By Invitation

Labor Law Reform in India: Insights from Tangled Legacy of Sidney & Beatrice Webb

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Sidney and Beatrice Webb, co-founders of the industrial relations field and early pioneers of Fabian Socialism significantly influenced Jawaharlal Nehru and India's post-Independence model of economic development. Part of this model was a protectionist regime of labor law which has now come under increasing criticism as a structural impediment to growth. This article reviews the ideas of the Webbs and uses them as a prism for evaluating the case for labor law reform and the direction it should take. The article advances a three-prong conclusion: the Webbs' program for labor market regulation remains sound in principle but the specifics in India need substantial adjustment; the most important way to generate higher employment growth is not from labor market deregulation but continued liberalization of product markets and encouragement of entrepreneurship; and the most critical pro-growth reform is more efficient and honest institutional-regulatory governance.

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Introduction

India posted an impressive growth record after economic liberalization in 1991. A slow-down during the world financial crisis of 2008-2010 was expected but so too was a rebound once the crisis passed. The crisis is now four years over but the growth recovery for India is disappointingly anemic. A number of analysts inside and outside the country conclude growth is obstructed by structural problems. Illustratively, IMF Report (2014:19) concludes, "There is consensus that structural reforms are going to be the lynchpin of an eventual rebound in growth". Five key areas of structural reform are listed: (1) power and natural resources, (2) agriculture, (3) health and education, (4) investment climate, and (5) labor regulation.

The IMF report is tactful and frames these structural problems, not as government failures of the past, but as agenda items for swift legislative action going forward.

Other analysts, however, are far more critical and say these problems have been allowed to fester and worsen because, rather than take liberalization the next step forward, Indian governments of the last decade have reverted to "the old recipe of social spending and industry mandates… and granting massive new entitlements" associated with "Nehru's turn to Fabian Socialism" in India's post-Independence era (Dalmia, 2014: 1-2). In a similar vein, the press in India is starting to wonder if the economic miracle is returning to the more anemic 'Hindu rate of growth' which Das (2006:2) explains, "had nothing to do with Hinduism and everything to do with the Fabian socialist policies of Prime Minister Jawaharlal Nehru". A well-known America labor law professor, having recently returned from a trip to India, also puts the finger of blame for India's growth problems on failure to jettison the "hopeless forms of Fabian Socialism that Jawaharlal Nehru, India's first prime minister, brought into public life between 1950 and 1990" (Epstein , 2014: 2).

The failed policies associated with Nehru and Fabian Socialism provide a natural segue into the implications for labor law reform of the seminal writings of Sidney and Beatrice Webb, two of the founders of not only Fabian Socialism but also the field of industrial relations (Cole,1943; Harrison, 2000; Kaufman, 2004).Many observers believe that Indian labor law is increasingly out of date, complex and burdensome and poses a structural impediment to sustained economic growth (VenkataRatnam, 2004; Hill, 2009; Saini, 2009; Krueger, 2013). But, as cited above, a number of analysts also believe that the policies and practices historically associated with the industrial relations field, particularly as it came from Britain and Fabian Socialist writers such as the Webbs, are part of the source of the labor regulation muddle.

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This article tries to sort through parts of the Webbs' writings with enduring value as guides for industrial relations and labor law reform and parts of which have been shown incorrect or harmful by historical experience. Analogous to the idea of Freeman &Medoff (1984) that trade unions have two faces — a positive voice face and a negative monopoly face, it is argued that the theory of the Webbs also has two faces, a positive industrial relations face and a negative Fabian Socialism face. The paper briefly identifies and delineates these two faces and then applies them to working-out useful principles for Indian labor law reform. Since much of the existing IR and labor law literature in India is descriptive and empirical, introducing a stronger conceptual element may be helpful for both the endeavors.

American & British Influences

Industrial relations started in the late 19th and early 20th centuries as an Anglo-American project among reform-minded academics broadly linked to a social-institutional approach to economics, albeit

with a clear link to Germany and that country's tradition of historical economics and active social policy (Kaufman, 2004). Industrial relations was a response to the growing labor problem and attendant class-conflict in late 19th century industrializing countries and was positioned as a middle-way solution between laissez-faire orthodox economics and revolutionary Marxist-radical economics. These Western ideas on a middle way solution to the labor problem became a uniquely Indian third-way approach when integrated with the Gandhian philosophy of industrial harmony and self-government (Bose, 1956).

The concept of industrial relations and its formalization as a field of teaching and research in universities appeared first in the United States in the late 1910s under the leadership of Richard Ely and John Commons, institutional economists at the University of Wisconsin. The industrial relations term in early American usage was a short-hand for 'relations between employers and employees in industry and, hence, at its beginning industrial relations was conceived broadly as the study of the employment relationship and the labor problems which grow out of it. Illustrative of this broad focus, IR textbooks often used 'labor problems' in the title (e.g., *Labor Problems in American Industry*, Daughtery, 1933) and featured chapters on personnel management, trade unions, labor law, social insurance, and national labor policy.

In Britain, Sidney and Beatrice Webb are widely regarded as IR founders (Hyman, 1989; Ackers & Wilkinson, 2003). They also founded the London School of Economics (LSE) in 1895. Their seminal contributions, however, were not to launch the IR field itself – labor studies was not part of the early LSE curriculum and IR as a constituted field of study did not emerge in Britain until the late 1940s – but to initiate the study of organized labor as a legitimate topic of scholarly inquiry in England. The Webbs' most famous books are *History of Trade Unionism* (1894) and *Industrial Democracy* (1897). They also wrote on other labor topics, such as the poor laws and labor conditions of women, but labor law and personnel management were peripheral to their research agenda and remained so in the British IR field until the 1980s.

The subject of industrial relations in Britain started out, therefore, more union-centric than in the USA and also substantially to the left in the political spectrum (Hyman, 1989; Ackers & Wilkinson, 2003; Kaufman, 2014). The Webbs, and their intellectual successor G.D.H. Cole, were proponents of democratic socialism and, from experiences such as World War I and the Great Depression, became increasingly outspoken critics of capitalism. The democratic socialist and leftist Labor Party leaning of British industrial relations continued after World War II, albeit moderated by the Cold War chill of anti-communism, and found expression in the Atlee government's Fabian-inspired program of nationalization of key industries, industrial democracy through widespread industry-level collective bargaining, steeply graduated income and estate taxes, and extensive welfare state social

programs (Hinton, 1983). This economic growth model, attractive in theory and appealing to anti-capitalist sentiments widespread at the time, proved debilitating in practice and by the 1970s Britain declined to the unenviable status of 'poor man of Europe.'

As an organized area of teaching and research, the early field of industrial relations in India has in some visible ways more affinity to the American model than the British. For example, the organizing concept of labor problems for the study of industrial relations was widespread in America but not Britain and in India the term found frequent use (e.g., Agarwala, 1947; Mehrotra, 1965). Also, Indian writers followed the American model and included within industrial relations the full range of topics related to labor problems and the employment relationship, albeit with more emphasis on collective than individual relations (Seth, 1966). Giri's textbook is illustrative since it includes separate chapters for personnel management, labor law, social insurance, trade unions, and national labor policy. Also illustrative are early issues of *Indian Journal of Industrial Relations* which contain articles on all areas of the employment relationship, including labor law and management. By way of contrast, the range of topics in early issues of the *British Journal of Industrial Relations* is noticeably narrower.

America has one of the least regulated labor markets among advanced industrial countries and yet India has, by most accounts, much the opposite with a highly complex, bureaucratic, and protective regime of labor law (Debroy & Kaushek, 2005; Venkatta Ratnam & Verma, 2010). One has to conclude therefore, that while the American model may have to some perceptible degree influenced the formation of industrial relations in India as an academic field of study, its influence on the regime of IR institutions and labor laws actually put in place in India pales next to the influence of Great Britain (Kennedy, 1965). Not surprisingly, therefore, one of the imports from Britain – most visibly and influentially brought back by India's first Prime Minister — was the democratic socialist economic development model espoused by intellectuals and political leaders associated with the Fabian Society, British Labor Party, and other left-leaning groups (Narayan, 1964; Nanda, 1996).

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Nehru spoke often and eloquently on his desire to steer India toward a democratic form of economic planning and market socialism which was positioned between American-style capitalism and Soviet style communism (Akbar, 1990). The exemplars of the period, from which he gained inspiration on his extensive foreign travels throughout Europe in the 1910s-1940s, were countries such as Britain, France and Sweden which moved toward nationalization of core industries, five year economic plans with state directed investment, national labor movements, social welfare states, state

bureaucratic regulation of business, steep income, wealth, and estate taxes, and an end-goal of 'euthanasia of capitalism.' American ambassador to India in the early 1960s, John Kenneth Galbraith, recalled that, "Nehru loved to reminisce about the world of R.H. Tawney, the Webbs and of Trinity College and Cambridge" (Nanda, 1996: 478). Unfortunately, India also followed in Britain's post-World War II footsteps and went down the socialist path to 'poor man of East Asia' by the late 1980s (Das, 2001; Drèze & Sen, 2013).

Two Faces of the Webbs

The Webbs are co-founders of two different intellectual streams of thought. The first stream is a field of labor studies known as industrial relations with roots in historical-institutional economics and sociology and the second is a collectivist-oriented doctrine of evolutionary democratic socialism known as Fabian Socialism. Although the Webbs intend both parts to seamlessly fit together, they nonetheless have an identifiably separate presence in their work and the latter is considerably more radical and transformative than the former. A brief synopsis follows, labeled as their *industrial relations face* and *Fabian socialism face*, respectively.

Industrial Relations Face: A detailed review and exposition of the Webbs' theory of industrial relations is provided in Kaufman (2004; 2013) and Kaufman & Barry (2014). Provided here is only a brief summary as it pertains to consideration of labor law reform. A more general exposition of the industrial relations theory of labor law is provided in Kaufman (2012a).

The Webbs, like Commons and other IR founders, were attracted to the study of labor as a way to discover methods to raise the condition of the working people, reduce class conflict, and make the work world more efficient, equitable, and democratic. They gained insight from Marx but rejected his theory of class struggle and proletarian revolution. The Webbs saw that the labor problem writ large, and individual labor problems writ plural, come from structural features of the capitalist employment relationship which can be contained and de-radicalized by institutional reform but never eliminated.

Central to their diagnosis are three interacting factors in a private property, competitive market, laissez-faire system. The first is that human labor is treated as a commodity to be traded on a buy-low/sell-high basis, putting workers in a de-humanized, insecure, and distrustful position which, in turn, undercuts productive efficiency, abuses human rights, and breeds conflict. The second is that the capitalist employment relationship contains an inherent inequality of bargaining power between employers and workers in both external and internal labor markets with consequent low wages, long hours, harsh conditions, sizable income inequality, and arbitrary treatment, arising from widespread surplus labor, involuntary unemployment, market and organizational failures, and employers' unrestricted private property rights. The third

is that in early capitalism the mass of workers are typically given little-to-no voice, representation, and due process rights inside firms, thus making the workplace an industrial autocracy — sometimes benevolent but often despotic — while in the polity at large capitalists and the rich dominate the government and set the rules of the game to keep labor politically and economically subordinated and exploited.

The Webbs point to many onerous and inequitable outcomes that arise from these defects in the capitalist employment relationship. Topping their list, however, are two. The first is persistent and widespread unemployment which puts the employer in a despotic 'take it or leave it' position and forces workers to accept shameful conditions and callous exploitation – outcomes orthodox economic theory either denies as a matter of logic or claims flexible wages automatically eliminate. The second is glaring social injustice when rich, powerful, and socially privileged elites use the government to rig the game so they can siphon large surplus income (economic rents) produced by a mass of common laborers working all year round in life-shortening sweatshop conditions.

Having diagnosed the cause of labor problems in capitalism, the Webbs offer a variety of solutions. They recognize the place to start an evaluation of labor policy is specification of the social objectives which policy is intended to achieve. They follow orthodox economics and make efficiency the first priority but argue for an enlarged conception of social efficiency.

An economic system is socially efficient when it best satisfies consumers' wants but subject to covering all social costs of production. For labor, social cost includes minimum sustainable living expense for a worker and family, ability to acquire and maintain the human and social capital required for production, and provision of workplace conditions and treatment which cover socially recognized human and political rights. Non-labor social costs include infrastructure, environmental sustainability, and quality of life dis-amenities. These costs must be covered and incorporated into product prices or private cost of production is less than social cost, leading to a negative externality-type market failure.

The Webbs put-forth a two-prong labor policy program to promote social efficiency. The first prong is to improve wages, conditions, and treatment for workers in the lower part of the industrial pyramid. Doing so also keeps wages and labor conditions growing in line with productivity growth, thus maintaining macroeconomic demand/supply balance and social justice (Hobson, 1923; Commons, 1934). American writers call this part of the IR strategy 'raising the plane of competition.' To accomplish this goal, the Webbs propose establishment of a common rule that extends across the national labor market and requires all employers to provide a minimum standard of terms and conditions of work.

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This minimum is called the Social Protection Floor by the International Labor Organization (ILO).Since social cost rises over time, so should the level of the minimum standard.

Many employers and neoclassical economists oppose protective labor laws, or resist strengthening them, because they increase the price of labor, move firms up their labor demand curves, and reduce jobs (Wachter, 2012). However, what they fail to appreciate is that this loss of jobs promotes social efficiency by bringing private cost closer to social cost, thus ending an implicit social subsidy for consumers and firms – particularly the affluent elite who do most of the consumption (Kaufman, 2009). The parallel situation is loss of jobs when government decides to curb industrial pollution, say by putting an emissions' tax on firms.

The social cost common rule can be established through one or a combination of methods, all of which the Webbs promoted and were later made staple subjects in labor problems textbooks. A common rule, for example, can be established by industry-wide collective bargaining, protective labor laws such as minimum wages and maximum hours, social insurance such as unemployment compensation and old age pensions, or public sector funded jobs programs. Setting the common rule is challenging because social cost of labor varies by family size, urban vs. rural location, stage of economic development, and other such factors; nonetheless, many countries, including India, specify an official poverty line based on such contingencies so the task is not insuperable.

Also challenging is the contradictory role of trade unions in this process. On one hand, without a strong labor movement workers suffer from an inequality of bargaining power in labor markets and the government is inevitably dominated by business interests who block or greatly weaken protection for workers through labor law and social insurance. On the other hand, a strong labor movement inevitably leads to many counter-inefficiencies which frequently grow worse over time. In the labor market, the initial effect of unions is 'monopsony-reducing' as they level the playing field and promote social justice; however, over time they become 'monopoly-creating' as their continual push for 'more,' coupled with only patchwork organization across industries, gradually leads to inflated wages, productivity-sapping work practices, and a privileged labor aristocracy (Kaufman, 2012b). Likewise, in the political process unions have a tendency to shift from a broad-based voice of the working class to a narrow sectional interest group largely concerned with protecting their institutional power and member's vested perquisites.

The first prong of the Webb's labor strategy is to push up on the lower end of the industrial pyramid by using collective bargaining, legal enactment, and social insurance to establish and then gradually raise the plane of competition. The second prong is to push down on the top end of the pyramid through egalitarian social policies and progressive income, wealth, and inheritance taxes. The Webbs agree that people who make large contributions to production through

successful entrepreneurship, management, and technical skills deserve higher wages and income. In this respect the Webbs accept the marginal productivity theory doctrine. However, it is also their view that much of the income received by top-end groups in society takes the form of an economic rent, called surplus value by Marx and unearned income by J. S. Mill.

Much of the income received by top-end groups in society takes the form of an economic rent.

An economic rent is created when a resource owner receives a return higher than minimum supply price, such as in the case of a monopoly rent when a firm with market power charges a price higher than cost of production. From the Webb's perspective, and as also expounded by their Fabian colleague Hobson (1923), a significant portion of profit, interest, land rent, and high-end salaries – factor returns mostly accruing to socially privileged people in the top end of the income and wealth distributions – are a rent payment made possible by various natural and contrived scarcities and barriers to competition. Large CEO salaries, for example, are partly a payment for valuable leadership and business acumen but, also, a rent payment made possible by family connections, political patronage, or cronyism with the board of directors. Similarly, the high salaries of doctors, professors, and government officials are partly a return on human capital investment and hard work but, for many, also a rent payment for being born into a socially advantage family with the money, social connection, caste, and skin color to first get into elite private schools and universities and then high-end professions and corporations.

The nature of an economic rent is that it can be taxed away without reducing supply or distorting incentives. Since rent is an unearned income, and because it also provides the affluent and powerful with large sums of money to twist the political process to preserve and strengthen their privileged position, the Webbs were strongly in favor of enacting steeply progressive income, wealth, and inheritance taxes. They were also strongly in favor of social policies that break down artificial barriers to competition and social mobility, such as contained in preferential laws, institutional rules, and social norms favoring men over women, upper class over lower class, and light-skinned over dark-skinned. Equally favored were policies that opened the door to equal opportunity, such as quality universal public education and health care and civil service rules for government employment.

Fabian Socialism Face

Part of theWebbs' claim to founders' status is that they were among the first writers to articulate these principles in such a thorough and penetrating way. If this part of the Webbs' thought is all that had influenced Nehru, the post-Independence history of India would be considerably different. However, the influence of the Webbs, Hobson, Tawney, Besant,

and other Fabianson Nehru and India was not primarily through the case they developed for industrial relations but, rather, the case they built for transition of the national economy from free market capitalism to democratic socialism and industrial planning (Narayan, 1964; Akbar, 1990; Das, 2001).

Surveying the history of 19th century England, Sidney Webb in his chapter in the *Fabian Essays in Socialism* (Shaw, 1889: 46-47) tells readers of the "hopeless failure of an almost complete industrial individualism…[with] unrestrained private property… [and] subjection to a political oligarchy". Like Marx, Webb thought the transition to socialism is inevitable and, indeed, states, "the economic history of the century is an almost continuous record of the progress of Socialism" (ibid.). But unlike Marx, Webb sees no need for class struggle and revolution. He and Beatrice were convinced that the wage-earning class was coming to realize the superiority of planned socialism over anarchic capitalism. They also thought, with the gradual democratization of the national government driven by popular pressure and extension of suffrage, political control of the state was shifting from the oligarchy of capital and land owners who dominated Parliament and most benefited from laissez-faire capitalism to the mass of wage-earners who most benefit from socialism. He concludes his chapter, therefore, with this forecast: "private ownership of the instruments of production is irreconcilable with the common weal…[It] keeps the many workers permanently poor… in order to make a few idlers rich…[and] will inevitably go the way of feudalism which it superseded" (Shaw, 1889: 81-82). Part of the reason the Webbs founded the LSE was to train administrators and managers to staff the future socialist state planning apparatus.

Many socialists are frustratingly vague about the transformation from capitalism to socialism and the institutional structure and performance of a socialist economy. The Webbs are exceptions and devote an entire book, *A Constitution for the Socialist Commonwealth of Great Britain* (1920), to this purpose. With the wage-earning class exercising democratic control of the government, a process of nationalization of industry is initiated, starting with core or 'commanding heights' sectors (e.g., steel, banking, transport, communication) with gradual but not complete extension to other sectors. Planning boards are created for each industry to make strategic investment, production, and pricing decisions and exercise supervisory oversight of publically-appointed management. Private property for individuals is protected but private ownership of industry is gradually extinguished through a mix of confiscation, fair market value compensation, and steep profits tax. The end result is the "transformation of profit-making enterprise into public service" (Ibid: 334) with greater efficiency achieved by replacing capitalist monopoly, waste, and boom-bust cycles with public price regulation, scientific enterprise administration, and coordinated planning of production and investment.

Implications for Labor Law Reform

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Nehru and the National Congress Party gradually implemented a democratic socialist planned economy model for India which in broad outline matched the Fabian prescription and post-war governance regimes in Britain, France, and other European countries, albeit with numerous Indian adaptations for its status as an Asian developing nation and non-aligned country in the Cold War. The initial growth results were encouraging but then faltered in the 1970s and 1980s amidst rising crises with inflation, balance of payments deficits, and mounting labor strikes (Bhattacherjee, 2001; Nankervis, Cooke, Chatterjee & Warner, 2013: Ch.4).

Many other countries experienced similar problems. In reaction, British voters in 1979 and American voters in 1980 decided to shift toward neo-liberalism by electing Thatcher and Reagan. Although the score card for both leaders is mixed, two trends are clear. The first is the growth rate of both economies staged a considerable rebound until punctured by the world financial crisis of 2008-2010, fueled in part by liberalization of product and financial markets and expansion of small-medium entrepreneurial-driven firms. The second is that both countries also reshaped their labor law regimes through a two-pronged strategy which rolled-back union power and collective bargaining and substituted expansion of minimum employment standards through specific labor law additions. The UK, for example, adopted a national minimum wage and various European Union directives on work hours and workplace information-sharing while the USA adopted guaranteed family and medical leave for women workers and discrimination protection for handicapped workers. Although neo-liberalism is typically associated with deregulation, it is particularly evident in the case of Britain (less so the USA) that breadth of labor market regulation actually increased, partly to fill the void left by receding collective bargaining and partly to protect the vulnerable from a market-induced race to the bottom by setting-up a strengthened floor of minimum employment standards à la the Webbs (Mitchell, Gahan, Stewart, Cooney, & Marshall, 2010).

Now, what about India? To an outside observer, it appears that India has only partially accomplished product and financial market liberalization and barely touched labor market liberalization. However, in the case of labor law the kind of reform that is needed is only partly liberalization — i.e., loosening regulatory/legal constraints to spur job-creation by reducing labor cost and promoting employment flexibility – and more in the direction of regulatory modernization and improved governance. This dimension of the subject is postponed, however, to later in the paper. The strategic point of entry into the labor law reform debate is, perhaps paradoxically, not in labor markets but product markets.

India needs to generate roughly twelve million new jobs each year to keep-up with labor force growth. Further, these jobs need to offer better wages and conditions to satisfy the rising quality of life expectations of the Indian people. One can reasonably argue about the degree of blame to be laid at the door of European socialist doctrines and their importation by Nehru and the Congress Party but, regarding the general argument that India still suffers from excessive government intervention and costly economic regulation, the evidence seems clear-cut. Indeed, this theme runs like a gold thread through books and policy reports on the growth prospects for the Indian economy (e.g., Drèze & Sen, 2013; Hope, Kochar, Noll & Srinivasan, 2013; World Economic Forum, 2014).

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India, as oft-observed, is a land of sharp contrasts and contradictions (Nilekani, 2009). On one hand, liberalization has spawned a rapidly growing IT sector and expanding number of world-competitive companies. On the other hand, much of India remains mired in poverty and archaic business practices. Although only an anecdotal account, mentioned earlier was law professor Richard Epstein's discussion of his first visit to India in early 2014 and in it he provides in microcosm the extent to which liberalization still remains a considerably incomplete project (Epstein, 2014). Rather than being able to buy a mobile phone at one store with a credit card and relatively transparent and easy-to-complete contract, he had to travel around the choked streets of Mumbai to seven different stores to get photographs, purchase the phone, purchase the SIM card, on several occasions fill-out lengthy paperwork, and always pay with cash. In the short-run, this round-about process creates jobs for the taxi driver, shop keepers, and government officials but in the long-run it keeps India trapped in a low productivity third-world type economy with anemic job growth as other Asian countries gain competitiveness, move upstream into higher paying manufacturing, and increase export share at the expense of Indian companies (Drèze & Sen, 2013).

More comprehensive and authoritative evidence on sources of growth in GDP and employment is provided in several policy reports, such as the World Economic Forum's *Global Competitiveness Report 2013-2014* and World Bank's *Doing Business 2014*. Both reports paint a depressing picture of India's economy hobbled by institutional constraints and mal-governance. In terms of global competitiveness (World Economic Forum, 2014: Table 3), India ranks 60 out of 148 countries and is behind numerous other developing East Asian countries, including Singapore (2), Taiwan (12), Malaysia (24), China (29), Thailand (37), Indonesia (38), and Philippines (59). In terms of ease of doing business (World Bank 2014, Table 1.1), India ranks 134 out of 190. The anomaly of this poor performance on competitiveness and business creation is that when Indian people

emigrate to better governed and more market-friendly countries they achieve impressive success in entrepreneurship, occupational attainment, and family income.

Job creation is only another name for what economists call labor demand and economic theory teaches that the strength of labor demand is a direct function of the strength of product demand. Thus, adopt measures that increase Indian companies' product demand and their labor demand is certain to follow, albeit moderated by productivity growth. The message of this insight for the labor law reform debate in India is: put strategic emphasis where it counts the most, which is not in labor markets per se but on impediments to growth in product markets.

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Two pieces of evidence support this proposition. First, the *Global Competitiveness Report* divides countries into five stages of economic development, starting at the low end with Factor Driven, in the middle with Efficiency Driven, and at the top with Innovation Driven. The report also notes that the key drivers of growth differ across stages of development; for example the best way for a Factor Driven country such as Cambodia to improve competitiveness is not necessarily the best way for an Innovation-Driven country such as Germany. The report identifies twelve 'pillars of competitiveness' and ranks the most important for each development stage. The report places India in the low Factor Driven stage. At this stage, the report identifies four pillars as critical: Institutions, Infrastructure, Macroeconomic Environment, and Health and Education. If ranked only on these four competitiveness pillars, India falls from an overall position of 60 to 96. In other words, on the critical 'must do' ingredients for growth India is actually in a considerably worse position than suggested by its overall competitiveness ranking.

Labor Market Efficiency is also one of the twelve pillars in the competitiveness ranking. However, it is rated as a critical success ingredient only when countries get to the intermediate Efficiency Driven stage – which India has not reached. Further, with respect to labor market efficiency, and five other pillars considered critical for countries at the intermediate stage, India's ranking actually rises from 60 to 42. Hence, the evidence is fully consistent with the conclusion earlier reached by Venkata Ratman (2011): excessive and overly rigid labor regulation is *a* problem for India but not *the* problem.

Additional insight on why labor market over-regulation is not the strategic factor with respect to India's growth and job creation conundrum comes from reading the report's discussion of the first of the twelve pillars, Institutions. It states (World Economic Forum, 2014: 4-5),

"The institutional environment is determined by the legal and administrative

framework within which individuals, firms and government interact to generate wealth…[However,] the role of institutions goes beyond the legal framework. Government attitudes toward markets and freedoms and the efficiency of its operations are also very important: excessive bureaucracy and red tape, overregulation, corruption, dishonesty in dealing with public contracts, lack of transparency and trustworthiness, inability to provide appropriate services for the business sector, and political dependence of the judicial system impose significant economic costs to business and slow the process of economic development".

This quotation highlights fundamental constraints on job creation in India because they obstruct the long-run productivity and competitiveness of the nation's employers (more below). A debate on labor law reform, therefore, must be broadly framed to include these types of obstacles in product markets. Shortening the purchase process for a mobile phone from seven transactions to one is a concrete example.

The second piece of evidence comes from the report *IFC Jobs Study* by the International Finance Corporation (2014), a subsidiary of the World Bank. The report develops a conceptual framework for thinking about the factors that stimulate and impede job growth. The framework begins with the labor market and the forces shaping labor demand and labor supply. However, the report also concludes that a labor market focus by itself is greatly incomplete. Illustratively, the report analyzes responses from managers at over 45,000 enterprises in 106 developing countries to the question: "Which of the following elements [15 items in a list] of the business environment, if any, currently represents the biggest obstacle faced by this establishment?" Respondents listed the following items as the top seven: Access to finance, Access to electricity, Informality, Tax rate, Political instability, Inadequate educated workforce, and Corruption. Labor regulation was #14 on the list and was cited by only 3 percent of respondents.

What is the connection between this discussion and the Webbs? One can plausibly argue it reveals the fatal contradiction in their theory of political economy. The Webbs correctly identify in their industrial relations face that surplus labor and unemployment are the most serious causes of poverty, substandard labor conditions, and unequal bargaining power. However, they also propose in their Fabian Socialism face a growth model which creates these conditions by stifling entrepreneurship and capital investment. In fairness, when the Webbs formed their opinions on capitalism vs. socialism the record of capitalism had a number of serious blotches, including periods of deep economic crisis and mass unemployment. Their conversion to socialism was thus partly born of skepticism that capitalism could ever produce reasonably sustained and balanced growth. The most recent world financial crisis suggests their concerns are not to be cavalierly dismissed. Nonetheless, the record of the last sixty years – with the considerable help of economist J.M. Keynes and government demand management – suggests

the Webbs picked the wrong horse in the growth and prosperity race. Their policy program of slowly restricting and narrowing the economic space for market forces and entrepreneurial action appears, therefore, ill-advised and harmful to the interests of the working class which, paradoxically, they sought to promote. Unfortunately, on achieving independence India also bet on the socialist horse and seven decades later the pernicious effects in stifled product market performance are still reverberating into lackluster labor market performance.

Regulation & Performance of Labor Markets.

The message of the previous section is that all of India's labor laws and regulations can be shredded and the positive effect on economic growth is likely second-order. But, at least in industrial relations, this scenario is not countenanced even if it were politically feasible. The reason is that industrial relations has from its beginning days maintained that capitalism functions best when labor law and social insurance are used to stabilize, balance, professionalize, and humanize labor markets and workplaces (Budd, 2004; Kaufman, 2004).

Diagrammatically, IR theory predicts the relationship between labor market regulation and economic performance is an inverted U (regulation on the horizontal axis from 0% to 100% and GDP/job growth on the vertical axis) so that optimal labor law is not zero but an interior point somewhere in the moderate middle (recalling IR = the 'middle way'). One notes that proponents of neo-liberal free market economics, such as Professor Epstein, disagree with industrial relations proponents on this critical point. Epstein (2012:203) advances a close-to-zero position, stating, "Why not try competition across the board – which would lead to repeal of virtually every labor law that regulates wages and terms of employment, except perhaps with respect to health and safety?"

The IR answer to his 'why not?' question comes from the Webbs, Commons, Gandhi, and other proponents of a human conception of labor (Kaufman 2010, 2012a). That is, when labor is treated as a commodity in unprotected external and internal labor markets the results are likely to be closer to the predictions of Karl Marx than Milton Friedman. Reasons are because productivity sinks (from low morale, trust and cooperation), firms skimp on investments in human capital and human resource management, costs escalate from high turnover, conflict, and shirking, and workers look to militant unions and socialism for protection. Note may be made here that in this regard the IR argument for labor law is paradigmatically different from the standard neoclassical model. In the latter, a competitive labor market is the ideal and labor law is sanctioned only in the case of irremediable market failures; in the former, a competitive labor market is far from ideal as a basis for a high-performance employment relationship and labor law is required to create order and stability (Kaufman, 2010; 2012a). Thus, from an IR perspective, Fabian Socialism does not provide the optimal amount of labor regulation (to the

right of the inverted U) but neither does free market neo-liberalism (to the left of the inverted U).

Little doubt exists that India needs a substantial overhaul of its labor law regime.

Little doubt exists that India needs a substantial overhaul of its labor law regime. The basic framework was created in the late 1940s-early 1950s, but with substantial roots in British colonial statutes going back to the 1920s. Maintaining industrial peace was then the central goal, partly a reflection of British imperial interests but also the Gandhian emphasis on social harmony (Kennedy, 1965; Sundar, 2010). Not even the most presciently designed labor law system, however, can remain a good fit in the 2010s when designed more than a half-century earlier for a largely rural, handicraft, and informal economy. Of course, Indian labor law has not been completely static over the decades and economic liberalization and globalization of product markets have increased the pressure for change. Also, labor law reform has been the subject of numerous commissions, reports, political speeches, and proposals to Parliament (Venkata Ratnam, 2004; Shah, 2013). To the frustration of actors in all parts of the IR system, however, direct government action has been exceedingly slow, particularly at the national level.

Where change in labor regulation has occurred, the movement is sometimes in the wrong direction. For example, the labor law provision which critics cite as the impediment to growth (Das, 2006; Datta & Sil, 2007; Krueger, 2013) – the ban in the Industrial Disputes Act (1947) on terminating workers and closing establishments – has been revised over the years but by *lowering* the employment threshold so it covers not only large firms but numerous small-to-medium sized firms (firms with more than 100 employees). Even people committed to fully protecting workers' rights can see that this rule – coupled with equally restrictive business insolvency rules — imposes potentially severe financial risks and penalties on firms in a market system with fluctuating sales due to product life cycles, business cycles, and seasonal customer orders. Further, this rule undermines competitiveness and economic development by incenting investors and entrepreneurs to keep firm size below the 100 person floor, thus sacrificing economies of scale and modern production technology and exacerbating industrial dualism and a stunted manufacturing sector (Debroy,2005; Kruger, 2013; Kumar, 2014). Companies also evade the rule by hiring more contract workers and closing down facilities through the subterfuge of a labor dispute lock-out.

Looking at the Indian labor law regime through the lens of the Webbs' industrial relations face, two structural problems look most important to reform. Recall, as context, the Webbs seek to promote social efficiency and justice by using legal enactment and trade unions to push-up on the lower end of the industrial pyramid and push-down on the top end. The first structural reform, there-

The main corpus of Indian labor law applies to only about 7 percent of the labor force, limited mostly to people in the organized sector.

fore, is of the 'push-up' nature, achieved by extending the basic protections of labor law to a much larger part of the workforce. This task is difficult because 60 percent of the Indian workforce is still in the agricultural sector and another large share are wage workers or self-employed in the informal sector (Hill, 2009; Venkatta Ratnam & Verma, 2010). But, in another reflection of extreme economic dualism, the main corpus of Indian labor law applies to only about 7 percent of the labor force, limited mostly to people in the organized sector (Shah, 2013). In the Indian context, 'organized sector' includes all public sector organizations and private sector non-agricultural enterprises with 10 or more employees.

The Webbs advocate that a common rule be established across all labor markets – including the market for day laborers, contract workers, and self-employed – which provides minimum wages, conditions, and treatment consonant with social costs and human rights. Nine out of ten people in the Indian workforce do not have this minimum guarantee and several hundred million live in abject poverty (Hill, 2009). Hence, the first-prong of labor law reform is to broaden the base of coverage. An example in this spirit, defects in implementation and administration notwithstanding (Shankar & Gaiha, 2013), is the Mahatma Gandhi National Rural Employment Guarantee Act (MGNREGA) – a law passed in 2005 which guarantees 100 days of wage employment to rural households if adult members volunteer for unskilled manual labor on community projects. Also illustrative are various income supplement devices, such as for widows, disabled, and retired people, under the National Social Assistance Program (1995), although it so far provides benefits to only 21 million people (Subrahmanya, 2013).

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The Webbs also counsel using legal enactment to push-down on the top of the industrial pyramid on the argument that a significant part of the high earnings of the affluent elite is economic rent siphoned from society through monopoly market barriers, government-created privileges, and closed family and social networks. Part of the success of the Indian economy over the last two decades is that it has created a new middle class, numbering approximately 50 million or 5 percent of the population. However, it has also spawned a tiny elite of super-rich whose share of the country's wealth has skyrocketed from 1.8 percent to 26 percent (Peeples, 2014). Some of the super-high income is a much deserved return to entrepreneurship and capital investment; however, another portion is from gaming the system. As part of liberalization, India also substantially reduced the progressivity of income tax

rates and eliminated an estate tax. Labor law (broadly defined), therefore, needs to counter this trend toward rent-seeking and inequality. One avenue is social initiatives to open-up access to high income parts of the job distribution, such as greater educational opportunities for society's poor and disadvantaged and greater legal enforcement of hiring, promotion and pay on the basis of merit rather than connection and caste (Bhandari, 2014). The other avenue is to impose higher effective tax rates on family income through base-broadening and better enforcement while shutting-off egregious sources of rent-skimming, such as the too-often corrupt process of awarding public contracts.

Finally, although nearly all commentators say touching trade union law is politically impossible, a Webbian perspective suggests that here too significant reform is needed. Currently trade unions represent perhaps as few as 3 percent of the workforce (Sundar, 2010), mostly in the small organized sector and often in public sector employments, and exact a considerable efficiency cost through restrictive employment practices, political infighting, and adversarial relations. Labor law reform should take politics and conflict out of union recognition and collective bargaining by institutionalizing recognition and bargaining procedures (Venkatta Ratnam, 2004); the same procedures would help shift trade unions from an entrenched protector of a narrow-based labor aristocracy to a broader-based but less adversarial and politicized workers' representative.

Effective Implementation & Good Governance

Liberalization in the early 1990s opened-up the opportunities and incentives needed to fuel a growth surge but, as noted in the introduction, the surge may have faded. Observers can pick-out a variety of structural reforms, including labor reform, which will help put stronger wind into India's economic sails. None of these reforms are likely to make much difference, however, if not well implemented, administered, and governed. Here seems to emerge the critical weak spot in India's future and thus the key point for strategic attack (Nilekani, 2009; Debroy, Bhandari, 2013; World Economic Forum, 2014) Das (2006:1) remarks about India's growth surge, "what is most remarkable is that rather than rising with the help of the state, India is in many ways rising despite the state". He adds, "Although Indians blame ideology (and sometimes democracy) for their failings, the truth is that a mundane inability to implement policy – reflecting a bias for thought against action – may have been even more damaging" (ibid: 2). The same diagnosis is made by Nandan Nilekani (2009:457), founder of one of India's IT success stories, Infosys Technologies Ltd. "Implementation, sadly, has long been India's weak spot".

Indian workforce is the most highly protected in East Asia.

India currently has more than 45 national-level labor laws and five times that many at the state level (Debroy & Kaushek, 2005), making the Indian

workforce the most highly protected in East Asia (Basu, Fields & Debgupta, 2000). The reality, however, is starkly different. Due to substantial dualism, about 10 percent of the workforce enjoys too much labor protection while the other 90 percent enjoys too little. However, many Indians feel cynical and frustrated about the government's ability to redress this imbalance (Debroy & Bhandari, 2013; Transparency International, 2014), albeit with a bounce in hope that the new Modi government can do better.

Implementation and governance are separate but related dimensions of institutional performance. Implementation occurs after a labor law is passed; for example, firms need to make sure they are paying at least a minimum wage and government must monitor and enforce compliance. Governance is faithfully and efficiently executing the law and keeping it free of corruption. By some accounts, India currently has the worst-performing bureaucracy in East Asia and the nation ranks 94 on perceived corruption (Political & Economic Risk Consultancy Ltd, 2013; Transparency International, 2014). This nation-state problem is reflected in lax labor law implementation and corrupt governance. For example, labor inspectors are bribed, firms keep double sets of accounting and payroll records, union officers take kick-backs, and government program administrators embezzle funds. It is estimated that only 15 percent of the government's anti-poverty funds reached the poor in the mid-2000s ("Corruption in India, Cause of Instability & Inequalities," poverties.org/corruption-in-india, 2014) and the annual funds diverted through corruption are one-third larger than total government expenditure on health care ("Corruption – An Epidemic of Epic Scale in India," *Huffington Post India*, May 5, 2014).

The point to be emphasized, therefore, is that enacting new labor laws and modifying existing ones is only part of the labor law reform battle. Attention must also be given to the unglamorous but critical aspect of implementation. This insight is hardly new. American IR founder John Commons noted (Commons &Andrews, 1936: 448), "More important than the hasty enactment of additional laws is the adoption of methods of administration that will enforce them. It is easy for politicians or reformers or trade union officials to boast of new laws which they have secured for labor, and it is just as easy to overlook details or appropriations or competent officials." Translated into the inverse U- shaped diagram of optimal labor regulation (earlier cited), this consideration makes the theory more complicated because it is not only an issue of too much or too little regulation but, perhaps more importantly, better regulation.

The Webbs were quite mindful of the importance of efficient and honest labor regulation and, indeed, as earlier noted they founded the LSE in part to train high-class managers and administrators for the new socialist planned economy. The Webbs were optimistic for they thought England possessed one of the finest government bureaucracies in the world (Webb &Webb, 1920: 319). As it later proved, the Webbs were too optimistic on the possi-

bilities of socialist administration and here is another fatal flaw in their political economy. Commons (1921) judged the Webbs woefully naïve about the possibilities of administering a socialist state and concluded such a system was an impossibility in the USA because the American people are "administratively incompetent" (Commons, 1934: 846).

When the Webbs visited India in 1911, they were impressed with the quality of governance exhibited by Indians recruited into the Indian Civil Service, although on the voyage home Sidney Webb was moved to say, "Three months' acquaintance has greatly increased our estimate of the Indians, and greatly lessened our admiration for, and our trust in, this Government of officials" (Jayal, 1987: 209). In rendering this negative verdict, however, Webb noted that "we have found the British officials more inaccurate and more disingenuous than the Indians" (ibid: 119). Braibanti (1963) claims the Indian government administration was among the dozen best performers in the 1950s; other observers, however, questioned at the time whether Nehru's idealism and faith in people were matched by the administrative capacity of the Indian state and indicate that corruption was growing around him (the Gorwala report of 1951, cited in Akbar, 1990). These fears turned out to be justified and India has traveled a six decade path toward less efficient and honest administration. The USA featured rampant corruption and mal-administration in government in the 19th century and one of the keys to its successful development in the 20th century was reforming a diseased system from within. Here, it seems, is a similar institutional challenge for India and of which labor reform is a part.

Conclusion

The Webbs' writings present a mixed picture with respect to Indian economic development and industrial relations policies. The industrial relations part continues to provide sound principles, such as a national minimum set at the social cost of labor. The Fabian Socialism part of their writings, however, has proved a recipe for sclerotic growth. This paper tried to untangle these diverse threads and work-out the implications for restructuring Indian labor law. Partly this exercise is useful because it stimulates thinking about the industrial relations field and, in particular, to what extent it has general principles and concepts useful for framing the reform debate and guiding it to a consensus program. Also, the debate on labor reform in India seems to follow along a fairly well-worn groove of analysis so perhaps bringing a different perspective to the matter à la the Webbs is useful for stirring new thinking and dialogue.

India is long over-due for substantial modernization and rationalization of its labor law regime.

India is long over-due for substantial modernization and rationalization of its labor law regime; a large cross-section of Indian people recognize this imperative; many books, papers and reports with detailed recommendations have been written on the subject; and yet frustratingly little happens. Possibly the Webbs

and the Fabian tradition make a contribution of a different kind for people who want change but are discouraged. The Fabian founders chose to name the organization after Roman emperor Fabius Maximus, renowned for his patience before launching an attack on the enemy. Even if the socialism part of the Fabian legacy is not helpful for the Indian IR field and labor law reform project, certainly helpful in a messy democracy is the patience and perseverance part.

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