 100, and the *wage* is not more than 100.

In the utopian case of perfect competition, one can reach firmer conclusions about the relationship between wages and marginal contribution. Perfect competition is a case in which each player takes the price, in this case the salary, as given. In other words, each player is too small to influence the market wage. None of the players tries to influence the salary, and does not take into account considerations such as if they sell a product cheaply, they will have to sell the rest of the products cheaply, or if they pay a high amount to one worker, they will have to raise the salary for the rest of their employees.⁸⁷ In the case of a perfect competition, and in the case that the marginal contribution of the workers to the employer is diminishing, the employer will employ workers until the marginal contribution from the last hour of work is equal to the wage they pay for this hour of work. In a perfect competition the worker would earn the “market wage.” The market wage is the wage such that if the employer were to offer less than this wage, they would find no worker, and if the worker were to demand more than this wage, they would not find any work.⁸⁸

Economists usually end the discussion of the example at this point, however, the socialist theory continues the discussion. Therefore, there is truth in Marx's statement that

86. It is easy to calculate this: the average production of the most productive worker and the least productive worker is 550, the average production of the second most productive worker and the second-least productive worker is 550, and so on.

87. This is in contrast to a monopoly, where the price is not considered as given, and therefore it is preferred to produce less in order to maintain a high price.

88. “The assumption of perfect competition says, first, that each of the participants is of the opinion that his own transactions do not influence the prevailing prices; second, it is assumed that the same price conditions exist for all participants.” Abraham Wald, *On Some Systems of Equations of Mathematical Economics*, 19 *ECONOMETRICA: J. ECONOMETRIC SOC.* 368, 380 (1951).

his theory is a natural and necessary continuation of the theories of Smith and Ricardo.⁸⁹ The socialist would say, wait, wait, there is exploitation here. Each labourer contributes 550 and receives only 100. A landlord employs many workers, and on average receives the worker's *average* contribution, but pays each worker only their *marginal* contribution, which is much lower! Since the capitalist market is structured so that one landlord employs many workers, and for him, every worker is easily replaceable, there is a relationship of exploitation in the capitalist labour market. But what is exploitation at all?

The extent of exploitation, according to Marx, is the difference between the average contribution of the worker and their salary.⁹⁰ According to this definition, the degree of exploitation that exists in the capitalist system is the delta between the workers' average contribution and their marginal contribution. In the above example, the extent of exploitation will be the difference between the average contribution of the employee (550) and their wage (no more than 100), and therefore, the degree of exploitation in our main example will be at least 450.

The problem with the Marxist definition of exploitation is that it views as exploitation any situation wherein the landlord does not earn zero from the employment of workers. If the owner earns zero, what interest will they have to initiate production? Marx did not consider this as a problem, since the desired situation, from his point of view, is that there would be no landlord at all, the production workers would own the means of production, and each would earn the average contribution.⁹¹ Marx did not recognize that the landlord is entitled to compensation for the risk they take, their land, and management. Brecht's poem illustrates the Marxist attitude towards the landlord's part:

It's just as difficult, so they tell us
To run a factory. Without the owner
The walls would fall in and the machines rust, so they say.
Even if a plough could get made somewhere
It would never reach a field without the
Cunning words the factory owner writes the peasants: who
Could otherwise tell them that ploughs exist? And what
Would become of an estate without the landlord? Surely

89. Marx wrote:

An excellent Russian translation of "Das Kapital" appeared in the spring of 1872. The edition of 3,000 copies is already nearly exhausted. As early as 1871, N. Sieber, Professor of Political Economy in the University of Kiev, in his work "David Ricardo's Theory of Value and of Capital," referred to my theory of value, of money and of capital, as in its fundamentals a necessary sequel to the teaching of Smith and Ricardo. That which astonishes the Western European in the reading of this excellent work, is the author's consistent and firm grasp of the purely theoretical position.

Karl Marx, *Capital Volume I, 1873: Afterword to the Second German Edition of Capital*, MARXISTS INTERNET ARCHIVES, <https://www.marxists.org/archive/marx/works/1867-c1/p3.htm> (last visited on Nov. 22, 2020).

90. Karl Marx, *Capital, A Critique of Political Economy Volume I, Book One: The Process of Production of Capital*, MARXISTS INTERNET ARCHIVES 127–41 (1867), <https://www.marxists.org/archive/marx/works/download/pdf/Capital-Volume-I.pdf> (last visited Nov. 22, 2020).

91. "The proletariat will use its political supremacy to wrest, by degree, all capital from the bourgeoisie, to centralise all instruments of production in the hands of the State, i.e., of the proletariat organised as the ruling class". KARL MARX & FREDERICH ENGELS, *THE COMMUNIST MANIFESTO* 91 (Jeffrey Isaac ed., Yale University Press 2012) (1848).

They'd be sowing rye where they had set the potatoes.⁹²

Before I propose a social democratic definition, I present how Marx continued the discussion, a continuation that I want to make transparent, to declare that I am skipping it. Marx also stated what the workers' wages would be equal to the wages required for them to exist in a minimal existence, including the birth and raising of children.⁹³ Marx, as a student of Ricardo, considered the price of goods as the cost of production.⁹⁴ Thus, since they considered the worker as a commodity in the capitalist market, they considered wages as the cost required to produce the worker: the money required for their existence, including the expenditure on raising children. In Marxist thought, wages in the capitalist market will therefore remain the same, even if there is technological improvement.⁹⁵ The worker will not benefit from it. The worker will earn what they need to have a minimal existence. If a worker demands more than what is necessary for their minimal existence, they will not find a job, since the capitalist can hire another worker for such wages. This stands in contrast to Smith's analysis:

The money price of labour is necessarily regulated by two circumstances; the demand for labour, and the price of the necessaries and conveniences of life. The demand for labour, according as it happens to be increasing, stationary, or declining, or to require an increasing, stationary, or declining population, determines the quantity of the necessaries and conveniences of life which must be given to the labourer; and the money price of labour is determined by what is requisite for purchasing this quantity. Though the money price of labour, therefore, is sometimes high where the price of provisions is low, it would be still higher, the demand continuing the same, if the price of provisions was high.⁹⁶

I now propose a social-democratic definition of exploitation: There is exploitation in the labour relationship, when the profits are divided between the employer and the workers in a way that is clearly disproportionate or in a manner that does not allow them to live in dignity. I intend to propose an open definition; what can be considered as a respectable existence in a specific society at a specific time can be considered as an undignified existence in another period or in another society.

After presenting the problem of exploitation, I turn to the question of how to deal with the problem of exploitation in the labour market, that is, the problem that the worker will gain no more than their marginal contribution, while on average, each worker contributes the average contribution, which is much higher. I present a capitalist response, a Marxist answer, and a social-democratic response. Before the discussion, I emphasize that in this article, I focus on the power gap that arises from the fact that in the competitive market the employer earns the average contribution from the workers' labour, while the worker only receives the marginal contribution, which is lower than the average. I also mention a few other factors in the gaps in power.

First, I quote Adam Smith:

92. BERTOLT BRECHT, *BERTOLT BRECHT POEMS 1913–1956* 296 (John Willet et al. eds., 1979).

93. Marx, *supra* note 90.

94. *Id.*

95. *Id.*

96. SMITH, *supra* note 3, at 76.

The masters, being fewer in number, can combine much more easily; and the law, besides, authorises, or at least does not prohibit their combinations, while it prohibits those of the workmen. We have no acts of parliament against combining to lower the price of work; but many against combining to raise it. In all such disputes the masters can hold out much longer . . .

We rarely hear, it has been said, of the combinations of masters, though frequently of those of workmen. But whoever imagines, upon this account, that masters rarely combine, is as ignorant of the world as of the subject. Masters are always and everywhere in a sort of tacit, but constant and uniform combination, not to raise the wages of labour above their actual rate. To violate this combination is everywhere a most unpopular action, and a sort of reproach to a master among his neighbours and equals. We seldom, indeed, hear of this combination, because it is the usual, and one may say, the natural state of things, which nobody ever hears of. Masters, too, sometimes enter into particular combinations to sink the wages of labour even below this rate. These are always conducted with the utmost silence and secrecy, till the moment of execution, and when the workmen yield, as they sometimes do, without resistance, though severely felt by them, they are never heard of by other people. Such combinations, however, are frequently resisted by a contrary defensive combination of the workmen; who sometimes too, without any provocation of this kind, combine of their own accord to raise the price of their labour. Their usual pretences are, sometimes the high price of provisions; sometimes the great profit which their masters make by their work. But whether their combinations be offensive or defensive, they are always abundantly heard of. In order to bring the point to a speedy decision, they have always recourse to the loudest clamour, and sometimes to the most shocking violence and outrage. They are desperate, and act with the folly and extravagance of desperate men, who must either starve, or frighten their masters into an immediate compliance with their demands. The masters upon these occasions are just as clamorous upon the other side, and never cease to call aloud for the assistance of the civil magistrate, and the rigorous execution of those laws which have been enacted with so much severity against the combinations of servants, labourers, and journeymen. The workmen, accordingly, very seldom derive any advantage from the violence of those tumultuous combinations, which, partly from the interposition of the civil magistrate, partly from the necessity superior steadiness of the masters, partly from the necessity which the greater part of the workmen are under of submitting for the sake of present subsistence, generally end in nothing, but the punishment or ruin of the ringleaders.⁹⁷

Second, in a capitalist market there is, in general, a difference between an employer's risk aversion and an employee's risk aversion. For the employee, risking dismissal can result in losing their entire income (and they may even be starved in societies without a safety net), while an employer would lose only a small portion of their income as a result of the termination of their relationship with a specific employee. The employer is

97. SMITH, *supra* note 3, at 59–60.

sometimes also a firm whose shares are scattered among many owners, therefore, the damage is divided between them. The same is true in the case wherein the employer is the state.

Third, tradition affects labour relations, and it may cause, for example, the perception of certain roles as unsuitable for women. Suffice to mention that, according to Chicago theory (mainly due to GARY S. BECKER), a perfect competition will lead to the elimination of discrimination, because discrimination is irrational behaviour that will not survive in the market.⁹⁸ In contrast, Kenneth Arrow pointed out that discrimination can survive in the market in cases where there are discriminating preferences by consumers or discriminating preferences by employees (for example, working with people of a particular race).⁹⁹ There can also be statistical discrimination. Barak Atiram and Uri Weiss argued that tax could increase the ethnic/gender discrimination in the labour market, since the employer's enjoyment of the discrimination is exempt from tax, while the employer's material profit from the worker is taxed.¹⁰⁰ Joseph Agassi argued that even if the Chicago School's theory of free market influence on discrimination was correct, a law against discrimination in the labour market is still needed.¹⁰¹ Sociologist Yehudit Buber Agassi argued that even if there is legal equality, tradition may cause gaps between the sexes in the labour market.¹⁰² For example, tradition causes inequitable division of labour in the family unit, and this in turn causes inequality in the labour market.¹⁰³ We argue that the theory of Arrow that there is a general equilibrium in the marketplace can explain why Buber Agassi is right: the equilibrium in the job markets may be dependent on the equilibrium in the marriage market.¹⁰⁴

Fourth, power gaps can arise from an agency problem. The agency problem is the problem that the agent acting on behalf of someone, such as on behalf of a firm, may promote their personal good even when they are required to promote the good of the firm.¹⁰⁵ Thus, the superior may use the power that the organization has entrusted to them

98. See generally GARY S. BECKER, *THE ECONOMICS OF DISCRIMINATION* (2010).

99. ORLEY ASHENFELTER, *THE THEORY OF DISCRIMINATION* 3–33 (1973).

100. See generally Atiram Barak & Uri Weiss, *The Discriminative Effect of Taxes* (May 5, 2010) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1600866&download=yes (evaluating relationship between taxation and discrimination).

101. Joseph Agassi, *Discrimination*, in *INTERNATIONAL ENCYCLOPEDIA OF THE SOCIAL SCIENCES* 396–97 (William A. Darity, Jr. ed., 2d ed. 2008).

102. Judith B. Agassi, *Gender Equality: Integrating Work and Parenting*, 4 *HUM. FACTORS IN ORG. DESIGN & MGMT.* 599, 600–04 (1994).

103. *Id.*

104. Kenneth J. Arrow, *General Economic Equilibrium: Purpose, Analytic Techniques, Collective Choice*, 64 *AM. ECON. REV.* 253 (1974). In his nobel lecture Arrow said:

The adjective, “general,” refers to the argument that we cannot legitimately speak of equilibrium with respect to any one commodity; since supply and demand on any one market depends on the prices of other commodities, the overall equilibrium of the economy cannot be decomposed into separate equilibria for individual commodities.

Id. at 254.

105. Jensen and Mackling wrote:

We define an agency relationship as a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent. If both parties to the relationship are utility maximizers

in order to advance the best interests of the firm, to instead advance their personal interests while harming their employees or extorting their employees of their own personal interests, while also harming the best interests of the firm.¹⁰⁶

Fifth, the power gaps can be due to differences in the rate of inter-temporal preference. Simply put, the employees may require more money now. Referring to Smith's words:

In all such disputes the masters can hold out much longer. A landlord, a farmer, a master manufacturer, or merchant, though they did not employ a single workman, could generally live a year or two upon the stocks which they have already acquired. Many workmen could not subsist a week, few could subsist a month, and scarce any a year without employment. In the long-run the workman may be as necessary to his master as his master is to him; but the necessity is not so immediate.¹⁰⁷

It should be noted that the institution of unemployment benefits significantly weakens the power gap mentioned above.

Sixth, the power gaps can be caused by information problems. Sometimes, the market cannot detect an outstanding employee since their performance is not visible to their potential employer, but only to their current employer.¹⁰⁸ This makes them dependent on the employer, for example, for their letter of recommendation, which may provide room for extortion.¹⁰⁹ The game of letter of recommendation is similar to the dictator game: one

there is good reason to believe that the agent will not always act in the best interests of the principal.

Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 308 (1976). Andrei Shleifer and Robert W. Vishny wrote:

The essence of the agency problem is the separation of management and finance, or-in more standard terminology- of ownership and control how can financiers be sure that, once they sink their funds, they This content downloaded from get anything but a worthless piece of paper back from the manager? The agency problem in this context refers to the difficulties financiers have in assuring that their funds are not expropriated or wasted on unattractive projects.

Andrei Shleifer & Robert W. Vishny, *A Survey of Corporate Governance*, 52 J. FIN. 737, 740 (1997).

106. Orit Kamir claimed:

If a supervisor promises promotion to an employee in exchange for sexual pleasure - he uses the resource of the workplace (Professional promotion) to "finance" the personal benefit he acquires himself. If in exchange for the sexual pleasure he produces for himself he ignores lack of professional functioning - it harms the workplace in order to "finance" his personal achievements.

[Translation from Hebrew]. ORIT KAMIR, HARASSED, LIVING WITH ISRAEL'S SEXUAL HARASSMENT LAW 157 (2009).

107. SMITH, *supra* note 3, at 59.

108. This proposition is an application of Spence theory:

In most job markets the employer is not sure of the productive capabilities of an individual at the time he hires him.' Nor will this information necessarily become available to the employer immediately after hiring. The job may take time to learn. Often specific training is required. And there may be a contract period within which no recontracting is allowed. The fact that it takes time to learn an individual's productive capabilities means that hiring is an investment decision. The fact that these capabilities are not known beforehand makes the decision one under uncertainty. To hire someone, then, is frequently to purchase a lottery.

Michael Spence, *Job Market Signaling*, 87 Q.J. ECON. 355, 356 (1973).

109. The Israeli movie *Working Woman* (2018) presented a story of a woman who is sexually coerced by

player decides what would be the benefit of the other, and the other has no say. An alternative to the game of letter of recommendation may be that the contribution of the worker will be transparent, such that the marketplace can see it without the mediation of the boss. This shift will cause much less abuse in work, much less sexual harassment, and much more gain for the firms; it provides much better incentives for their workers to work well. There is actually an agency problem: the interest of the firm is to make the contribution transparent, such that the workers will have effective incentives to excel, while the incentive of the manager may be to blur who achieves what, so that the employer can claim the fame that their agent is entitled to, and the employer can personally exploit their workers and gain their flattery. This is another reason why abusive managers destroy their firms: they distort the incentives of their workers. I raise the question of how the law should handle such an agency problem.

Seventh, the power gaps can arise because the employees have no effective way (or the knowledge required) to exercise their full legal rights. Sometimes, the employees will not realize their rights because they are not aware of it: William L.F. Felstiner et al. made the point that in order to make it practicable for people to go to court they should have the capacity to give a legal name to the event, to blame the ones that are responsible, and to claim in the court.¹¹⁰ Sometimes, they will have to settle for lower amounts, because the employer is a repeat player¹¹¹ or because the legal rule is uncertain,¹¹² and for them, it is more difficult to cope with legal uncertainty.¹¹³ Moreover, labour laws are exposed to the danger of “they judge not the fatherless, neither doth the cause of the widow come unto them.”¹¹⁴ Sometimes the employee will not be able to afford the costs of the trial, such as paying the fee or hiring an attorney.¹¹⁵ If the labour laws are structured such that employees cannot exercise their right without incurring the costs of an attorney from their own pocket,

her boss, who refuses to write her a recommendation letter.

110. See William L.F. Felstiner et al., *The Emergence and Transformation of Disputes: Naming, Blaming, Claiming*. . . , 15 L. & SOC’Y REV. 631, 631–54 (1980).

111. Marc Galanter, *Why The “Haves” Come Out Ahead: Speculations on the Limits of Legal Change*, 9 L. & SOC’Y REV. 95, 98 (1974).

112. See Uri Weiss, *The Regressive Effect of Appealability* (Dec. 21, 2011) (unpublished manuscript), <https://ssrn.com/abstract=1688877> (describing the regressive effects legal uncertainty has on various actors within the legal system). See generally Uri Weiss, *The Regressive Effect of Legal Uncertainty*, 2019 J. DISP. RESOL. 149 (2019) (discussing legal uncertainty).

113. *Id.*

114. *Isaiah* 1:23 (King James).

115. Cappelletti and Garth claimed:

Formal dispute resolution, particularly in the courts, is very expensive in most modern societies. . . This high cost to the parties is particularly obvious under the “American rule,” which does not oblige the losing party to reimburse the successful litigant for his lawyer’s fees; but high costs also serve as a powerful barrier under the more generally used “winner-takes-all” system, where unless the prospective litigant is sure to win, which is very rare indeed given the usual uncertain-ties of litigation, he must face an even higher risk of litigation than a litigant in the United States . . . [i]t is certainly clear that high costs, to the extent ‘that one or both of the parties must bear them, constitute a major access-to-justice barrier. The single most important expense to the litigant is of course attorneys’ fees . . . Any realistic attempt to confront problems of access must begin by recognizing this situation: lawyers and their services are quite expensive.

Mauro Cappelletti & Bryant Garth, *Access to Justice: The Newest Wave in the Worldwide Movement to Make Rights Effective*, 27 BUFF. L. REV. 181, 186–87 (1977).

workers will be subject to the employer's good will, who may act arbitrarily.

Eighth, since the compensation for a work accident is a function of the wage that the employee receives, and the loss of work ability is the main compensation for an accident at work, the tort law encourages employers to risk the weakest workers more and to take fewer precautions. Moreover, the proportion of uncompensated torts in the case of low wage workers appears to be much larger than the proportion of uncompensated torts in the case of high wage workers.¹¹⁶ This is so because traditionally the law compensates for the loss of wages, but not for non-monetary torts, this is particularly valid in a system in which the injuries will not be compensated for the loss of life itself, for emotional damages etc., for the same degree they are compensated for the loss of their wages.¹¹⁷

Ninth, labour relations can be in the shadow of discrimination such as discriminatory laws, colonialism, occupation, or apartheid. Although the great economists, such as Smith and Keynes, view warfare as a part of economic theory, economic theory hardly refers to labour relations in the shadow of an occupation regime.¹¹⁸ However, it is sufficient to say that Smith believed that the colonists operate for economic reasons, but what the colonists do not understand is that colonialism is not profitable.¹¹⁹ One of the major contributions of economic theory is the understanding that discrimination causes damage to the national economy, as it leads to allocation, including an inefficient division of labour (and this is why Backer's introducing of contemporary economical methods to analyse discrimination is so important).¹²⁰ Reducing discrimination in a country will therefore greatly contribute to its national economy. In addition, when a state robs refugees—by, for example, imposing a special income tax on them—their credibility is damaged, which weakens their economy.

Tenth, there is a big difference between the employer's "outside option" and the worker's "outside option." For the employer, one worker's loss is significantly less than the loss of work for the employee (this difference also affects the risk aversion that I have discussed above).¹²¹

116. If the wage loss is compensated and other loss is not compensated, and the other loss is equal in the case of low wage and high wage worker, then the conclusion will be that the proportion of uncompensated torts in the case of low wage workers will be much larger than the proportion of uncompensated torts in the case of high wage workers.

117. See generally Jeffrey Standen, *The Fallacy of Full Compensation*, WASH. U. L.Q. 145 (1995). David Gruning, *Pure Economic Loss in American Tort Law: An Unstable Consensus*, 54 AM. J. COMPAR. L. 187 (2006).

118. KEYNES & VOLCKER, *supra* note 40.

119. SMITH, *supra* note 3, at 530. He explained the economical mistake of the colonialists by this:

They did not consider that the value of those metals has, in all ages and nations, arisen chiefly from their scarcity, and that their scarcity has arisen from the very small quantities of them which nature has anywhere deposited in one place, from the hard and intractable substances with which she has almost everywhere surrounded those small quantities, and consequently from the labour and expense which are everywhere necessary in order to penetrate to and get at them. They flattered themselves that veins of those metals might in many places be found as large and as abundant as those which are commonly found of lead, or copper, or tin, or iron. The dream of Sir Walter Raleigh concerning the golden city and country of Eldorado, may satisfy us that even wise men are not always exempt from such strange delusions.

Id.

120. See generally GARY S. BECKER, *THE ECONOMICS OF DISCRIMINATION* (2d ed., 2010).

121. Caldwell and Danieli claimed "that differences in options explain 30% of the gender wage gap, 88% of the citizen-non-citizen wage gap, and 25% of the premium for higher education." Sydnee Caldwell & Oren Danieli, *Outside Options in the Labor Market* (Nov. 7, 2018) (unpublished manuscript).

Eleventh, Paul Krugman wrote:

America is an open society, in which everyone is free to make his or her own choices about where to work and how to live. Everyone, that is, except the 30 million workers now covered by noncompete agreements, who may find themselves all but unemployable if they quit their current jobs; the 52 million Americans with pre-existing conditions who will be effectively unable to buy individual health insurance, and hence stuck with their current employers, if the Freedom Caucus gets its way; and the millions of Americans burdened down by heavy student and other debt.¹²²

Finally, the gaps in power can stem from social de-legitimization of unemployment, which means that social condemnation of the unemployed undermines the power of the workers. If an employee's dismissal leads to their condemnation, the worker is stimulated by not losing their job, which increases the employer's power.¹²³ To understand the degree of social denigration of the dismissed person, one should approach writers and poets who are sensitive to the human soul.

In Ibsen's *Pillars of Society*, Ibsen describes the fate of the dismissed worker.¹²⁴ From the beginning of the section we can learn about the gaps in power because of the lack of an out option (for an old worker). From the rest of the section we learn about the shame that is cast on the dismissed employee:

Aune (coming a step nearer to him): Mr. Bernick, have you ever realised what discharging an old workman means? You think he can look about for another job? Oh, yes, he can do that; but does that dispose of the matter? You should just be there once, in the house of a workman who has been discharged, the evening he comes home bringing all his tools with him.

Bernick: Do you think I am discharging you with a light heart? Have I not always been a good master to you?

Aune: So much the worse, Mr. Bernick. Just for that very reason those at home will not blame you; they will say nothing to me, because they dare not; but they will look at me when I am not noticing, and think that I must have deserved it. You see, sir, that is—that is what I cannot bear. I am a mere nobody, I know; but I have always been accustomed to stand first in my own home. My humble home is a little community too, Mr. Bernick—a little community which I have been able to support and maintain because my wife has believed in me and because my children have believed in me. And now it is all to fall to pieces.¹²⁵

122. Paul Kurgman, *The Unfreeing of American Workers*, N.Y. TIMES, May 22, 2017, at 25.

123. "Reservation wage is the lowest wage at which an individual would supply labor to a particular market". Robert Hall & Marc Lieberman, *Economics: Principles and Applications*, CENGAGE LEARNING, https://www.cengage.com/economics/discipline_content/preview_guide/preview_guide/PreviewGuide_HallLieberman_5e.pdf (last visited Nov. 23, 2020). Let us conclude: the dismissal of an employee leads to their condemnation, their reservation price is decreased. It is a matter of economically rationality that where unemployed are condemned, people will be ready to work for less.

124. Henrik Ibsen, *The Pillars of Society*, PROJECT GUTENBERG (Feb. 27, 2010), <http://www.gutenberg.org/files/2296/2296-h/2296-h.htm>.

125. *Id.*

In conclusion, the main question in this Part is how to deal with the problem that the worker benefits only as much as the marginal productivity, while the average contribution of workers to employers is much higher. In the labour market, one employer usually employs many workers, and their marginal contribution decreases, therefore, a gap of strength is created between employers and employees (let us remind that according to Marx, the capitalistic production begins when one landlords employs a big number of workers, and this structure leads to an exploitation).¹²⁶ How serious is the problem and how should it be dealt with? I focus on this power gap in this article, but there are a host of other power gaps. These include, for example, gaps arising from the differences in risk aversion, differences in an employee's ability to hold out in the event of an end of contract, an employer's ability to do so, differences in organizational capacity, the vagueness of law, and tradition, as well as information problems and the inability of the weak workers to exercise their legal rights.

In the next two Parts, I present different ways of coping with the power gaps.

III. THE WAY IN WHICH CAPITALISM DEALS WITH THE POWER GAPS BETWEEN THE EMPLOYER AND THE EMPLOYEE

I begin with the capitalist answer that there is no problem in the fact that the worker earns only as much as their marginal contribution to the employer and is certainly not a problem for the state to intervene in.¹²⁷ This is due to reasons of liberty (the labour agreement was created in a free contract, while respecting property rights), efficiency (both sides agreed to the contract and therefore both benefit from it; the market leads to efficient employee allocation), and fairness (the landlord invests their resources and take risks).¹²⁸ Before I describe the capitalist justifications for why there is no problem, I present in the next Section the capitalist approach, and in particular the role of the state according to the capitalist-Smithian approach.

126. See generally MARX, *supra* note 61.

127. "And classical economics said that the answer to almost all problems was to let the forces of supply and demand do their job." Paul Krugman, *Who Was Milton Friedman?*, THE N.Y. REVIEW (Feb. 15, 2007), <https://www.nybooks.com/articles/2007/02/15/who-was-milton-friedman/>.

128. Adam Smith claimed:

Whoever derives his revenue from a fund which is his own, must draw it either from his labour, from his stock, or from his land. The revenue derived from labour is called wages. That derived from stock, by the person who manages or employs it, is called profit. That derived from it by the person who does not employ it himself, but lends it to another, is called the interest or the use of money. It is the compensation which the borrower pays to the lender, for the profit which he has an opportunity of making by the use of the money. Part of that profit naturally belongs to the borrower, who runs the risk and takes the trouble of employing it; and part to the lender, who affords him the opportunity of making this profit. The interest of money is always a derivative revenue, which, if it is not paid from the profit which is made by the use of the money, must be paid from some other source of revenue, unless perhaps the borrower is a spendthrift, who contracts a second debt in order to pay the interest of the first. The revenue which proceeds altogether from land, is called rent, and belongs to the landlord. The revenue of the farmer is derived partly from his labour, and partly from his stock. To him, land is only the instrument which enables him to earn the wages of this labour, and to make the profits of this stock.

SMITH, *supra* note 3, at 46.

A. *The Capitalist-Smithian Approach*

He was without that dithyrambic
 frenzy which wrecks our lives for sound,
 and telling trochee from iambic
 was quite beyond his wit, we found.
 He cursed Theocritus and Homer,
 in Adam Smith was his diploma;
 our deep economist had got
 the gift of recognizing what
 a nation's wealth is, what augments it,
 and how a country lives, and why
 it needs no gold if a supply
 of *simple product* supplements it.
 His father failed to understand
 and took a mortgage on his land.¹²⁹

What are the functions of the state? When should the state intervene in the market or economy? Let us refer to Smith's answer to this question:

According to the system of natural liberty, the sovereign has only three duties to attend to; three duties of great importance, indeed, but plain and intelligible to common understandings: first, the duty of protecting the society from the violence and invasion of other independent societies; secondly, the duty of protecting, as far as possible, every member of the society from the injustice or oppression of every other member of it, or the duty of establishing an exact administration of justice; and, thirdly, the duty of erecting and maintaining certain public works, and certain public institutions, which it can never be for the interest of any individual, or small number of individuals to erect and maintain; because the profit could never repay the expense to any individual, or small number of individuals, though it may frequently do much more than repay it to a great society.¹³⁰

The debate over which goods the state should provide is also a discussion that will affect the scope of the public sector and will therefore shape labour relations. It is known that the public sector has shorter working hours, and therefore enables work even for those who have the burden of raising children.¹³¹ It is also well known that the social tradition is that of gender-unequal division of labour.¹³² However, even if it is agreed that the state should provide a certain product, this is not the end of the argument. The debate then begins

129. A.S. PUSHKIN & MICHAEL BASKER, *EUGENE ONEGIN*, VII (Charles Johnston transl., revised ed., Penguin Books 2003).

130. SMITH, *supra* note 3, at 914–15.

131. “Compared to private sector employees, public sector employees report fewer working hours and less willingness to exert considerable effort on behalf of the organization.” Marc Buelens & Herman Van den Broeck, *An Analysis of Differences in Work Motivation Between Public and Private Sector Organizations*, 67 *PUB. ADMIN. REV.* 65, 67 (2007).

132. See generally Vanessa Cunha & Susana Atalaia, *The Gender (ed) Division of Labour in Europe: Patterns of Practices in 18 EU Countries*, 90 *SOCIOLOGIA, PROBLEMAS E PRÁTICAS* 137 (2019) (describing the unequal division of labour among genders).

as to whether the state should supply it by manufacturing it itself—which will lead to an increase in the public sector employees—or through its acquisition in the private sector. Should the municipality repair its bumps on the street, or should it buy the service? Should the state provide the health services itself or through a contract with external companies?

B. Why is There No Problem of Exploitation in the Above Game from the Capitalist Point of View?

From the capitalist economic approach, the distribution in which the employee earns their marginal contribution while the landlord receives the average contribution is not a problem which demands state intervention in the market or economy, for the following reasons.

1. Efficiency

First, if two sides, the employer and the employee, willingly transact with each other, it means that both of them expect to profit from it, otherwise they would not have given their consent to the transaction. If they repeat it over and over, it means that they both benefit from it. Thus, if the employees agreed to the transaction, they expect to profit from it. This does not mean that a cleaning worker would not prefer a higher salary or to be a CEO, rather that the cleaning worker prefers to be a cleaner over the option of not working. This is how Adam Smith formulated the argument, “trade which, without force or constraint, is naturally and regularly carried on between any two places, is always advantageous, though not always equally so, to both.”¹³³

Smith’s thesis mentioned above is completely contrary to the Mercantilist approach, which was the dominant approach before Smith’s thought revolution.¹³⁴ According to the Mercantilist approach, the rich state is the state that has more money and gold, and therefore it will win the war.¹³⁵ Therefore, in international trade, one country loses what another country earns because one country receives money and gold (for the goods) and another country pays money and gold. Smith also goes against the notion that wealth consists only of money and gold and indicates that they are sometimes only a small part of the capital of a state.¹³⁶

Smith argues that in international trade both countries make a profit, and the evidence is that each give their consent.¹³⁷ In translating his claim into game theory language, Smith argues that the game of (international) trade is not a zero-sum game.¹³⁸ A game is a zero-

133. SMITH, *supra* note 3, at 640.

134. MILL, *supra* note 11, at 621.

135. *Id.*

136. *Id.*

137. SMITH, *supra* note 3, at 639–53.

138. Cho and Moon claimed:

Mercantilism viewed trade as a zero-sum game in which a trade surplus of one country is offset by a trade deficit of another country. In contrast, Adam Smith viewed trade as a positive-sum game in which all trading partners can benefit if countries specialize in the production of goods in which they have absolute advantages.

sum game if, and only if, each time one side favours one result over another, then the other side necessarily favours another result over it. From game theory, one can learn why Smith was right in arguing that trade is not a zero-sum game: If one side prefers a particular agreement over a non-agreement, then the other party prefers no agreement over that particular agreement. From the fact that there is an agreement at all, it can be learned that the players do not play a zero-sum game. This is the case, at least, in cases where the agreement is not fraudulent.

Smith's theory is broader than international relations' theory: it is not true that in one transaction, one party engages the other or if at least one party has earned, it has done so by annihilating the other.¹³⁹ If both parties come to a voluntary deal, both expect to make a profit; if they repeat a deal over and over again, it means that they actually earn from the deal. Before Smith's revolution, it was common to think that there was a fair price, and if a man got rich, he probably sold at an unfair price. As per capitalist thought, a fair price is what the parties have agreed on, as consent means that both parties expect to make a profit.¹⁴⁰

Paul Anthony Samuelson wrote about the abovementioned justification for a free marketplace:

Perhaps the common reason for believing competition to be optimal stemmed from the recognition that no party could be hurt by exchange as compared to his position before trade, since he could always refuse to trade. *Thus, trade is better than no trade; exchange is mutually beneficial; one party does not gain what the other loses.*¹⁴¹

However, he offered to read the justification carefully: "If we examine the argument carefully, we find that it does not really imply that pure competition is optimal, even though properly interpreted it can provide a case against prohibitive tariffs."¹⁴²

Marx did not reject Smith's view that trade is a zero-sum game, since Marx recognized that it is better for the worker to work than to be unemployed, but perceived the capitalistic game as one in which the surplus is distributed unfairly, and one that enables the capitalist to exploit the workers absolutely, such that the worker does not receive more than his/her necessities for a minimal existence, while the capitalist takes the enormous gains. Therefore, Marx supported revolutionarily replacing the game.¹⁴³ Marx is the unacknowledged founding father of the mechanism design theory.¹⁴⁴

139. SMITH, *supra* note 3, at 639–40.

140. John Locke claimed:

Upon demand what is the measure that ought to regulate the price for which anyone sells so as to keep it within the bounds of equity and justice, I suppose it in short to be this: the market price at the place where he sells. Whosoever keeps to that in whatever he sells I think is free from cheat, extortion and oppression, or any guilt in whatever he sells, supposing no fallacy in his wares.

John Locke, *Venditio*, in *LOCKE POLITICAL ESSAYS* 339–43 (Raymond Geuss & Quentin Skinner eds., Cambridge University Press 2004) (1695).

141. PAUL ANTHONY SAMUELSON, *FOUNDATIONS OF ECONOMIC ANALYSIS* 140 (4th ed. 1947).

142. *Id.*

143. KARL MARX, *VALUE, PRICE, AND PROFIT* 127–28 (Eleanor Marx Aveling ed., Charles H. Kerr & Co. 1910) (1898).

144. Marx claimed: "Philosophers have hitherto only interpreted the world in various ways; the point is to change it." Karl Marx, *Theses on Feuerbach*, MARXIST INTERNET ARCHIVE,

Before I present further justifications, I turn to Thomas Schelling's thesis, which shows how to challenge the argument that since both parties enjoy the deal, they should not be interrupted.¹⁴⁵ Schelling's thesis can also indicate the justification for cogent labour laws. Schelling's motivation was to propose a hawkish policy in the Cold War, and he did not recognize that his thesis was a criticism of Smith (basically liberalism, and especially economic liberalism).¹⁴⁶ His thesis supports that contrary to what is commonly believed, in bargaining situations it is sometimes better for people to have less options, intelligence, information, rationality, etc.:

'Bargaining power', 'bargaining strength', 'bargaining skill' suggest that the advantage goes to the powerful, the strong, or the skilful. It does, of course, if those qualities are defined to mean only that negotiations are won by those who win. But if the terms imply that it is an advantage to be more intelligent or more skilled in debate, or to have more financial resources, more physical strength, more military potency, or more ability to withstand losses, then the term does a disservice. These qualities are by no means universal advantages in bargaining situations; they often have a contrary value.¹⁴⁷

Let us see John Nash's definition of a bargaining situation: "A two-person bargaining situation involves two individuals who have the opportunity to collaborate for mutual benefit in more than one way."¹⁴⁸ For example, suppose a statue is worth \$1,000,000 to the collector and \$100,000 for the person who inherited it. In this case, any price that will be higher than \$100,000 and lower than \$1,000,000 would lead to mutual profit, but each party obviously prefers a different price. According to Schelling, the parties have common interests and competing interests in bargaining situations.¹⁴⁹ Therefore, in this example, if the parties have symmetrical bargaining power, then the price of the statue would be \$550,000. However, a party could delete an option for itself (or make it more expensive for itself). For example, suppose the buyer pledges not to pay more than \$300,000, through an oath, a public commitment, a reputation development, or through a courier with a limited, non-changeable power of attorney. If the seller believes the buyer's commitment, then the seller shall agree to \$300,000. Therefore, in bargaining situations, sometimes it pays to be limited, that is, to have a commitment. It should be argued that Schelling does not claim that a player will always benefit from being limited in bargaining situations. Schelling offers various examples of how a person can limit their power, therefore binding themselves, and indeed shows that sometimes a person will benefit from being limited. However, Schelling does not offer a theory, but a refutation—a refutation of the claim that

<https://www.marxists.org/archive/marx/works/1845/theses/theses.htm> (last visited Nov. 22, 2020).

145. See generally Thomas C. Schelling, *An Essay on Bargaining*, 46 AM. ECON. REV. 281 (1956) (discussing the sacrifice of freedom of choice when bargaining).

146. For an example, see generally Thomas C. Shelling, *The Role of Deterrence in Total Disarmament*, 40 FOREIGN AFFAIRS 392 (1962), and his book, THOMAS C. SCHELLING, *THE STRATEGY OF CONFLICT* (Harvard University Press eds. 1980).

147. Schelling, *supra* note 145, at 282.

148. John F. Nash, Jr., *The Bargaining Problem*, 18 ECONOMETRICA 155, 155 (1950).

149. SCHELLING, *supra* note 146, at 4–6. It is interesting to read his words: "Viewing conflict behavior as bargaining process is useful in keeping us from becoming exclusively preoccupied either with the conflict or with the common interest. . . . A 'successful' employees' strike is not one that destroys the employer financially, it may even be one that never takes place." *Id.* at 5–6.

one always gains from having as many options as possible. This is an important refutation, as the liberal would say: It is clear that one cannot lose by having an option. If it is worthwhile for them to use it, they will use it and earn; if it is not worthwhile for them to use it, they will not use it and will not lose. In other words, a person has nothing to lose by having as many options as possible, giving him/her as much freedom as possible. This is true in situations such as Robinson Crusoe's, that is, single-decider situations. However, Schelling shows this is not true in bargaining situations. In such situations, if a person has an option, they can be pressured to use it.

Schelling is primarily concerned with the constraints that a party can bind themselves to, but it can be learned from his insights that sometimes a person can benefit from having the state bind them and that a person can benefit from not having perfect freedom of contract. The following example was suggested in my article on plea deals, written with Dr. Joseph Zohar: Assume that Reuben's optimum is to work five days a week. However, Reuben would rather work seven days a week than be unemployed. Reuben's employer's optimum is that Reuben works seven days a week. Let us assume that all other working conditions are regulated by an external entity and are not changeable. In this case, Reuben and his employer negotiate the range that Reuben will work between five and seven days a week. If the employer has the power to offer Reuben a 'take it or leave it' offer, then the employer would ask Reuben to work for seven days a week, and Reuben would take it.

Now let us change the rules of the game: The law prohibits working for more than six days a week. In that case, the deal would be that Reuben would work six days a week. Therefore, Reuben benefits from the fact that state law restricts him from reaching an agreement whereby he works for seven days a week. In this example, Reuben gained from having limited contract freedom. We can learn from this that it is not always better for parties to have unlimited freedom of contract. However, it should be noted that in this example, it is assumed that all variables other than the number of working days are fixed. One of the criticisms I discuss later in the article on labour regulation is that if the cogent law leads to the employee gaining more in one matter, then the employee will gain less in another matter.

I introduce another justification for the freedom of contract that can be learned from Smith. Smith, in his book *The Wealth of Nations*, deals with the question, what makes nations richer than other nations? Why are there rich nations and poor nations? Smith answers that wealthy nations have a more developed division of labour in the labour market, more specifically with specializations. Consider the following example: Reuben can pick 20 apples an hour or 10 oranges, and Simon can pick 10 apples an hour or 20 oranges. If each one wants to eat a fruit salad that will consist of 20 apples and 20 oranges, and if both make a fruit salad for themselves, each would have to work for three hours. However, if they exchange apples and oranges, they will need only four hours of work together, which means that both can save themselves one hour of work. It is the trade that allows the specialties (in Smith's analysis, trade is the natural tendency of the person pushing to specialize). Taxes, for example, sometimes result in a person providing themselves with a service, even though it was more socially efficient if they would have purchased in the market. Similarly, interventions in labour relations can also cause a person to deliver the service to themselves, even where it would have been more efficient to purchase it in the market.

Another justification for the idea that there is no problem in wages being determined

through the market mechanism can be provided through the first welfare theorem mentioned above. According to the first welfare theorem, in the case of perfect competition, no Pareto improvement will be missed, that is, no possible mutual improvement will be missed. In the absence of factors that prevent efficient transactions, such as information problems, efficient exchanges will not be missed. To do this, no social planner with information about the different preferences of individuals is required. In contrast, the social planner does not have enough information to bring about an assignment in which no mutual improvement is missed. Similarly, if a mechanism such as organized labour or a minimum wage law raises wages, then mutual improvement will be missed in those cases where the law or wages stipulated in the collective bargaining agreement hinders effective transactions. For example, a minimum wage law of \$350, in the prime example we discussed, would prevent the efficient transactions in employing the tenth, ninth, and eighth employees. Moreover, the market mechanism leads to efficient allocation between the various professions. For example, if an employee wants to work where they earn the highest amount, then in a free-market mechanism, they will work in a place that is willing to pay them the highest amount, and this is the place where they are most needed.

In this Section, we have seen justifications of efficiency when the state does not interfere in employee-employer contracts: (1) if the parties have reached a contract, it is a signal that both benefit; (2) the freedom of contract allows each player to focus on their relative advantage, which increases the wealth of a nation; and (3) in perfect competition, where there is no friction such as information problems, we will not miss mutual improvements, which is not true in the case of social planning.

2. *Justifications of Liberty and Fairness*

Another justification that there is no problem in the distribution of wages created by the competitive market mechanism is that the division is created by a fair procedure of respecting property rights and free consent, and therefore its result is right, or at least one that the law should not interfere with. The freedom of contract allows the parties to shape their own relationships. It allows them to legislate for themselves, and more precisely, the freedom of contract allows the parties to set the rules of the game for themselves, and also impose legal obligations on them. A contract transforms the relationship from a relationship that relies on status to one that relies on desire. Milton Friedman, the leading prophet of the capitalistic thought in the second half of the twentieth century, criticizes social democrats for wanting civil liberty but opposing economic freedom.¹⁵⁰ He argues, that the freedom of contract and the freedom to choose occupation are part of freedom, and that political civil liberty cannot be achieved without economic freedom. The mechanism of a socialist regime would lead to the loss of the civil-political.¹⁵¹ Friedman in *Capitalism and Freedom* replies to Marx in these words: “The achievement of allocation of resources without compulsion is the major instrumental role in the market place of distribution in accordance with product.”¹⁵² Another capitalist justification for wages being set through

150. See generally MILTON FRIEDMAN, *CAPITALISM AND FREEDOM* (1962).

151. See generally FRIEDRICH AUGUST HAYEK, *THE ROAD TO SERFDOM: TEXT AND DOCUMENTS: THE DEFINITIVE EDITION* (Bruce Caldwell ed., 2007) (advocating that government should not have a role in economic decision making).

152. FRIEDMAN, *supra* note 150, at 200.

the market mechanism could be, for example, that if a person has a field and employs workers and takes on risk, they deserve to earn. They deserve compensation for land, management, and risk. Had it not been for the homeowner who set up the factory, the employees would not have built it. Friedman attempts to refute Marx by pointing to his internal contradiction: On one hand, Marx criticizes the free-market method of exploiting workers (i.e. they do not receive their income from the product), and on the other, according to his model, wages do not depend on GDP, but on necessity.

To sum up this Part, according to the capitalist approach, the state should not intervene in the market except in cases of breach of contract, fraud, etc., or in cases where it is the supply of a public product. The main justification for the freedom of negotiation is that if two parties agree on a deal, both of them expect to profit from it. Another justification is respect for the freedom of the parties to determine for themselves the rules of the game that will regulate their relationship.

IV. THE SOLUTIONS OFFERED IN THE SOCIAL-DEMOCRATIC APPROACH

I turn to four social-democratic solutions to the problem of power disparities in the labour market: regulation (cogent laws), unemployment benefits and minimum income guarantees, transitions to organized labour, and wealth transfers through tax laws.

A. Regulation and Unemployment Benefits and Minimum Income Guarantees

Cogent laws prevent parties from shaping their relationships as they choose. They impose a legal restriction on designing free relationships between parties.¹⁵³ In doing so, they restrict the freedom of contract. A simple example of a cogent law is a law that requires the employer to pay the employee a minimum wage. Even if the employee agrees to work for less than the minimum wage, there will be no legal validity of their consent, and the employer will still be required to pay the employee the minimum wage. The legislature can also determine that it is a criminal offense on the part of the employer to pay the employee less than the minimum wage.

Key mandatory laws that social democrats support are the Minimum Wage Act, anti-discrimination laws, anti-sexual harassment laws, legislation that limit working hours, workers' entitlement to sick days, statutes requiring pension benefits for the employee, and so on.¹⁵⁴ In addition, legal institutions such as "Good Faith" or "Unenforceability on Grounds of Public Policy" can be used by the court to intervene in the freedom of contract in employment relations. For example, courts may see a non-compete clause as unenforceable.

To what extent can regulation actually protect workers? I focus here on the minimum wage law. What would happen if there were a minimum wage law of \$300 in the story presented in the main example of our article? In other words, what will happen in the *new*

153. "The term "dispositive law" designates those rules which can be "disposed away" by the parties. "Cogent law," on the other hand, refers to rules which override party stipulations". George G. Hoff, *The Intensity Principle in the Conflict of Laws: The Force of Legal Rules as a Factor in Selecting the Law Applicable to a Conflicts Controversy*, 39 VA. L. REV. 437–58, 448 (1953). HEINRICH DERNBURG, SYSTEM DES ROMISCHEN RECHTS 49 (8th ed. 1911).

154. See generally Keith Ewing, *Democratic Socialism and Labour Law*, 24 INDUS. L.J. 103 (1995) (listing issues social democrats support).

game that will be created by a minimum wage law? This time, the wages of all unpaid workers will be raised to \$300, but the employer on their part will fire the two employees who produce less than \$300. On one hand, minimum wages raise workers' wages, and on the other hand, they impose unemployment on workers who cannot produce value that is equivalent to the minimum wage.

The argument that the minimum wage law leads to unemployment can be challenged as follows: minimum wage leads to a rise in consumption; the rise in consumption leads to more workplaces, which leads to an increase in consumption, and so forth. True or not, this argument does not challenge the argument that a minimum wage forces anyone who cannot produce value that is equivalent to the minimum wage not to work but argues that a minimum wage leads to an increase in unemployment.

What, then, would be the case for those people who cannot produce value that is equivalent to the minimum wage? These people would be sentenced to unemployment or illegally employed. Therefore, the minimum wage debate should be conducted in conjunction with the debate on unemployment benefits, income support, etc. The justification of minimum wage should be a function of unemployment benefits and the minimum guaranteed income. If a safety net is not deployed for those who do not work, then the minimum wage law is essentially demanding the person who cannot produce value that is equivalent to the minimum wage and who does not have economic reserves, to starve or to illegally employed.

Minimum wages without unemployment benefits and ensuring a minimum income can therefore hurt the weakest workers—those who are unable to produce a product that at least equals the minimum wage. An effective minimum wage raises the welfare of all employees but sacrifices the weakest workers. If this argument is accepted, then from a Rawlsian point of view—that introduces to select a policy that would benefit the weakest group—the Minimum Wage Act should be rejected in the event that there are no unemployment benefits or income guarantees.¹⁵⁵ However, the answer to this may be that without a minimum wage there would be more unemployment because the minimum wage increases the ability to consume, and even if it forces people into unemployment, the absence of a minimum wage will be more significant.

I turn to a brief review of the claims raised in this regard: Nicolas Marceau and Robin Boadway have argued that sometimes the optimal welfare policy is the combination of the minimum wage and unemployment insurance.¹⁵⁶ They perceive unemployment insurance as an appendix to minimum wages, in the context of the unemployment caused by the minimum wage.¹⁵⁷ They state that the unemployment insurance analysis should be different in cases of non-voluntary unemployment, such as in the case of unskilled workers,

155. Banerjee claimed:

But Rawls does not require work to be a basic right, nor does he require the government to have a full employment policy or set a minimum wage standard because these would interfere with the functioning of a more or less free market economy.

Mahasweta M. Banerjee, *Applying Rawlsian Social Justice to Welfare Reform: An Unexpected Finding for Social Work*, 32 J. SOCIO. & SOC. WELFARE, Sept. 2005, at 43–44.

156. Nicolas Marceau & Robin Boadway, *Minimum Wage Legislation and Unemployment Insurance as Instruments for Redistribution*, 96 SCANDINAVIAN J. ECON. 67, 67 (1994).

157. *Id.*

when there is an effective minimum wage.¹⁵⁸

Yoram Margalioth argued that a minimum wage promotes distributive justice only on the assumption that it does not lead to unemployment.¹⁵⁹ A minimum wage may be a worthwhile tool for remedying certain market failures if we assume an effective labour market, that is, if the minimum wage is higher than the rate required to correct labour market failures, the minimum wage will promote distributive justice only if complementary policies are introduced that equip the unemployed or compensate them.

Precisely, if one accepts the argument that a minimum wage causes unemployment, it should draw compensation to the employees who are denied the right to work at a lower wage than the minimum wage—a situation that forces them to unemployment. This denial of their right to work is appropriate (i.e. to maximize the value of the unskilled labour group), but to be proportionate, their hardship must be compensated. Otherwise, it is disproportionate, since the public interest seems to be achieved in a way that is less prejudicial to human rights.

I therefore propose to discuss the argument that, by virtue of the right to work, the right to unemployment benefits and income security is constitutional, with the state imposing restrictions such as the Minimum Wage Act on the free play of the market.

Furthermore, when there is an effective minimum wage law, unemployment benefits are a necessary condition for the rule of law to exist. A minimum wage law without unemployment benefits is a decree upon the community that most of the community is not able to abide by it, and one should not expect a person to starve and refuse to work for less than the minimum wage.¹⁶⁰ Therefore, a minimum wage law without unemployment benefits or income guarantees necessarily leads to systematic violation of the law. Ironically, it is precisely the anticipated penalty for employers who violate the Minimum Wage Law, that lowers the market wages of those workers who are employed at less than the minimum wage, since the expected penalty reduces employers' willingness to pay employees. When the deal imposes a 'fine' on the buyer, it lowers the price.

In addition, in the case of minimum wages, some of the justifications for avoiding unemployment benefits/income support are also crumbling. The Chicago School of Economic Theory argues that perfect competition leads to no unemployment,¹⁶¹ since the unemployed is the one who does not work at the market price. If there is unemployment, then market wages will drop until there is full employment. If so, why is there unemployment anyway? Free market economists explain this as a friction of theory, that this is short-term unemployment, and it will disappear in the long run. To which Keynes replied: "In the long run we are all dead."¹⁶² However, if there is a minimum wage law,

158. *Id.*

159. Yoram Margalioth, *Tax Law*, in *ECONOMIC ANALYSIS OF LAW* (Uriel Procaccia, ed., Harry & Michael Sacher Inst. for Legis. Rsch. & Compar. L., 2013).

160. The Talmud says: "our Sages relied upon the statement of Rabban Shimon ben Gamliel and upon the statement of Rabbi Elazar bar Tzadok, who would say: The Sages issue a decree upon the community only if most of the community is able to abide by it." *Avodah Zarah* 36a (William Davidson).

161. See generally Robert L. Hetzel, *The Contributions of Milton Friedman to Economics*, 93 *FRB RICHMOND ECON. Q.* 1 (2007) (describing the Chicago School of Economic Theory).

162. N. Gregory Mankiw, *What Would Keynes Have Done?*, *N.Y. TIMES* (Nov. 28, 2008), <https://www.nytimes.com/2008/11/30/business/economy/30view.html>.

even Chicago economists will admit that there will necessarily be unemployment!¹⁶³ Therefore, it is no longer appropriate to dismiss the unemployed, whose unemployment lies in their idleness and laziness. Also, the argument that unemployment benefits will encourage unemployment is very weak when there is a minimum wage law, since there will necessarily be unemployment in the presence of a minimum wage law.

If the Minimum Wage Law causes the unemployment of 50,000 unskilled workers in society, as long as the number of unskilled workers who prefer unemployment benefits over work is below 50,000, there is no harm from the incentive that unemployment benefits provide. With or without unemployment benefit, the number of unemployed in such a market would be 50,000. Under such conditions, no unemployment benefit will add one unemployed person. Generally, if the Minimum Wage Act necessarily results in the unemployment of X unskilled workers, then the harm resulting from unskilled workers preferring unemployment benefits is zero, as long as the number of workers who prefer unemployment benefits over employment is less than X . This is so since in this case, one unskilled worker who chooses unemployment benefits over work results in replacing one unemployed worker with one employee. In this game the minimal possible unemployed unskilled workers is X , and thus when the number of unemployed unskilled people is X , the pressure cannot reduce the number of unemployed unskilled people, but only to lead one person to go into the marketplace, what leads to the layoff of another one.

In fact, the replacement here is of those who prefer unemployment benefit over minimum wage with someone who prefers minimum wage over unemployment benefit. In the case mentioned, if the unemployed are pressured to get a job—while being denied unemployment allowance—it causes damage to the national economy (since it decreases the net social benefits). Therefore, even if a certain program for bullying the unemployed has “succeeded” in reducing unemployment in a country with a low minimum wage law, it cannot be assumed that it will succeed in a country with a high minimum wage law. I explain it as: Let us take this hypothetical example in order to, illustrate the theory. Imagine that one country has a high minimum wage and it imposes 5% unemployment, while another country has a low minimum wage and it imposes 1% unemployment. We also assume that in each of the countries there is 5.1% unemployment, and there is an unemployment benefit. In each country, there are people who choose not to work for the minimum wage, and the government is beginning to pester the unemployed. In the country with low minimum wage, the upper bound of success of such pestering, is unemployment reduction by 4.1%, while in the country where the minimum wage is high, the upper bound of unemployment reduction is 0.1%. Even in a country with a high minimum wage, far more than 0.1% of the population is unemployed, and bullying of the unemployed may cause them to change their choices, but in this case, unemployment cannot fall by more than one-tenth of the percentage, and more people joining the labour market (beyond 0.1%) will cause other layoffs. It would only make unskilled workers who wanted to work find themselves unemployed, they would be replaced by unskilled workers who did not want to work. One of the practical conclusions of the discussion is not to be enthusiastic about bullying programs for the unemployed that have succeeded in countries where there

163. See generally George J. Stigler, *The Economics of Minimum Wage Legislation*, 36 AM. ECON. REV. 358 (1946). Stigler is the 1982 laureate in Nobel Memorial Prize in Economic Sciences and considered to be a key leader of the Chicago School of Economics.

is a much lower minimum wage than in the state that is considering adopting the program.

Moreover, unemployment benefits are important beyond the compensation of those who lose due to the minimum wage law. An important justification for unemployment benefits can be learned from “search theory” economists. They ask: When will a rational person stop searching and get a job? The answer they offer: They will accept the job if, and only if, the salary is higher than their indifference wage; that is, the indifference wage is the benefit of continuing the search given their beliefs about their chances of finding a job. The higher the unemployment benefit, the higher the wage rate will be, and this will raise the wage in the labour market. When there are large unemployment benefits, employees will be able to look for work over time and not jump on the first job they find. Since we do not live in a world of perfect information, a person must be financially stable in order to find the job for which they are paid the highest salary (traditionally we have not had a theory of how to find a job, and the difficulty to find a job was a “friction” of the theory, and thus the search theory is such important theory: this theory teaches us about the important of unemployment benefits, since we do not live in a world of perfect competition without friction).¹⁶⁴

Unemployment benefits also have benefits in dealing with other employer-employee gaps in strength. When there is unemployment benefit, it is easier for employees to leave the workplace, and they are therefore less constrained. Unemployment benefits are also likely to reduce workplace bullying and sexual harassment. If there is no unemployment benefit and the worker has no financial reserves, leaving the job even in the event of harassment may not be practical; therefore, the employer would be more extortionate and the workers’ threat of legal prosecution will be less credible as continued work in the workplace prevents a legal claim. Of this, Auden said: “Hunger allows no choice [t]o the citizen or the police.”¹⁶⁵ In contrast, in the presence of unemployment benefits, the employee has an effective “exit,” which is why they are less susceptible to extortion and their threat to file a lawsuit is more reliable.

After the criticism that minimum wages could cause unemployment, I now provide a more general critique of the protective laws at work. Law and economics analysts criticize the laws that intervene in the labour market by requiring the employer to provide the employee with facilities such as sick days, severance pay, etc., that would make the

164. This conclusion is a great achievement of the “Search Theory,” that won a Nobel prize in economics. Diamond claimed: “Search theory is designed to help make sense of these flows and to frame analysis of related government policies such as unemployment benefits. Considering “ordinary” times, captured by a rational expectations model set in a steady state, a primary purpose of unemployment benefits is to provide insurance to workers against involuntary job loss. The provision of insurance affects the willingness of workers to accept particular jobs, making it more attractive to pass up some opportunities in expectation of doing better later. And it affects the diligence of job search. This is always the case with insurance with asymmetric information—the provision of insurance affects behavior, commonly referred to as a moral hazard problem. Of course, there are behavioral changes that reflect income effects and can have a positive efficiency implication as well as those that reflect substitution effects and can have a negative efficiency implication. The negative effects do not mean one should not have insurance, but that the strength and design of the insurance should take into account the behavioral responses it induces. Less diligent search and greater willingness to wait for a future job make it harder for employers to find workers but easier for other workers to find jobs.” See Peter Diamond, *Unemployment, Vacancies, Wages*, 101 AM. ECON. REV. 1045, 1052–53 (2011); see generally Christopher A. Pissarides, *Equilibrium in the Labor Market with Search Frictions*, 101 AM. ECON. REV. 1092 (2011).

165. W.H. Auden, *September 1, 1939*, POETS, <https://poets.org/poem/september-1-1939> (last visited Nov. 23, 2020).

employee less likely to work elsewhere.¹⁶⁶ For example, if the legislature requires the employer to pay the employee \$200 every Sunday, it will not change the employee's salary; the total amount will be deducted from their salary at the end of the month. If the employer is obliged to give the employee sick leave or advance notice, this will reduce the employee's salary. Moreover, the employee's loss elsewhere is likely to be higher than the right they have received. This is why the parties prefer a contract that is preferable to both over a discount contract for both; and if they choose to pay money rather than sick days or advance notice, such a contract is preferable to both, unless there are market failures such as externalities or information problems (e.g. employees may not ask for sick days so as not to lose pay; it is precisely in this case that employees generally will benefit from regulation that provides sick days as a cognitive right). Consider, for example, a case where the cost to the employer of giving the employee the right is X . If the right is worth more than the employee by X , the employer and the employee agree that the employee will receive the right to a reduction in wages, a reduction that ranges between X and the value of the right for the employee. However, if the right is worth less than X in the eyes of the employee, then both parties would prefer that the law does not impose such a right unless the regulation prevents the reduction elsewhere (for example, if it is a minimum wage employee, then the employer may not employ the employee, but cannot reduce their salary when there is a rule of law). The protective regulation prevents them from moving from contract A, which has the curtailing obligation, to contract B, which does not have the curtailing obligation, even when the transition is preferable to both parties.

The above criticism of social democratic legislation is widespread among law and economics scholars and itself merits the following criticism: Their criticism of labour regulation should not rest on an implicit assumption that this is a competitive market without regulation and trade unions. In such a market, indeed, if the legislature requires the employer to pay an X -fee allowance, the legislation would result in a reduction of X from his/her salary. However, let us consider the next two games. In the first game, there is a minimum wage, and the state now imposes an X -fee travel allowance. In that case, the employer will not be able to lower the wages of those earning minimum wages by X , or more precisely, the wages of those earning a minimum wage plus X . It is possible to reduce to X at most. In the second game, suppose there is no government regulation, but wages are set in a collective labour contract. Now, the government changes the game and adds the right to an X -fee allowance. Will the workers' union agree to lower the X -pay wage? Keynes criticised the economic analysis that preceded him as: The analysis assumes that if there is deflation, workers will agree to lower their wages, so that in real terms, they will continue to earn the same amount. Keynes argued that in this case the workers would refuse to reduce their wages.¹⁶⁷ Similarly, I argue that the workers' union would not agree to a

166. Schwab claimed that era one of law and economics emphasizes that labour laws and mandatory employment rules might reduce overall social welfare by preventing a benefit or term from going to the party that values it most highly". Stewart J Schwab, *Law-and-Economics Approaches to Labour and Employment Law*, INT'L J. COMPAR. LAB. L. 115, 115 (2017). See also Richard A. Posner, Labor Law Lecture, LAB. AND EMPLOY. COLLEGE (Apr. 27, 2000), <https://www.laborandemploymentcollege.org/pdfs/Lecture042700.pdf>. See generally Richard A. Epstein, *A Common Law for Labor Relations: A Critique of the New Deal Labor Legislation*, 92 YALE L.J. 1357 (1983).

167. Keynes claimed: "In fact, a movement by employers to revise money-wage bargains downward will be much more strongly resisted than a gradual and automatic lowering of real wages as a result of rising prices."

pay cut in response to the new beneficiary legislation.

Ironically, the law and economics schools' criticism of the ineffectiveness of protective legislation is reminiscent of Marxist criticism;¹⁶⁸ this may not come as a surprise, as the school of law and economics also emerges from legal realism that, like the Marxist approach, does not consider law as an instrument to change reality. Marx criticized workers' organizations for trying to change the effects of the price mechanism rather than changing the mechanism itself:

Trades Unions work well as centers of resistance against the encroachments of capital. They fail partially from an injudicious use of their power. They fail generally from limiting themselves to a guerilla war against the effects of the existing system, instead of simultaneously trying to change it, instead of using their organized forces as a lever for the final emancipation of the working class that is to say, the ultimate abolition of the wages system.¹⁶⁹

Law and economics scholars are similar to Marx in that they believe that in order to lead to a good contract, it is impossible to rely on legislation to change the effects of existing power relations.¹⁷⁰ If law and economics scholars are right in saying that the rights granted by labour regulation are ineffective because they result in a pay cut, and blocking the pay cut will result in layoffs,¹⁷¹ these are good reasons for unemployment benefits and minimum income assurance and organized labour encouragement.

I end the discussion on labour regulation with a few questions: How much protection could protect workers? One possibility is that protective laws create a kind of cartel, which raises employee wages but causes other workers to be dismissed. The welfare of all disadvantaged workers grows, but workers will be laid off. One of the questions raised is: What will happen to them? I support compensation through unemployment benefits and a minimum income guarantee. However, can regulation benefit beyond its cartel effect, protecting the group of workers? Is it possible to deduce from the thesis that, even in a negotiated situation, the employee can benefit from their restriction? I have presented an example above, in which the employee benefits from having limited contract freedom, but the employer and the employee negotiated only one variable—working days. When, then, does the employee benefit from labour contract regulation? To what extent is total regulation required in cases where there is partial regulation, as partial regulation will only cause the employee to pay an unpaid price for the right?

To summarize the section: One of the main ways to deal with labour market disparities

JOHN MAYNARD KEYNES, *THE GENERAL THEORY OF EMPLOYMENT, INTEREST, AND MONEY* 233 (1964); *see generally* JOHN MAYNARD KEYNES, *A TRACT ON MONETARY REFORM* (1923).

168. Posner claimed:

I have a theory about the "new" labor law, which will occupy my in the remainder of this talk; and it is that it is largely illusory so far as actual effects on employment practices is concerned. It increases the cost of labor to employers, and most of that cost is probably borne by the workers themselves; it may actually reduce employment opportunities for the protected classes; and it probably does not deter much discrimination.

Posner, *supra* note 166.

169. MARX, *supra* note 143.

170. Posner, *supra* note 166.

171. *Id.*

and the low wage problem is through regulation. Alongside their advantage, mandatory rules have two main problems. The first problem is that cogent laws, in particular the Minimum Wage Act, may result in the dismissal of employees, as it would not be worthwhile for an employer to employ employees whose marginal contribution to the employer is less than the minimum wage plus all other mandatory costs imposed by the legislature.¹⁷² The second problem is that if the employer is required to grant the employee a certain right, such as the right to a travel allowance, then the employer may reduce the employee's salary or any other benefit that would otherwise be given to him (this is how Omri Ben Shahar & Yuval Procaccia summarized the contribution of the law and economics movement to criticize those kinds of intervention in the freedom of contracts).¹⁷³ The regulation of labour can result in a situation wherein, instead of the employee and employer choosing a certain package of pay and benefits, they will choose another package of pay and benefits, even though the other package is less desirable for both parties. A key lesson from the discussion, therefore, is that a minimum wage must incur unemployment benefits and a minimum income guarantee, in order to compensate the aggrieved. I also suggest that the restriction on the right to work of the weak worker, through minimum wage laws, should incur a constitutional right to unemployment benefits and to a minimum income guarantee in order to make the loss proportionate. Unemployment benefits also change the working relationship in a way that gives the worker a practical exit, and therefore the worker is protected from phenomena such as work abuse and sexual harassment. They allow the employees flexibility in the search for work, helping them to choose more rewarding jobs. When there is a minimum wage, the fear that unemployment benefits will provide an incentive not to work should be much smaller. Additionally, there is the other side of the coin: If bullying programs have been able to reduce unemployment in places that have a low minimum wage, it is wrong to conclude that such a program will also succeed where there is a high minimum wage. A second key lesson to be learnt from the discussion is that mandatory labour rules are particularly effective when it comes to weak workers, such that the employer cannot reduce their wages as a result of the new protection they receive. They are also more effective in cases where labour organizations will not agree to a wage cut as a result of a new benefit, or when, in the case of civil servants, the state will not respond to the legal benefit in reducing their wage.

172. Gary Becker, *It's Simple: Hike the Minimum Wage, and You Put People Out of Work*, BUS. WEEK (Mar. 5, 1995, 11:00 PM), <https://www.bloomberg.com/news/articles/1995-03-05/its-simple-hike-the-minimum-wage-and-you-put-people-out-of-work>. On the other hand, Samuelson and Nordhaus claimed:

Most studies indicate that a 10 percent increase in the minimum wage would reduce employment of teenagers by between 1 and 3 percent. The impact on adult employment is even smaller. Some recent studies put the adult employment effects very close to zero, and one set of studies suggests that employment might even increase.

P. A. SAMUELSON & W. D. NORDHAUS, *ECONOMICS* 100 (19th ed. 2010).

173. See Omri Ben Shahar & Yuval Procaccia, *The Economics of Contract Law*, in *THE ECONOMIC APPROACH TO LAW* 153 (Uriel Procaccia ed., Sacher Institute for Legislative Research and Comparative Law Press, 2012).

B. Trade Unions

Another way to reduce the exploitation problem is to reorganize the bargaining unit: instead of a personal negotiation between the employer and the employee, collective bargaining between the employee and the employer will take place. In personal negotiations, the employee threatens the employer that if they do not raise his/her salary, then he/she would not work for them. This is a weak threat. The employer can replace the threatening employee with another worker, or at most, lose the marginal contribution of that worker. Conversely, in collective bargaining, the threat posed by the workers is different: If you, the employer, do not raise our wages, then we will all strike/resign. If one cleaning worker resigns, it is negligible for a municipality, and it can easily find another cleaning worker. However, if all cleaning workers strike/resign, the city is paralyzed.

I return to the main example of this article. Above, I analysed the following game of unorganized work: a homeowner employs 10 workers. The best plot yields 1,000, the second plot, 900; the third plot, 800; and the last plot, 100. The landlord employs ten workers, and the workers are not organized. In this case, none of the employees will earn more than 100, because if the wage is more than 100, the landlord would prefer to employ less than 10 employees. Therefore, in this game, no worker will earn more than their marginal contribution. The landlord is better off dismissing a worker who earns more than their marginal contribution.

Below is another game, which is a variant of the game I analysed. In this game, employees have a workers' organization, and they can retire or resign *collectively*, or at least *collectively* stop working. What will be the result of the bargaining? The range of possible bargaining outcomes is the range of preferential agreements for both parties over a non-agreement. The landlord would certainly not agree to pay the workers more than their average contribution (\$550), because no agreement is better for the landlord than paying more than \$550. The workers on their part will not accept less than their indifference wages. Suppose it is equal to their marginal contribution in the previous game; in perfect competition, the landlord employs employees to the point where their marginal contribution equals their wages. If the worker's indifference wage is \$100, then the negotiation range is between \$100 and \$550. If the bargaining power is symmetrical, then the labour wage will be 325. $[(550 + 100) / 2]$. We can see that the transition from personal to collective bargaining in this example raises wages from \$100 to \$325, from the employee's marginal contribution to the average of the marginal contribution and the average contribution.

However, how is it possible that this time the landlord agrees to hire workers with higher wages than their marginal contribution? If the wage is \$325, the landlord would be better off dismissing the tenth, ninth, and eighth labourers! The answer is that such an agreement is possible because this time the negotiations are not personal, but collective. Trade unions can demand not only higher wages, but also not to lay off workers. An agreement in which the landlord employs ten workers at a cost of \$325 is preferable to the landlord from a no agreement situation if no agreement means that none of the workers will work. Therefore, such an agreement is possible.

Organizing therefore greatly improves the condition of the workers. When the bargaining power is symmetrical, their exploitation by the Marxist index drops by 50%. Of course, trade unions have disadvantages, as here described: First, collective bargaining can

lead to strikes.¹⁷⁴ The negotiations between the employer and the employee are a good approximation of bilateral monopoly negotiations, and such negotiations sometimes explode. If either party requires more than 50% of the surplus created by the agreement, then the agreement will be blocked (it is enough that both together will require more than 100% of the surplus in order to block agreements). Strikes can occur because of information problems, for example when a particular party is optimistic about the compensation, they can receive in the event of a strike.¹⁷⁵ Moreover, if each party commits itself to demand more than 50% of the surplus generated by the agreement, then the negotiations will explode.¹⁷⁶

Let us further examine this point: Perfect competition is one game, and bilateral negotiations are another. Each player in the competition sees the market price as a given, and therefore there is no range for negotiation; no worker can insist on getting more than the market wage, and no homeowner can insist on paying less than the market wage. (We are here students of Abraham Wald, one of the most important scholars of decision theory and economics).¹⁷⁷ Conversely, negotiation is a situation where the parties have the opportunity to gain from collaboration, but they can come to collaborate in more than one way, and usually, each party prefers a different way.¹⁷⁸ Negotiations have conflicting

174. David Card claimed:

A first-order fact about private sector bargaining in North America is that 10-15 percent of contract negotiations involving relatively large numbers of workers lead to a work stoppage. Two U.S. studies with broad industry coverage (Cynthia Gramm, 1987; Sheena McConnell, 1987) estimate the average probability of strikes among contract negotiations with 1000 or more workers at 13 percent. A Canadian study by Morley Gunderson et al. (1986), covering contract negotiations with 200 or more workers, estimates a similar 13 percent dispute rate. The incidence of strikes is slightly higher in manufacturing industries, and also varies substantially across narrowly defined manufacturing industries.

David Card, *Strikes and Bargaining: A Survey of the Recent Empirical Literature*, 80 AM. ECON. REV. 410, 411 (1990); Cynthia Gramm, *New Measures of the Propensity to Strike During Contract Negotiations, 1971-1980*, 40 INDUS. & LAB. RELS. REV. 406 (1987); Sheena McConnell, *Cyclical Fluctuations in Strike Activity*, 44 INDUS. & LAB. RELS. REV. 130 (1990); Morley Gunderson et al., *Logit Estimates of Strike Incidence from Canadian Contract Data*, 4 J. LAB. ECON. 257 (1986).

175. "Our view is that disputes largely are motivated from the presence of private information and the sharply conflicting interests of the union and the firm over the wage." Peter Cramton & Joseph Tracy, *Unions, Bargaining and Strikes*, in INTERNATIONAL HANDBOOK OF TRADE UNIONS (John T. Addison and Claus Schnabel, eds.) (2002), <https://core.ac.uk/download/pdf/6960651.pdf>.

176. Thomas Schelling claimed:

If the union is going to insist on \$2 and expects the management to counter with \$1.60, an effort is made to persuade the membership not only that the management could pay \$2 but even perhaps that the negotiators themselves are incompetent if they fail to obtain close to \$2. The purpose-or, rather, a plausible purpose suggested by our analysis-is to make clear to the management that the negotiators could not accept less than \$2 even if they wished to because they no longer control the members or because they would lose their own positions if they tried . . . they [all his examples – U.W] all run the risk of establishing an immovable position that goes beyond the ability of the other to concede, and thereby provoke the likelihood of stalemate or breakdown.

Schelling, *supra* note 145, at 286–87.

177. Abraham Wald, *On Some Systems of Equations of Mathematical Economics*, 19 ECONOMETRICA: J. ECONOMETRIC SOC. 368, 380 (1951). See generally Douglas Gale, *Bargaining and Competition Part I: Characterization*, 54 ECONOMETRICA: J. ECONOMETRIC SOC. 785 (1986).

178. Nash claimed:

interests alongside common interests. In the above example, any salary higher than \$100 but lower than \$550 results in mutual improvement, but each party prefers a different mutual improvement. The workers' union can therefore commit itself to reject any offer in which the union receives less than a certain wage, and the employer can restrain himself from agreeing to pay more than a certain wage. If the employer commits himself to lower wages than the workers commit themselves to, there cannot be an agreement unless at least one of them cancels their commitment.

Second, like minimum wages, raising workers' wages can encourage layoffs or prevent employers from hiring additional employees.¹⁷⁹ If the outcome of the negotiations is that the wages of employees are higher than their marginal contribution, then the landlord is encouraged to fire employees. Of course, employees can negotiate both wages and the number of workers at the same time, so layoffs because of raising wages through the Minimum Wage Act could be avoided through collective bargaining.¹⁸⁰ While the Minimum Wage Act causes an employer to fire all employees who produce a value lower than the minimum wage, in the case of organized labour, employees may require an agreement that the landlord will avoid laying off employees. However, employees would not require the landlord to hire new employees. Therefore, even if, in the prime example above, the employees agree with the employer on a salary of \$325 and the absence of dismissal, then if three employees retire, it would not be worthwhile for the employer to replace them if the agreement does not require it. Organized work can therefore make it difficult for new employees who cannot produce a product equal to the wages stipulated in a collective agreement, to find jobs.

Third, another problem with organized labour is that the bargaining power between

A TWO-PERSON bargaining situation involves two individuals who have the opportunity to collaborate for mutual benefit in more than one way. In the simpler case, which is the one considered in this paper, no action taken by one of the individuals without the consent of the other can affect the well-being of the other one. The economic situations of monopoly versus monopsony, of state trading between two nations, and of negotiation between employer and labor union may be regarded as bargaining problems.

Nash, Jr., *supra* note 148, at 155.

179. Grossman even claimed:

It is widely believed that the seniority system, in conjunction with the collective bargaining process, contributes significantly to the determination of the unemployment level in unionized sectors. Causal empiricism suggests that real wage demands often remain buoyant in these sectors in the face of seemingly high rates of unemployment among union members. James Medoff convincingly documents the evidence that "adjustment through layoffs is substantially greater in unionized firms than in comparable non-unionized firms" (1979, p. 380). The usual but somewhat informal explanation is that the outcome of union voting is greatly influenced by senior workers who are fairly certain that they will not be laid off when normal shifts in the industry's demand for labor occur. These inframarginal workers are believed to vote for higher wage settlements than they would if their own jobs were not so secure.

Gene M. Grossman, *Union Wages, Temporary Layoffs, and Seniority*, 73 AM. ECON. REV. 41, 41 (1983); James L. Medoff, *Layoffs and Alternatives Under Trade Unions in U.S. Manufacturing*, 69 AM. ECON. REV. 380, 380 (1979).

180. "It is now well known (see McDonald and Solow, 1981) that actual inefficient unemployment of union members depends upon the inability of the union to bargain over employment as well as wages." Jeff Frank, *Trade Union Efficiency and Overemployment with Seniority Wage Scales*, 95 ECON. J. 1021, 1021 (1985).

the employer and the labour organization is not symmetrical. I refer to Smith's remarks on this in *The Wealth of Nations*:

In all such disputes the masters can hold out much longer. A landlord, a farmer, a master manufacturer, or merchant, though they did not employ a single workman, could generally live a year or two upon the stocks which they have already acquired. Many workmen could not subsist a week, few could subsist a month, and scarce any a year without employment. In the long-run the workman may be as necessary to his master as his master is to him; but the necessity is not so immediate.¹⁸¹

Bargaining power is, for example, a function of the degree of harm that an employee's strike causes to the employer, if it is to such an extent that the employer does not have the capacity to absorb it.¹⁸² Therefore, social workers will be rewarded far less than cleaning workers or electric company employees, who, during a short strike, make a significant impact. This has two negative consequences. One, it will cause distributive injustice, and trade unions without the power to cause their employer immediate loss as a result of their strike will not be able to protect workers, and those trade unions will have to settle for low wages.¹⁸³ It will create gaps between workers in workplaces where trade unions are strong and those in workplaces where trade unions are weak.¹⁸⁴ Second, it will encourage people to choose to work, or train themselves to work, in places that have strong trade unions, rather than in jobs or areas that have trade unions. While the price mechanism encourages job seekers to choose to work where their marginal contribution is highest, organized labour encourages them to choose to work where there is a strong labour organization. As a result, there may be distortions in the allocative efficiency of workers.

The results of the power disparities between trade unions naturally raise the question—how to correct the distortion caused by these power disparities? The socialist

181. SMITH, *supra* note 3, at 59.

182. See generally AVINASH K. DIXIT & BARRY J. NALEBUFF, THINKING STRATEGICALLY: THE COMPETITIVE EDGE IN BUSINESS, POLITICS AND EVERYDAY LIFE (1991). They claimed: "One important element that determines how the pie will be split is each side's cost of waiting. Although both sides may lose an equal amount of profits, one party may have other alternatives that help partially recapture this loss. Suppose that the members of the union can earn \$300 a day in outside activities while negotiations with the hotel management go on. Now each time the management's turn comes, it must offer the union not only what the union could get a day later, but also at least \$300 for the current day. The entries in our table change in the union's favor. . . . The general idea is that the better a party can do by itself in the absence of an agreement, the higher will be its share of the pie that is the subject of the bargaining." *Id.* at 289–90.

183. "A union's bargaining power at any point of time is, for example, management's willingness to agree to the union's terms. Management's willingness, in turn, depends upon the costs of disagreeing with the union terms relative to the costs of agreeing to them." NEIL W. CHAMBERLAIN & JAMES W. KUHN, COLLECTIVE BARGAINING 176 (3rd edition, 1986).

184. Nordhaus and Samuelson claimed:

Taking into account worker differences, economists have concluded that union workers receive on average a 10 to 15 percent wage differential over nonunion workers. The differential ranges from a negligible amount for hotel workers and barbers to 25 to 30 percent higher earnings for skilled construction workers or coal miners. The pattern of results suggests that where unions can effectively monopolize labor supply and control entry, they will be most effective in raising wages. There is some evidence that the impact of unions on wages has declined in recent years.

SAMUELSON & NORDHAUS, *supra* note 172, at 321.

vision is that strong trade unions will protect weak trade unions; the strong trade unions must be ready to take strikes to protect the weak trade unions.¹⁸⁵ If the state bans solidarity strikes (second-order strikes), it will prevent large trade unions from protecting small ones. As a result, wage gaps between port workers and social workers, for example, will increase. We argue that the right to second-order strikes not only promotes distributive justice but also allocative efficiency, as it reduces the economic distortion in the choice of profession, which is created by the different bargaining power of various trade unions. Therefore, I suggest recognizing a strong right to conduct a solidarity strike.

Even if someone believes that it is best to have no organized work, and perhaps not even the right to organize or to strike, the second best, from their point of view, should not be to limit the right to strike as much as possible. This is especially true about the right to exercise solidarity strikes. In a system that has the right to strike but not the right to solidarity strike, there would be greater distortions.

For the legal recommendation to establish a strong right to solidarity strikes I add a political recommendation: I recommend that the strong trade unions must be ready to threaten solidarity strikes, both to protect the weak and to maintain the legitimacy of the organized labour mechanism.

Along with the above, I support a restriction on physicians' right to strike. I explain my approach: I am a heretic in the common belief that a doctor has an exemption from the good Samaritan law when the patient does not pay them enough or has no money. Indeed, imposing a legal duty of "neither shalt thou stand against the blood of thy neighbor" on doctors makes more sense, since the physician by receiving their license accepts special obligations. In addition, the doctor has usually gained public resources during their studies and internship. In my opinion, just as the absence of public health insurance is a violation of the rule "neither shalt thou stand against the blood of thy neighbor,"¹⁸⁶ so also it is appropriate to regard a doctors' strike or their collective resignation as a violation of this rule. However, since I support the right to strike, I believe that the doctors should be compensated by society for limiting their right to strike. For example, recognizing the right of doctors to block an intersection in the event of a work conflict, with a commitment not to strike, can improve everyone's condition. It will give doctors a bargaining chip that hurts society less and creates pressure and transfers the burden of the strike from the patients to the general public. Of course, one can think of other compensation mechanisms and other pressure levers that doctors will receive. However, since this is a matter of human life, an alternative "sting" should be found to equip doctors in negotiations. The logic of economic theory and game theory can teach us that the game of a labour negotiation in the shadow of a doctors' strike can be substituted for another game, a replacement that will be good for all parties, and if the game of a "roadblock" is not so, one should look for a game that is good for all parties.

The above analysis of the relationship between the trade union and the firm may be criticized by arguing that the model is not applicable for economic sectors, in which the firms have a third option—for example, to relocate the factory to China. In this case, the

185. Those are the last words of the Communist Manifesto: "Working Men of All Countries, Unite!" Karl Marx & Friedrich Engels, *Manifesto of the Communist Party: Chapter IV. Position of the Communists in Relation to the Various Existing Opposition Parties*, MARXIST INTERNET ARCHIVES (1848), <https://www.marxists.org/archive/marx/works/1848/communist-manifesto/ch04.htm>.

186. *Leviticus* 19:16.

disagreement payoff of the firm will be to pay a much lower wage. If, for example, a firm can relocate the factory to China, and has to pay only \$130 and the relocation cost is equivalent to paying ten to each worker, the bargaining range will be between \$100 and \$140. If the two sides have equal bargaining power, then the wage would only be \$120. This is why in the current globalization period trade unions may lose their effectiveness in sectors wherein the firms have the option of relocation. Thus, in the current period, work regulation and wealth transitions via tax laws have become much more important.

C. Wealth Transfers Through Tax Laws

Another way to deal with the distributive results of the free market is to transfer wealth from rich to poor through tax laws. In the previous Part, unemployment benefits were mentioned as a way to protect employees. Another way to protect employees could be through negative income tax. Another way is to grant welfare allowances that compensate for low wages. This, of course, begs the question: To what extent should the state transfer wealth from the rich to the poor through tax laws? I present a vigorous introduction to this issue, and then discuss the question: When is it better to protect the weak through tax laws and when should they be protected through labour or organized labour?

1. A Vigorous Literature Review of the Question: To What Extent Should Wealth Be Redistributed Through Tax Laws?

The libertarian approach negates progressive wealth transfers through tax laws on the grounds of lack of legitimacy. (Robert Nozick may be considered to be the most important prophet of this intellectual and political stream).¹⁸⁷ From the libertarian point of view, imposing such a tax on the individual infringes on the right of property, and the imposition of the tax is akin to theft by the state. While everyone benefits from delivering a public good, the justification for taxes is that every taxpayer enjoys the public good; this justification is not valid in the case of transferring wealth from the rich to the poor.

The libertarian approach has several limitations. First, it assumes that the proprietary order is created in a way that is legitimate enough to justify its constitutional sanctification. It is known that the proprietary order is validated by legal institutions, such as “market overt” and “the statute of limitation,” and that in almost all human societies the proprietary order is also a result of past wrongs, and that the establishment of the state framework actually “*changes usurpation into a true right and enjoyment into proprietorship*,” as pointed out by Jean-Jacques Rousseau.¹⁸⁸ There are good practical reasons to recognize the proprietary order and not reset it and start distributing wealth from the beginning (such as maintaining the incentive for production or the fear that it might result in totalitarianism),¹⁸⁹ and surely it is impossible for anyone to receive what they deserve, as we have no information on how to effectuate a just distribution, one that will fix all the

187. See generally Robert Nozick, *Distributive Justice*, 3 PHIL. & PUB. AFFAIRS 45 (1973).

188. JEAN-JACQUES ROSSEAU, *THE SOCIAL CONTRACT* 30 (G.D.H. Cole trans., Cosimo Classics 2008) (1762).

189. Regarding fear that it might result in totalitarianism, see DAVID CIEPLEY, *LIBERALISM IN THE SHADOW OF TOTALITARIANISM*, 315 (2006). See also generally HANNAH ARENDT, *THE ORIGINS OF TOTALITARIANISM* (2017); FRIEDRICH AUGUST HAYEK, *THE ROAD TO SERFDOM: TEXT AND DOCUMENTS: THE DEFINITIVE EDITION* (Bruce Caldwell ed., 2007).

wrongs of the past. However, if we accept that the proprietary order is legitimized by legal institutions, such as the statute of limitation, the sanctity that libertarians attribute to it dissipates. If the proprietary order rests on practical considerations, then there may also be countervailing practical considerations. If one accepts that the proprietary order is based on past wrongs, it is precisely the gradual redistribution of wealth that will bring us closer to what everyone deserves, rather than a full acceptance of the proprietary status quo. The fundamental dispute between libertarian anarchism and socialist anarchism is the question of how property should be treated.¹⁹⁰ Libertarian anarchism views property as sacred, or a natural legal right and therefore the state must not take it; in contrast, socialist anarchism sees the state and violence of the state as that which forms the proprietary order.¹⁹¹ Therefore, Proudhon declared: “Property is theft,”¹⁹² and therefore, socialist anarchism does not recognize the proprietary order. If socialist anarchism is right, a gradual transfer of wealth from the rich to the poor will reduce injustice.¹⁹³ Institutions such as the statute of limitations and the market overt—institutions that the proprietary order is based on—violate the constitutional right to property. This violation is for good public purposes. However, in order for the violation to be proportionate, a gradual progressive transfer of wealth through tax laws is required.

Another possible, liberal, way to cope with the libertarian claim is that the social contract, the same hypothetical agreement, authorizes the state to tax, and thus the hypothetical consent of citizens differentiates between the tax official and the robber, and the same agreement can also impose taxation restrictions.¹⁹⁴ This begs the question, to what extent do each of the various social convention narratives allow the transfer of wealth from the rich to the poor?

Another idea with the libertarian argument offered in literature is the joint project theory: The product that a man produces in a wealthy state market would be worth far less than in a poor country, and therefore all citizens of the country are actually their partners.¹⁹⁵

190. For an anarcho-capitalism approach, see generally David D. Friedman, *Law as a Private Good: A Response to Tyler Cowen on the Economics of Anarchy*, 10 *ECON. & PHIL.* 319 (1994); DAVID D. FRIEDMAN, *THE MACHINERY OF FREEDOM: GUIDE TO A RADICAL CAPITALISM* (1989). For a socialist-anarchist approach, see generally, MIKHAIL ALEKSANDROVICH BAKUNIN ET AL., *BAKUNIN: STATISM AND ANARCHY* (1990), and PIERRE-JOSEPH PROUDHON, *1 WHAT IS PROPERTY? AN INQUIRY INTO THE PRINCIPLE OF RIGHT AND OF GOVERNMENT* 12 (Benjamin R. Tucker trans., Princeton, MA, Benjamin R. Tucker 1876).

191. For an anarcho-capitalism approach, see Friedman, *Law, supra* note 190; FRIEDMAN, *MACHINERY supra* note 190. For a socialist-anarchist approach, see BAKUNIN, *supra* note 190; PROUDHON, *supra* note 190.

192. PROUDHON, *supra* note 190, at 12.

193. “Our practical activity may be a gradual approximation towards the ideal, or it may be a sudden revolutionary realization of that ideal, but it must never be a compromise.” HERBERT READ, *A COAT OF MANY COLOURS: OCCASIONAL ESSAYS* 59 (2015).

194. Locke claimed:

It is true, governments cannot be supported without great charge, and it is fit every one who enjoys his share of the protection, should pay out of his estate his proportion for the maintenance of it. But still it must be with his own consent, i.e. the consent of the majority, giving it either by themselves, or their representatives chosen by them: for if any one shall claim a power to lay and levy taxes on the people, by his own authority, and without such consent of the people, he thereby invades the fundamental law of property, and subverts the end of government: for what property have I in that, which another may by right take, when he pleases, to himself?

JOHN LOCKE, *THE SECOND TREATISE OF CIVIL GOVERNMENT* 266 (George Routledge & Sons ed., 1884).

195. Yoseph Edrey, *Constitutional Review and Tax Law: An Analytical Framework*, 56 *AM. U. L.*

The weakness in the joint project theory is that the theory attempts to handle a challenge from the individualistic perspective through a reply from the collectivist perspective.

Moreover, from the above discussion of the problem of the distribution of wages in the labour market, one can learn another justification for progressively transferring wealth through tax laws. If one accepts that the labour market leads to an unfair wage distribution, it may be fair to correct it through tax laws, or at least, it is not unfair to transfer wealth from the rich to the poor. In addition, accepting the ban on transferring wealth from the rich to the poor means that there will be distressed people who will starve. In the Jewish tradition, theft is not included in the only three commandments for which one must be prepared to die rather than violate it.¹⁹⁶ If there is no wealth transfer to people who would starve without it, I wonder how society can demand them not to steal. Berthold Brecht wrote about it as follows:

The man who defends himself when hands are at his throat
 And stopping his breath, there's a law that intercedes
 And cries: He acted in self-defense. But
 That same law looks away and steps aside
 When they stop your bread and you defend yourselves.
 But you die if you don't eat and if you don't eat enough you die
 Only more slowly. All the years dying
 You are not permitted to defend yourselves.¹⁹⁷

Nevertheless, it should be noted that even if one accepts the fact that wealth is not intentionally transferred through tax laws, that does not mean that the tax burden should be divided so that the poor and the rich pay the same tax. Smith claimed:

The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state. The expense of government to the individuals of a great nation is like the expense of management to the joint tenants of a great estate, who are all obliged to contribute in proportion to their respective interests in the estate. In the observation or neglect of this maxim consists what is called the

REV. 1187, 1214–18 (2007).

196. I have stated:

Exegetes of the Talmud argued over how to interpret the discussion about whether one is permitted to save oneself by using another person's money. The Tosafists – 12nd century C.E. commentators on the Talmud – note that it's clear that a person is permitted to save his life with another's money, as theft is not one of the three violations of religious law in which a Jew must give his own life rather than commit the violation (yehareg ve'al ya'avur). The question is only whether he is required to compensate the other.

Uri Weiss, *Talmud's Solution to the Coronavirus Dilemma: Save Lives, or the Economy?*, HAARETZ (Jul. 23, 2020), <https://www.haaretz.com/israel-news/premium-talmud-s-solution-to-the-coronavirus-dilemma-save-lives-or-the-economy-1.9016090>.

197. BERTOLT BRECHT, *THE COLLECTED POEMS OF BERTOLT BRECHT* (Tom Kuhn & David Constantine, trans. and eds., 2018).

equality or inequality of taxation.¹⁹⁸

Moreover, from a utilitarian perspective, aggregate happiness should be maximized.¹⁹⁹ Therefore, utilitarianism can teach us a strong reason for redistributing wealth through tax laws: The poor will enjoy the money that is transferred to them more than the rich will lose pleasure from the money, as the poor would acquire much needed resources and the rich would have to give up luxury. People benefit more from their first dollar than from their last; with their first, they fulfil their most basic needs, and with their last, they acquire luxuries. If they do not know whether they will be rich or poor but they have a 50% probability of being rich and the same probability of being poor, then, if asked who they would prefer to receive \$1,000, the rich or the poor, they would choose the poor.²⁰⁰

The above utilitarian justification can be criticized by three arguments. First, the mere imposition of tax in order to redistribute wealth is a kind of theft as previously discussed. Second, it is impossible to compare the benefits of different people, and therefore the utilitarian principle is not easily applicable and is incomprehensible. To this, Amartya Sen replies that even if the benefits of different people cannot be compared, it is clear that the benefit to Nero Caesar from the incineration of Rome will be less than the benefit to the residents that he will not burn Rome.²⁰¹ Third, taxation also has disadvantages, such as reducing the incentive to work, even when it is efficient for the person to work. If, for example, a person can earn \$100 in the next hour, and their alternative to work is walking to the sea, which is worth \$90, then the person will choose to work in the next hour; However, if a tax of more than 10% is levied, they will choose not to work in this job but to go to sea. The tax causes them to externalize their share of work which will go to another benefit—the state. Arthur Laffer pointed out that maximum tax does not lead to maximum tax rewards, as 100% tax will neutralize the financial incentive to work.²⁰² Peter Diamond and Emmanuel Saez therefore ask: What is the optimal income tax rate that should be imposed on top millionaires?²⁰³ They answer that top end of the millionaires' marginal benefit derived from money is negligible, and so the question is: What is the tax rate that will result in the highest tax receipts (i.e. they suggest not to even consider the loss of the pleasure of those millionaires, as they will lose no real pleasure in having the state take

198. SMITH, *supra* note 3, at 1103–04.

199. Mill claimed:

The creed which accepts as the foundation of morals, Utility, or the Greatest Happiness Principle, holds that actions are right in proportion as they tend to promote happiness, wrong as they tend to produce the reverse of happiness. By happiness is intended pleasure, and the absence of pain; by unhappiness, pain, and the privation of pleasure.

JOHN STUART MILL, *UTILITARIANISM* 13 (1895).

200. Weiss, *The Regressive Effect of Legal Uncertainty*, *supra* note 112.

201. See generally Amartya Sen, *The Possibility of Social Choice*, 89 *AM. ECON. REV.* 349 (1999) (discussing the issue central to social choice theory: Is it possible to make judgments that impact society when there is great diversity in the views of individual members of society).

202. Arthur Laffer, *The Laffer Curve: Past, Present, and Future*, HERITAGE FOUND. (June 1, 2004), <https://www.heritage.org/taxes/report/the-laffer-curve-past-present-and-future>.

203. Peter Diamond & Emmanuel Saez, *The Case for a Progressive Tax: From Basic Research to Policy Recommendations*, 25 *J. ECON. PERSPS.* 165, 165 (2011).

money from them)?²⁰⁴ They also offer an empirical answer of about 70% based on an econometric examination, but I am more interested in the criterion they offer, since the answer varies from state to state.²⁰⁵

Keynes, in the last chapter of *The General Theory of Employment, Interest, and Money*, argued that his theory could reduce the resistance to the redistribution of wealth.²⁰⁶ Transferring wealth from the rich to the poor means transferring wealth from people whose marginal tendency to consume is low to people whose marginal tendency to consume is high. In other words, the rate at which the rich consume their income is smaller than that of the poor. Consequently, transferring wealth from the rich to the poor encourages consumption. Increasing consumption creates a cycle; it causes people that consumers buy from to have more money, and therefore they themselves shall consume more, and therefore, the people they consume from shall consume more in return. Keynes particularly pointed out that economic crises are sometimes caused by low consumption, which is why he suggested that during times of crisis, the state should increase government spending, which could lead to a rollback as recalled.²⁰⁷ Keynes also noted that inheritance tax encourages consumption.²⁰⁸ Stiglitz echoes Keynes, claiming that inequality drives down demand, leading to solutions like lowering interest rates, which could cause bubbles.

Moreover, Stiglitz raised the question: What is the price of inequality?²⁰⁹ He replied that extreme income inequality today could hurt both democracy and the economy.²¹⁰ Therefore, he argues that the price of social inequality is not only moral but also economical, and therefore refutes economic justifications for inequality.²¹¹ This is because the market does not exist in a vacuum, but in a certain political reality. Extreme inequality distorts democracy, such that the ‘one person one vote’ method is replaced by ‘one vote for one dollar.’ Politicians and regulators influence the market, and equity holders can cause rules of the game that hurt the economy. In the realm of extreme inequality, the danger that a top percentage would invest in lobbying lurks, which in turn shall lead to deregulation leading to monopolies; deregulation will cause banks to expose themselves to excessive risks, and firms will receive subsidies as they received during the 2008 economic

204. *Id.* at 173.

205. *Id.* at 167.

206. JOHN MAYNARD KEYNES, *THE GENERAL THEORY OF EMPLOYMENT, INTEREST, AND MONEY* 332–72 (2018).

207. *Id.* at 280.

208. *Id.* at 332.

209. *See generally* JOSEPH E. STIGLITZ, *THE PRICE OF INEQUALITY: HOW TODAY’S DIVIDED SOCIETY ENDANGERS OUR FUTURE* (2012); Joseph E. Stiglitz, *How Today’s Divided Society Endangers Our Future*, THE PONTIFICAL ACAD. OF SCIS. (2014), <http://www.pas.va/content/dam/accademia/pdf/es41/es41-stiglitz.pdf>.

210. Stiglitz said:

Growing inequality within most countries around the world is one of the critical issues facing the world today. People everywhere sense that it is morally wrong. We sense that it cannot be justified. We sense that it is dividing our societies and undermining our democracies. And we are right in sensing this harm. These effects of inequality should be more than enough to steel the resolve to do something to reduce growing inequality. But even if one didn’t care about these effects, there are further reasons to fight inequality. It is self-defeating: it undermines our economies.

Stiglitz, *How Today’s Divided Society Endangers Our Future*, *supra* note 209, at 1.

211. *Id.*

crisis.²¹² For the rich pay tax rates that are clearly unfair, and also to curb legislation needed to deal with climate problems. Moreover, because of differences in the reality of inequality, the society shall find it difficult to agree on the supply of required public goods, such as public transport. The inequality that polarizes society leads to a decline in trust in the society and impairs the ability of its members to have common goals. Furthermore, inequality in the United States is turning the American dream into a myth. It deprives people of opportunities to acquire education and skills and, in the long run, also harms the GDP.²¹³ Poor nutrition also causes long-term social damage.²¹⁴ Therefore, inequality is likely to hurt not only the democracy, but also the economy. Stiglitz has a theory, but not just a theory. He points out (based on a study by the World Monetary Fund)²¹⁵ that in companies with greater inequality there is actually less growth and more instability.²¹⁶

Another answer I discuss is that of Rawls.²¹⁷ Rawls argues that the fair rules of the game are those that the citizens would agree on under a veil of ignorance, such that no one knows if they are rich or poor.²¹⁸ The first rule they would agree on is that every person should have an adequate scheme of equal fundamental liberty, and the second rule (the first to enjoy superiority) is that social gaps must meet the conditions of equal opportunity and must bring maximum welfare among the most disadvantaged members of society.²¹⁹ If one accepts Rawls' idea and does not accept the view that equal liberty precludes wealth

212. *Id.*

213. *Id.*

214. "With nearly one in four American children growing up in poverty, many of whom face a lack of access to adequate nutrition and education, the country's long-term prospects are being put into jeopardy." *Id.* at 11.

215. ANDREW G. BERG & JONATHAN D. OSTRY, *INEQUALITY AND UNSUSTAINABLE GROWTH: TWO SIDES OF THE SAME COIN?* (2011), <https://www.imf.org/external/pubs/ft/sdn/2011/sdn1108.pdf>; INT. MONETARY FUND, *FISCAL POLICY AND INCOME INEQUALITY* (2014), <https://www.imf.org/external/np/pp/eng/2014/012314.pdf>.

216. *See generally* STIGLITZ, *supra* note 209.

217. *See generally* John Rawls, *Justice as Fairness*, 67 *PHIL. REV.* 164 (1958) (arguing that fairness is fundamental to the concept of justice).

218. Rawls said:

This original position . . . is understood as a purely hypothetical situation characterized so as to lead to a certain conception of justice. Among the essential features of this situation is that no one knows his place in society, his class position or social status, nor does any one know his fortune in the distribution of natural assets and abilities, his intelligence, strength, and the like. I shall even assume that the parties do not know their conceptions of the good or their special psychological propensities. The principles of justice are chosen behind a veil of ignorance.

JOHN RAWLS, *A THEORY OF JUSTICE* 11 (1999) (footnote omitted).

219. More precisely:

First Principle: Each person has the same infeasible claim to a fully adequate scheme of equal basic liberties, which scheme is compatible with the same scheme of liberties for all;

Second Principle: Social and economic inequalities are to satisfy two conditions:

They are to be attached to offices and positions open to all under conditions of *fair equality of opportunity*;

They are to be to the greatest benefit of the least-advantaged members of society (the *difference principle*).

JOHN RAWLS, *JUSTICE AS FAIRNESS: A RESTATEMENT* 42–43 (Erin Kelly ed., 2001); *see also* Leif Wenar, *John Rawls*, *STAN. ENCYCLOPEDIA PHIL.* (Jan. 9, 2017), <https://plato.stanford.edu/entries/rawls/>.

transfers, then wealth transfer should be at the level that maximizes the welfare of the weak, as opposed to the utilitarian approach of general maximization (if we adhered to utilitarian philosophy, then maximization should have been universal, and not only in the given society).

Another answer is the Marxist one. Marx saw communism as the abolition of private property,²²⁰ and the Marxist vision is, “From each according to his ability, to each according to his needs.”²²¹ The Communist Revolution will inevitably happen, but it can and must be expedited. Marx did not elaborate on what the communist utopia would look like, but he did elaborate in the communist manifesto what would be in the interim phase of dictatorship of the proletariat. Let us quote:

1. Abolition of property in land and application of all rents of land to public purposes.
2. A heavy progressive or graduated income tax.
3. Abolition of all rights of inheritance.
4. Confiscation of the property of all emigrants and rebels.
5. Centralisation of credit in the hands of the state, by means of a national bank with State capital and an exclusive monopoly.
6. Centralisation of the means of communication and transport in the hands of the State.
7. Extension of factories and instruments of production owned by the State; the bringing into cultivation of waste-lands, and the improvement of the soil generally in accordance with a common plan.
-
9. Combination of agriculture with manufacturing industries; gradual abolition of all the distinction between town and country by a more equable distribution of the populace over the country.
10. Free education for all children in public schools. Abolition of children’s factory labour in its present form. Combination of education with industrial production.²²²

However, what would be the incentive to work? Did Marx ignore it? Let us refer to Marx’s answer: “8. Equal liability of all to work. Establishment of industrial armies, especially for agriculture,”²²³ and so Marx falls into a tyranny. Roger Myerson also argues that in cases where there is no property right and state coercion to work, sometimes, employees who did not “deserve” to be punished would also be punished, even though they really and truly worked hard. (Myerson applied institutional theory to markets’ investigation)²²⁴ This is because there is a moral hazard problem; the manager sometimes cannot know if the project failed because the worker did not make an effort or due to external circumstances (for example, in the case of a project where effort will lead to 50%

220. MARX & ENGELS, *supra* note 91.

221. KARL MARX, CRITIQUE OF THE GOTHA PROGRAM 10 (C.P. Dutt ed., 1966) (1891).

222. MARX & ENGELS, *supra* note 91.

223. *Id.* at 92.

224. See generally Roger B. Myerson, *Fundamental Theory of Institutions: A Lecture in Honor of Leo Hurwicz*, 13 REV. OF ECON. DESIGN 59 (2009).

chance of success and a lack of effort will lead to 0% chance of success). In a market economy, this is solved by a bonus that encourages the employee to make an effort, that is, if they invest effort they will have a chance of receiving the bonus, and if they do not make an effort they will not stand the chance. In contrast, in an economy that does not have property rights but has forced labour—to maintain the employees' incentive to make an effort, the employer should punish them in case of failure, so that even if they struggle, they will be somehow penalized for failing. One of the important things that social democrats can learn from Marx's tyrannical elements is that it is wrong to try to establish a social democracy that will partially fulfil the Marxist ideal. The subset of social democracy, that will be the partial fulfilment of the utopia of socialist anarchism, is preferable to the subset of social democracy, which will be the partial fulfilment of Marxist utopia.

To summarize the section: An important solution to the distorted wealth distribution in the labour market could be the transfer of wealth through tax laws. One important question that arises is: To what extent should wealth be transferred from the rich to the poor through tax laws? One libertarian answer is that it is not at all legitimate to transfer wealth through tax laws from the rich to the poor, as this transfer is akin to theft. However, this answer ignores the fact that the proprietary status quo is not created by legitimate wealth transfers, but sometimes, while at least one link in the chain of wealth transfers has been created by robbery and plunder, by acts bleached through institutions such as obsolescence and market overt. This economic status quo rests on strong practical considerations, but the reliance on practical considerations takes away its constitutional sanctity. Moreover, social contract theory can offer justifications for wealth transfers through the tax laws consent of the governed. There are also wealth transfers that are desirable for the entire society, such as those necessary to prevent crime or to allow a democratic regime. Another justification is the joint project theory. Another utilitarian answer is that wealth must be transferred in a way that maximizes happiness. Since the poor enjoy the last few dollars more than the rich enjoy them, the tax laws should transfer wealth progressively. Diamond and Saez offer a formula, such that the tax imposed on the top millionaires will be that which maximizes the revenue of the state; the reason is that the millionaires will not lose any significant benefit from parting with this money.²²⁵ An answer by Rawls is that wealth must be transferred in a way that maximizes the welfare of the disadvantaged group.²²⁶ A Marxist answer is that everyone will receive as they need and give as they can, but the problem is that neutralizing the incentive to work can lead to forced labour.²²⁷ Therefore, it is probably better for social democracy to be a partial realization of the anarcho-utopian utopia rather than a partial realization of the Marxist utopia.

225. See generally Peter Diamond & Emmanuel Saez, *The Case for a Progressive Tax: From Basic Research to Policy Recommendations*, 25 J. ECON. PERSP. 165 (2011) (describing this formula).

226. See generally RAWLS, *supra* note 218 (proposing his response).

227. In his words: "From each according to his ability, to each according to his needs." MARX, *supra* note 221, at 10.

2. *The Mechanism of Transfers Through the Tax Laws Versus the Minimum Wage Law and Organized Labour*

I mentioned solutions of labour legislation and organized labour versus the solution of wealth transfers through tax laws.²²⁸ According to Kaplow-Shavell's theory, wealth transfers should be preferred to occur through tax laws than through other legislative instruments.²²⁹ Their reasoning is as follows: Wealth transfers cause distortions in incentives.²³⁰ For example, they distort the incentive to work and thus block efficient transactions.²³¹ Just as income tax distorts a person's incentive to work, so does any other law that transfers wealth from the rich to the poor (e.g. tort law that transfers wealth from the rich to the poor). However, while in the case of taxation, only the incentive to work is distorted; when the law is inefficient, another distortion is created (e.g. an over-deterrent to harm the poor or the poor's reluctance to harm the rich), and therefore, according to their theory, we should prefer achieving distributive justice through tax laws.²³² Thus, according to this theory, it is preferable to transfer wealth through tax laws than to establish a minimum wage law.²³³

In this subsection, I examine the correction of the distributional distortions in the labour market by means of the Minimum Wage Law versus the negative income tax mechanism. The negative income tax solution was proposed by Milton Friedman to replace the existing welfare programs.²³⁴ To Friedman's dismay, he won the enthusiasm of economic leftists and opposition from the right-wing.²³⁵

I examine what happens in the main example of this article, if it changes such that there is now a negative income tax which raises the worker's wage from \$100 to \$300, while the state imposes the most effective tax on the employer in order to cover the cost of the negative income tax, and the minimum wage is \$100 (as the marginal benefit from the last employee). If the state determines a negative income tax without setting a minimum wage, it will lower the market wage of unskilled workers, since they know that they will be compensated by the state.²³⁶ What will the consequences be if the state imposes, for example, on the employer an income tax (or corporate tax) at a rate of 200/550 of its

228. Sections IV.A, IV.B., IV.C.

229. See generally Louis Kaplow & Steven Shavell, *Why the Legal System Is Less Efficient than the Income Tax in Redistributing Income*, 23 J. LEGAL STUD. 667 (1994) [hereinafter *Legal System*] (arguing the income tax system is a more efficient means of income redistribution than legal rules); see generally Louis Kaplow & Steven Shavell, *Should Legal Rules Favor the Poor? Clarifying the Role of Legal Rules and the Income Tax in Redistributing Income*, 29 J. LEGAL STUD. 821, (2000) [hereinafter *Legal Rules*] (revisiting their earlier 1994 article and addressing argument qualifications, including the question of whether legal rules should favor the poor—a question of doubtful practical importance).

230. *Legal System*, supra note 229; *Legal Rules*, supra note 229.

231. *Legal System*, supra note 229; *Legal Rules*, supra note 229.

232. *Legal System*, supra note 229; *Legal Rules*, supra note 229.

233. *Legal System*, supra note 229; *Legal Rules*, supra note 229.

234. See generally Milton Friedman, *The Case for a Negative Income Tax: A View from the Right*, in BASIC INCOME: AN ANTHOLOGY OF CONTEMPORARY RESEARCH (Karl Widerquist et al. eds., 2013) (describing Friedman's solution).

235. *Id.*

236. See generally Jerry A. Hausman & David A. Wise, *The Evaluation of Results from Truncated Samples: The New Jersey Income Maintenance Experiment*, 5 ANNALS OF ECON. AND SOC. MEASUREMENT 421 (1976) (demonstrating this result in New Jersey).

profits?²³⁷ In this case, it would be profitable for the employer to hire the first employee for \$100; of course, it would also be profitable to hire the ninth employee, and they will also hire the last employee. One can see that there is a mechanism that will lead each employee to earn \$300, but this time none will be fired. Thus, in the case of minimum wages, the employer is obliged to pay a minimum wage directly to any employee who is employed, and thus the employer has the option of dismissing all the employees who earn the minimum wage. After all, in the “minimum and negative tax” mechanism, every worker who works will receive a high minimum wage, but the employer will have to pay directly for each worker only a low minimum wage, while the difference to the worker will be paid by the taxpayers, including the employer. Therefore, this time the employer has no option of getting rid of minimum wage funding through layoffs. If employees are fired, they would still have to fund the minimum wage of employees they did not employ.

I propose a generalization of the same mechanism. I would call it a “minimum and tax mechanism.” If the market wage in perfect competition of the unskilled laborers is w , then a minimum wage of w is set. Alongside this, there will be a negative income tax, which will increase the wages of anyone earning w to W . Suppose the number of workers in the market who are not employed by firms is negligible. The state will raise the corporate tax rate to cover the same difference. If a minimum wage W mechanism was established, would more or fewer workers be laid off? The answer is that now the cost of hiring the unskilled workers is cheaper for the employer, and therefore the factory will fire fewer employees. However, in the proposed mechanism, the firm benefits less, and the employee group benefits more. Earlier, the firm was able to deal with ‘financing’ the minimum wage by laying off workers who were earning less than the minimum wage.²³⁸ In the current mechanism, the firm is forced to bear the minimum wage expenses.

While the mechanism of a high minimum wage law requires employers to choose whether or not to pay employees a minimum wage, the minimum-tax mechanism requires firms to choose between not operating in the market and paying taxes from which the weak will benefit. A high minimum wage renders the weak worker unattractive to the employer, while a negative income tax mechanism does not render the weak worker ineffective for the employer. The advantage of a minimum and tax mechanism is that even if the employer does not lower the unskilled workers’ wages due to the subsidy, the workers will also benefit as effectively as high minimum wages, and they will not be laid off. While minimum wages make the marginal cost of hiring an employee higher, the negative income tax mechanism does not significantly affect the cost of hiring.

The downside is that raising the tax can lead to the firm closing down or not setting up firms at all (if the initial expense is high and the entrepreneur takes into account the tax

237. Let us discuss the tax rate: the employer earns an average of \$550 from employing a worker, and \$200 is what is required to cover the negative income tax.

238. Neumark and Wascher claimed:

Using panel data on state minimum wage laws and economic conditions for the years 1973–89, the authors reevaluate existing evidence on the effects of a minimum wage on employment. Their estimates indicate that a 10% increase in the minimum wage causes a decline of 1–2% in employment among teenagers and a decline of 1.5–2% in employment for young adults, similar to the ranges suggested by earlier time-series studies.

David Neumark & William Wascher, *Employment Effects of Minimum and Subminimum Wages: Panel Data on State Minimum Wage Laws*, 46 *INDUST. LAB. RELATION REV.* 55, 55 (1992).

that they would have to pay on the profit). Moreover, unlike the case of trade unions, this time the firm will not be able to negotiate to prevent it from becoming unprofitable. However, a negative income tax can have the same effect as organized labour: raising wages without encouraging dismissal.²³⁹ Furthermore, unlike the organized labour mechanism, a negative income tax also does not weaken the incentive to hire more workers.

I propose a mechanism for discussion here as an application to Kaplow and Shavell's theory.²⁴⁰ The theory is not my favourite, as they do not distinguish between cases where compensation is possible and those where it is not possible. I acknowledge that the results surprised me and I should further consider the shortcomings of the mechanism and the information the social planner needs.

However, even if the attainment of minimum wage and organized labour can be achieved through the negative income tax mechanism, the absence of organized labour will be difficult to achieve politically. Organized work, for example, could require the government to raise wages by way of negative income tax. Furthermore, if we conclude that it is better to safeguard workers' rights through mechanisms such as negative income tax, the conclusion should also be to permit a strike that puts pressure on the government to change the negative income tax rates or to include welfare policy in the right to strike.

I summarize the subsection by stating that a low minimum wage and negative tax mechanism can sometimes lead to similar achievements to those of a high minimum wage law without causing workers to be dismissed.

V. SUMMARY

I recommend that questions of how to minimize harming the weak must be discussed in law and economics, and in political economy. I suggest discussing how to deal with the power gaps in the labour market. I have shown solutions of "non-intervention"²⁴¹ versus solutions through protective laws,²⁴² unemployment benefits,²⁴³ wealth transfers through tax laws,²⁴⁴ and the encouragement of organized labour.²⁴⁵ I review the main points of the concrete policy recommendations proposed in this article:

First, it is possible to learn from the literature that the justification for the minimum wage depends on the compensation of the unemployed through unemployment benefits

239. According to Bank of Israel, the first implementation of negative income tax in Israel resulted in: "2,300 families rising above the poverty line, and an increase of roughly 15,000 workers". ROBY NATHANSON ET AL., ISRAEL'S IMPLEMENTATION OF THE OECD RECOMMENDATIONS 17 (2011), <http://www.macro.org.il/images/upload/items/13967169044149.pdf>. Let me note that in Israel there is a combination of minimum wage and negative income tax. See *Negative Income Tax, Results from the First Year of Enactment*, BANK OF ISRAEL (June 2010), https://www.boi.org.il/he/Research/Pages/neumim_neum358h.aspx. See National Economic Council, *The Committee Examining Employment Policy, Final Report*, BANK OF ISRAEL (June 2011), <https://www.boi.org.il/deptdata/papers/paper19h.pdf>.

240. See generally Louis Kaplow & Steven M. Shavell, *Fairness Versus Welfare*, 114 HARV. L. REV. 961 (2001) (describing their theory); Louis Kaplow & Steven Shavell, *Why the Legal System Is Less Efficient than the Income Tax in Redistributing Income*, 23 J. LEGAL STUD. 667 (1994). I admit I do not like their theory but acknowledge that it is sometimes fruitful.

241. See *supra* Part II.

242. See *supra* Section IV.A.

243. See *supra* Section IV.A.

244. See *supra* Section IV.C.

245. See *supra* Section IV.B.

and guaranteed minimum income.²⁴⁶ This is because the minimum wage forces people who cannot produce enough to be unemployed, or at the least not legally employed. Therefore, workers affected by the minimum wage should be compensated in the form of unemployment benefits and income support. This article proposes that the freedom to contract and the right to work should entail a constitutional right to unemployment benefits in the event of a minimum wage. Furthermore, if bullying programs for the unemployed have succeeded in reducing unemployment in a place with a low minimum wage, it cannot be concluded that they would succeed in a place with a high minimum wage.²⁴⁷

Second, unemployment benefits may prevent employee abuse including sexual harassment and promote the rule of law. They give workers who are victims of abuse at work a practical possibility of leaving the workplace, which also gives them a credible threat to sue, and thus contributes to the rule of law in the workplace.

Thirdly, the rights granted in the labour law should be clear. The uncertainty in the labour law should be reduced. Legal uncertainty leads weak workers to settle for low amounts and sometimes even to avoid litigation.²⁴⁸

Fourth, the right to a solidarity strike must be substantially expanded. In a system that has organized labour, the right to a solidarity strike protects the trade unions that do not have pressure devices, thereby contributing to social justice. It also contributes to allocative efficiency, as it reduces the incentive for workers to work where they have pressure devices.

Fifth, organized labour has an advantage in that workers' organizations can simultaneously negotiate wage terms and can demand that employers not fire workers. Raising wages may result in employee layoffs and therefore there is an advantage to organized work over minimum wage regulation, in that it can simultaneously negotiate the issue of layoffs.

Sixth, in the case of physician strikes, the right to strike must be curtailed and at the same time compensated for, such as allowing doctors to block roads. We should design a game that is better for all sides than the game of negotiations in the shadow of the threat of a doctors' strike.

Seventh, sometimes a negative income tax can raise wages similarly to a minimum wage, but without causing workers to be dismissed.

246. *See supra* Section IV.A.

247. *See supra* Section IV.A.

248. *See supra* Part II; Weiss, *The Regressive Effect of Legal Uncertainty*, *supra* note 112, at 154–64.