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Enforcing Labour Standards in Fissured Workplaces: The US Experience

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Abstract

The employment relationship in a growing number of industries with large concentrations of low wage workers has become 'fissured', where the lead firms that collectively determine the product market conditions in which wages and conditions are set have become separated from the actual employment of the workers who provide goods or services. Instead, the direct employers of low wage workers operate in far more competitive markets that create conditions for non-compliance. We examine this evolution in employment and its implications for public policy in the US, discuss the factors driving fissured employment and sketch its main features and outcomes. We then look at the traditional methods used for labour standards enforcement in the US and discuss why they are poorly suited to address fissured workplaces. Finally, we survey how public policies might better address the realities of the modern workplace, including efforts in this regard by the Obama administration.

JEL Codes: J31; J38; J81; J88; K31

Keywords

Compliance; enforcement; fissured employment; labour standards; regulation.

1. Introduction

In recent decades, there has been a transformation of employment relationships within those sectors employing low wage workers in the United States of America (USA). The direct, two-party relationship assumed in federal and state legislation and embodied in traditional approaches to enforcement no longer describes the employment situation on the ground. Consider the following vignette.

A maid works in a well known, internationally-branded hotel. However, the property where she works is owned by a Real Estate Investment Trust — a legally established investment entity — who is her employer of record. Her work is supervised on a daily basis, her performance is evaluated, and the job's hours and payroll are managed by staff of a national, third-party hotel management company. At the same time, her daily work routines regarding cleaning, room

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set-up, and other work routines are set by standards established and monitored by the hotel chain whose name the property bears. Where does 'employment' reside in this situation?

This vignette is not limited to the hospitality industry. As major companies have invested in building well-known products as cornerstones of their business strategy, they have also shed their role as the direct employer of the people responsible for providing those products and services. In many cases, the jobs have been shifted to employers who pay low wages, seldom provide benefits, and frequently subject their workforce to conditions that violate wage and overtime, health and safety, and other workplace protection standards. These conditions are not an inevitable result of the nature of those jobs, but a result of how those sectors are organised.

Enforcement of labour standards in the millions of workplaces covered by US laws has always been challenging. The agencies charged with labour inspections have limited budgets and stretched staffing levels relative to their statutory responsibilities. But this is not the crux of the challenge. Adding additional investigators is a necessary, but not sufficient, requirement to address the regulatory task. The fundamental changes in employment relationships require a revised approach to enforcement, one that is built on an understanding of how major sectors of the economy employing large numbers of vulnerable workers operate and then using those insights to guide enforcement strategy. Just as the forces driving compliance with labour standards have changed, so must the strategies that agencies employ to improve conditions.

The employment relationship in a growing number of industries — particularly those with large concentrations of low wage workers — has become 'fissured', where the lead firms that collectively determine the product market conditions in which wages and conditions are set have become separated from the actual employment of the workers who provide goods or services. Instead, the direct employers of low wage workers operate in far more competitive markets that create conditions for non-compliance. We examine this evolution in employment and its implications for public policy in the US. We start by discussing the factors driving fissured employment and sketching its main features and outcomes. We then look at the traditional methods use for labour standards enforcement in the US and discuss why they are poorly suited to address fissured workplaces. Finally, we survey how public policies might better address the realities of the modern workplace, including efforts in this regard by the Obama administration.[1]

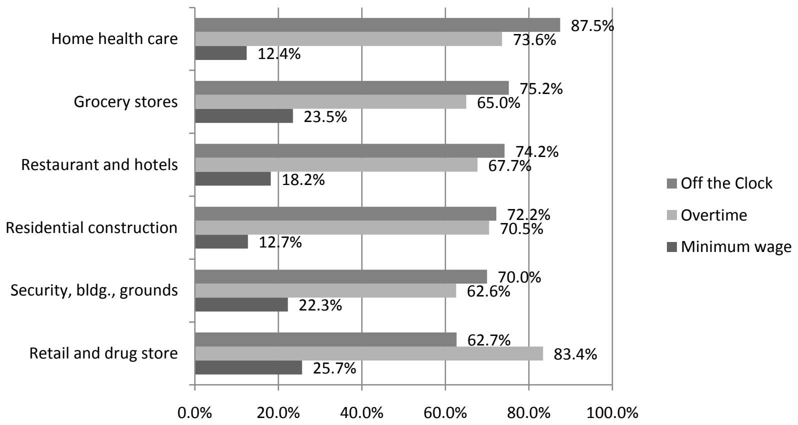
2. The Fissured Workplace

Industry Concentration of Vulnerable Workers

It has been well documented that jobs with low wages tend to also have other undesirable characteristics: few benefits, high turnover, higher safety and health risks, and limited opportunities for using voice, rather than exit, in dealing with workplace problems. Not surprisingly, these jobs also tend to have some of the highest rates of violations of basic labour standards as well as other workplace protections and rights (e.g. Carré et al. 2000; Bernhardt et al. 2008; Shulman 2003).

Bernhardt et al. (2009), in a landmark survey of low wage work in three major US cities, documented high rates of violations with labour standards in a number of low wage industries. Overall, 26 per cent of workers in their sample were paid less than the required minimum wage; 76 per cent of the workers who worked more than 40 hours in the previous week had not been paid the legally required overtime rate; 70 per cent of workers who were asked to come in early or stay after their shift were not paid for that work and were subjected to retaliation by their employers for complaining in some way about work conditions. Figure 1 presents estimates of the high rates of violation of standards regarding off-the-clock work, overtime pay, and minimum wage requirements in many of the industries discussed above.

Figure 1: Labour standards violation rates (per cent in violation) in selected fissured industries



Source: Bernhardt et al. 2009

Not only do jobs in retail, food services, accommodation (hotel and motel), and agriculture have high rates of labour standards violations, they also account for a disproportionate share of low wage work relative to the number of people they employ in the economy as a whole.[2] Thus, while retail workers constituted 10.2 per cent of the total workforce, they made up more than 20 per cent of all low-wage workers in the USA. Similarly, food and drinking services accounted for 6 per cent of employment but 12.5 per cent of all low-wage workers. Workers in both accommodation (hotel and motel) and agriculture sectors accounted for twice the proportion of low-wage workers that they represented in the economy as a whole. Overall, these industries make up about 20 per cent of total US employment, but close to 40 per cent of the country's low wage workers.

In contrast, construction contributed to about 5 per cent of all employment in 2006, and about the same percentage (4.7 per cent) of the low-wage workers. Workers in health care segments also accounted for about the same share of low-wage workers as they did in the economy as a whole, while a slightly higher share of low-wage workers (11.4 per cent) were found in manufacturing than in the economy as a whole (9.4 per cent).

Industries with high levels of labour standards noncompliance and large concentrations of low-wage workers are also a growing part of the US labour market. Close to 30 million workers are employed in the retail and leisure and hospitality industries in the US, the sectors employing the largest concentrations of low-wage workers. These sectors combined were projected to grow by almost 1.8 million workers between 2008 and 2018. Food services and drinking (the major component of the leisure and hospitality sector) was projected to grow by about 740,000 jobs over the same period (Woods 2009: 53, Table 4).

The factors responsible for the concentration of low wages and persistent violation of labour standards arise from a variety of economic and social factors that have been widely discussed (Bernhardt et al. 2008). These include increasing levels of global competition; a large influx of immigrant (sometimes undocumented) workers; changes in the organisation of work and in the structures of industries; and long-term declines in unionisation as well as workplace enforcement by federal and state governments.

Although all of the above factors play significant — albeit varying — roles, a critical factor derives from the market dynamics and business strategies of the sectors where those workers are concentrated. Lead firms in these industries relate to other, subsidiary businesses in those markets in a distinctive way and in so doing have altered the basic employment relationship.

Origins of Employment Fissuring

During much of the twentieth Century, the critical employment relationship was between large businesses and workers in major sectors of the economy. Large employers — General Motors, US Steel, and Alcoa — dominated major sectors of the manufacturing economy. Emerging industries also spawned giant companies: Kodak, IBM, and Xerox grew to be giants in their product markets and in the labour markets where they drew their workforces. While the service sector operated at a more local level, the national players that did emerge — Hilton and Marriott in hotels, Macy's and Sears in retail — similarly employed thousands (Brown, Hamilton and Medoff 1990).

Increasingly, however, the foci of employment shifted away from being between major businesses and the workforce that made or delivered their products. Large businesses with national and international reputations that operate at the 'top' of their industries continue to dominate the private sector landscape and play critical roles in shaping competition in their markets. However, they no longer directly employ legions of workers. Instead, like rocks split by elements, employment has been *fissured* away from these market leaders and transferred to a complicated network of smaller business units. Lower-level businesses typically operate in more competitive markets than those of the firms that shifted employment to them (Weil 2010).

Fissuring of this kind has been accomplished via the growing use of a wide variety of organisational methods: subcontracting, franchising, third-party management, changing workers from employees to self-employed businesses, and related contractual forms that alter who is the employer of record or make the worker-employer tie tenuous and far less transparent (Carré et al. 2000; Stone

2004; Ruckelshaus 2007; Zatz 2008). Lower-level businesses operate in typically more competitive markets, going head to head with other firms that also are seeking to provide services or goods to the lead firm or are in the network of one of the lead firm's top-level competitors.[3] More intense competition creates pressure to lower costs, particularly the most sizeable cost and the one most easily controlled: labour.

Multiple motivations underlie fissuring. In some cases, it reflects a desire to shift labour costs and liabilities to smaller business entities or to third-party labour intermediaries, such as temporary employment agencies or labour brokers. Employers have incentives to do so for obvious reasons. As has been documented in numerous studies, shifting employment to other parties allows an employer to avoid mandatory social payments (such as unemployment and workers compensation insurance, or payroll taxes) or shed liability for workplace injuries by deliberately misclassifying workers as independent contractors. Misclassification of this sort is a major problem, particularly in industries like construction and janitorial services (Carré and Wilson 2004; General Accounting Office 2009).

However, fissuring does not always arise from such direct and pernicious motivations. Some fissuring reflects technological developments that allow businesses to focus more productively on core competencies while shedding activities not central to the firm's operation. With the falling cost of coordination arising from information and communication technologies, productive reconfiguring of the boundaries of companies and entire industries naturally occurs and creates opportunities for new strategies.

Building Blocks

Employment fissuring represents the intersection of three business strategies, one focused on revenues, one on costs, and the final one providing the 'glue' to make the overall strategy operate effectively. First, in terms of revenues, companies in a wide variety of sectors have learned the competitive advantage arising from creating distinctive brands and identities for products and services. A successful brand creates a more loyal customer base more willing to pay premiums for products and services. Branding strategies require firms to create quality and performance standards to assure that the qualities underlying the brand are consistently achieved.

The intention to reduce costs — the second element of fissuring — shifts out the production of services or goods to other business enterprises. This has the impact of allowing lead companies to lower their costs since externalising activities to other firms operating in more competitive markets eliminates the need to pay higher wages and benefits that large enterprises typically provide. It also obviates the need to establish consistency in human resource policies since they no longer reside inside the firm. This aspect of fissuring also pushes liability for adherence to a range of workplace statutes (and other public policies) outward to other businesses.

Clearly, there is a tension between the two strategies: by shifting the provision of services to other businesses, companies that have created brands may jeopardise them if quality standards are not adhered to closely. The third element of fissured organisations is, therefore, the use of organisational structures and practices that allow the lead firms to promulgate, monitor, and enforce brand standards that the enterprises at lower levels must follow. These requirements also operate through organisational formats like franchising and licensing designed to create mechanisms to align the interests of lead and lower-level organisations.

The Revenue Side of Fissuring: Building Brands and Pricing Premiums

Enhancing revenue streams through product differentiation and the creation of market niches represents one side of fissuring strategies. In many of the industries where fissuring is common — hotel/motel, food services, retailing, and consumer products — major companies have sought to enhance the value of their products and services to enhance revenue streams. In part, this reflects the pressures on publicly and privately-held businesses to increase profitability to satisfy investors' target rates of returns.

Reputation-focused business strategy attempts to create a distinctive bond with consumers around products and services (Keller 2008). Successful branding allows a company to differentiate its products in the minds of consumers who, over time, become willing to pay a higher premium for them. Branding acts on the revenue side of profitability: the more successful the brand, the more that the business can charge a premium and expand and retain its customer base.

Take the fast food industry. Companies like Burger King, Subway and McDonald's spend millions of dollars each year creating a well-known brand for their products. This strategy fits an industry where perceptions of the quality, consistency, and variety of the product are critical to competitive performance. By establishing a brand, a fast food company can differentiate its product and create a loyal customer base willing to buy the product, and in some cases pay a premium for it, on an ongoing basis (Kaufmann and Lafontaine 1994). In the fast food industry, return business is partly based on the customer's belief that the experience will be the same in any outlet of the company visited. The investment in brand name and protection of its image is therefore a central part of the competitive strategy of national chains and an integral part of the way that it makes operational decisions.

The Cost Side of Fissuring: Solving the Webbs' Dilemma

> The most autocratic and unfettered employer spontaneously adopts Standard Rates for classes of workmen, just as the large shopkeeper fixes his prices, not according to the haggling capacity of particular customers, but by a definite percentage on cost. (Sidney and Beatrice Webb 1897: 281)

There is a more subtle and fundamental reason underlying employment fissuring, often missed by analysts who see it only in terms of attempts to avoid legal obligations or proponents who defend it as a positive reflection of the modern, flexible business organisation. As the social scientists Beatrice and Sidney Webb pointed out at the turn of the last century, large employers that dominated the economy and labour market of the last century required unified personnel and pay policies for a variety of reasons: to take advantage of administrative efficiencies; to create consistency in corporate policies; and to reduce exposure to violations of laws.

In addition, unified employment policies — particularly compensation policies — reduced frictions among workers: workers operating under one roof did communicate and might quickly discover that the person sitting in the next cubicle was being paid more for doing the same job. Paying individuals who did similar jobs different wages could have deleterious consequences on productivity, increase turnover, or even inspire a union organising drive.

There is a large empirical literature that shows that wages within firms vary far less than one would expect given the existence of considerable differences in productivity among workers (see Manning 2003, ch. 5 for a summary). Firms move towards a single wage policy for workers of similarly observable skill/ability because of the negative consequences arising from having multiple rates for workers who otherwise seem similar. Seniority-based pay is one imperfect way to vary wages based on differences in average productivity that strike most as 'fair'. But 'wage discrimination' (à la price discrimination) is rare with large firms.

Imagine instead if a large employer found a way to pay each worker a wage exactly equal to his or her value of production (that is, match the worker's wage to his or her marginal productivity). One way to do this without the internal organisational problems discussed above is to restructure its basic contract with workers so that the additional productivity of each worker hired is matched to his/her wage rate, and that the wage rate paid to one party has no impact on that paid to anyone else already employed (or potentially hired if production is expanded). In so doing, the employer captures the difference between the individual marginal productivity and what would be the prevailing single wage rate if it set one. Such a mechanism would benefit the employer over the case where it set a single wage rate for workers with similar job titles but variation in productivity, or in cases where an employer's wage policy impacts on the market as a whole.

A related argument for shifting work outward is related to the (dis)incentive effects of having large differences in wage rates in internal labour markets. Even if workers have differing skill levels and job assignments, equity norms in firms may lead large employers to pay lower skill workers higher wages because of the presence of higher paid workers whose compensation becomes a referent wage within the internal labour market. Shifting those lower skilled jobs outward can solve this problem. See Abraham and Taylor (1996) for a model and results showing that the likelihood of outsourcing low skilled work is higher in firms with high sklled occupations than in firms with only low-skilled occupations. Stark and Hyll (2011) provide a related discussion.

What happens, instead, if the large employer shifts the task of employing its workforce to multiple smaller parties who, in turn, compete with one another to obtain that large firm's business? Each small firm would offer its workers wages to perform work for the lead firm. As a result the lead firm would receive a price for the contractors' services or production rather than being required directly to set and pay wages to individual workers who actually undertake the work. As such, the larger employer creates competition for work among different purveyors, and pays them based on its assessment of their contribution. Less efficient producers could be paid less than more efficient producers. In this way, the lead organisation faces a schedule of *prices for services* rather than *wages for labour*, leaving the task of compensation to the individual providers of the service or product. In effect, the big player devolves its employment activity to a network of smaller providers. In so doing, it creates a mechanism — a competitive market for services that in the past was handled internally through direct employment — in the form of a network of service providers (subcontractors).

By shifting employment to smaller organisations operating in competitive markets, the lead firm creates a mechanism whereby workers will only receive a wage close to the additional value they create. At the same time, this avoids the problem of having workers with very different wages operating under one roof. The lead firm captures the difference between the individual additional productivity of each worker and what would be the prevailing single wage rate if it set one. As a result, two workers on the same project may effectively end up being paid very different wages, closer to something reflecting their individual marginal productivity than would be the case if they were in the direct employ of the 'parent' organisation.

The Glue: Brand Standards

A brand is a recipe for a particular product or service image in the mind of consumers,that, if successful, results in customer loyalty and a willingness to pay a premium for it. Creating a distinctive brand requires significant investment in the image (involving product development, consumer research and, of course advertising). But it also requires developing and promulgating standards for all units of the company to follow to ensure that the product meets consumer expectations once established. If delivery of the product is fissured off to other entities (franchisees, licensees, third party managers or others), the need to promulgate and assure adherence to standards is all the more critical.

In service-based industries like food and accommodation, standards describe how the product is made, presented, packaged, served or presented and advertised. Standards also proscribe the design, look, upkeep, and maintenance of the outlet or property where the product or service is provided. They also establish the role of the lead firm in assuring maintenance of those procedures.

The importance of standards to branding can be seen in the agreements that franchisees sign when they become part of a national chain. For example, the franchise agreement with Taco Bell states, 'You must operate your facilities according to methods, standards, and procedures (the "System") that Taco Bell provides in minute detail' (Taco Bell 2009). Similarly, Pizza Hut's agreement lays out the distinctive operational decisions that underlie the brand:

> A broad spectrum of the general public patronizes [Pizza Hut] Restaurants as a source of high-quality pizza and related products and services. A unique system characterizes Restaurants that consists of special recipes, seasonings, and menu items; distinctive design, décor, color scheme, and

> furnishings; standards, specifications, and procedures for operations; procedures for quality control; training and assistance programs; and advertising and promotional programs … (Pizza Hut 2009)

Not surprisingly, the methods, procedures, and guidelines regarding the creation of a good or provision of a service are the 'crown jewels' of a branded business. The book of standards associated with fast food or hotel/motel brands are highly confidential documents that are only provided to franchisees after they have been approved. Monitoring mechanisms, contract terms, and high-powered incentives (including, in the worst case, loss of the franchise) are associated with adherence to those standards (Blair and Lafontaine 2005).

Implications

Fissured employment, drawing on the three pillars of branding, shifting out the provision of work to other organisations, and promulgation and enforcement of standards plays out in a variety of ways. The factors pushing for devolution take different forms given the role that lead companies play in their particular industry structure.

Table 1: Fissured employment in selected industries

Industry	Lead firm/organisation	Lower level entity
Eating and drinking	Brands (franchisors)	Franchisees/outlets
Hotel and motel	Brands (franchisors) Brand operators Independent operators	Hotel/motel properties
Residential construction	Major homebuilders	Contractors/subcontractors
Janitorial services	Building service providers/ Franchisors	Contractors/franchisees
Moving companies/logistics providers	Branded national moving companies	Subcontracted local movers; interstate trucking companies; warehouses
Agricultural products — multiple sectors	Food retailers Major food processors	Farms; Farm labour contractors
Retail food stores (prepared foods)	Major food retailers	Franchised prepared food providers
Home health care services	Major purchasers of home health care services	Health care intermediaries; home health care providers

Employment decisions in the industries in Table 1 have been devolved from major employers to a complex network of smaller employers. Hence, the small contractor trying to win residential carpentry or masonry work in a small geographic area competes against a multitude of other small contractors, which creates intense pressure for it to lower costs, particularly the cost that is most controllable and that dominates its income statement: labour. On the other hand, the parties that set many of the conditions of competition — fast food chains or major hotel brands — operate in environments that afford them a variety of options with which to pursue profitability.

3. The Limits of Traditional Enforcement in a Fissured Landscape

The primary federal law governing labour standards in the US is the *Fair Labor Standards Act* (FLSA) of 1938. The FLSA sets a minimum wage for covered workers, currently set at $7.25 per hour; overtime pay at a rate not less than one and one-half time the regular rate of pay after 40 hours of work in a workweek; and sets standards regarding the employment of younger workers.[4] The standards and associated regulations of the FLSA are enforced by investigators of the Wage and Hour Division (WHD).

Like most workplace agencies, the WHD receives very limited resources relative to the size and scope of US workplaces covered by the FLSA. Budgets for enforcement by WHD have been limited for more than a decade. Annual spending for enforcement by WHD (in real, 1982–84 $US) went from $72 million in 1988 (at the end of the Reagan administration) up to $95 million in 2000 (at the end of the Clinton administration) and back down to $82 million in 2008 (at the close of the George W. Bush administration).[5] Over the same time period, the number of workplaces grew 11 per cent, from 6.94 million establishments in 1998 to 7.71 million in 2007. The number of paid employees rose similarly, by 11.5 per cent, from 108.1 million to 120.6 million (U.S. Department of Commerce 2008).

Long-term budget restrictions have constrained the resources made available to agencies for enforcement. The number of investigators fell 22 per cent from 942 in 1998 to 731 by 2008. WHD investigations declined substantially from 49,521 investigations in 1998, the closing years of the Clinton administration, to 23,848 in 2008 at the end of the Bush administration.

The reduction in investigations compared to the overall growth in establishments meant that the ratio of investigations to establishment declined by about 53 per cent over this period. Not all establishments are covered by the FLSA so this comparison is approximate. However, since it is likely the rate of increase in covered establishments grew at about the same rate as overall establishment growth, the estimated change in the rate seems a reasonable estimate of the decline. As a result, the estimated annual probability of investigation at a workplace in industries with high levels of fissuring is .0027 — that is about 0.3 per cent.[6] Even well-known employers faced little chance of seeing an investigator: the annual likelihood that one of the top 20 fast food restaurants (e.g., McDonald's, Burger King, Subway) received an investigation in recent years is about 0.008 (Ji and Weil 2011). Employers can therefore operate under an expectation that government investigators are simply not a matter of first order concern.

Even if an employer faced an investigation, the consequences for being found in non-compliance were minimal for most US employers over the last decade. Employers who repeatedly or wilfully violate the minimum wage and overtime requirements of the Act may be subjected to civil monetary penalties (CMPs) of up to $1,100 for each violation. As a practical matter, this means in most cases that a prior investigation must have occurred before a CMP can be imposed. Since the majority of employers investigated by WHD are first-time offenders, the number of investigations that assessed CMPs as a percentage of all investigations is extremely low. Less than 2 per cent of all investigations 1998–2008 assessed CMPs. What is more, CMPs were often not assessed even in the case of reinvestigations that found repeat violations. Indeed, among reinvestigations where repeat FLSA violations were detected, CMPs were assessed in only about 43 per cent of cases (Weil 2010). During the period 1998–2008, even in cases where CMPs were assessed, the amounts that employers agreed to pay were frequently substantially reduced from the amount initially set. For all cases concluded by the WHD that had CMPs assessed, the CMPs ultimately determined to be collected by the WHD were only 61 per cent of the total amount originally assessed, from an average of $13,899 to an average of $9,218 (Weil 2010).

Deterrence theory predicts that the likelihood of an investigation together with the cost of penalties for violations affect an employer's assessment of the 'benefits and costs' of complying with a law (Ashenfelter and Smith 1979). The higher the expected penalty relative to the benefits of not complying, the more likely a rational employer will be to comply with the law. The above enforcement estimates suggest that deterrence incentives have been low and declining over the last decade, given the tiny and diminishing probability of investigations and the small monetary penalties associated with violations.

Historically, the WHD measured its impact — and was evaluated by the US Congress and other oversight bodies — by the amount of back wages it recovered for workers. For the years 2003 to 2008, the average back wages recovered for workers per investigation were $15,823.[7] However, this average includes only those investigations in which monetary violations were found. If one includes all investigations concluded in this time period, average back wages found due were $8,838 per investigation. The large difference is explained by the relatively high percentage of investigations where no monetary violations of the FLSA were cited. Between 2003 and 2008, about one-quarter (24.6 per cent) of all investigations found no such violations.

Making sure that workers who have been underpaid — or not paid at all — receive the compensation they are entitled is, of course, important. But defining recovery of back wages as the principal measure of agency success is problematic. An apt analogy would be to occupational health and safety. Although workers' compensation policies provide benefits to workers who have been hurt at the workplace and whose earnings have been impacted, the ultimate objective of health and safety policy is to prevent injuries and fatalities in the workplace, not simply to ensure that those injured are compensated (as important as that objective is). Enforcement that only resolves past noncompliance but does not alter behaviour puts investigators on a hamster wheel: running very fast and working very hard, but not advancing the larger aim of protecting and enhancing the welfare of the workforce. The next section suggests an enforcement strategy more appropriate for protecting employees in today's fissured workplaces.

4. Enforcement Strategy for Fissured Workplaces

The modern employment relationship bears little resemblance to that assumed in core US workplace laws. Improving conditions in the workplaces where the most vulnerable people in the economy work requires navigating the complicated, fissured environment laid out in this essay. Some aspects of the fissured world have desirable aspects. For example, consumers benefit from companies that try to market goods and services that conform to their tastes. As well, there are productivity gains from many aspects of firms focusing on core competencies.

On the other hand, the association of fissuring with poor employment conditions represents a matter of public policy concern that cannot be remedied by traditional enforcement (particularly as government will never be sufficient). Nor will it be addressed by empty appeals to the corporate social responsibility of lead firms. The incentive system of fissured employment creates a landscape that is sloped towards downward pressure on labour costs and non-compliance with basic statutes. Governing a workplace characterised by fissured employment requires a different approach to thinking about the structure of workplace laws and how they are administered. This is a major topic of its own which I address elsewhere (Weil 2008, 2009, 2010). Several major categories of remedies, however, can be identified here.

Reimagining Enforcement

Traditional enforcement strategies assume that enforcement efforts should focus at the level where workplace violations are occurring (Weil 2008). Yet the forces driving noncompliance in many industries arise from the organisations located at higher levels of industry structures. Strategic enforcement should therefore focus on higher-level, seemingly more removed business entities that affect the compliance behaviour 'on the ground' where vulnerable workers are actually found.

Enforcement in a fissured industry requires creating a 'map' of business relationships indicating the different players that drive employer behaviour. The map, in turn, indicates which organisations ultimately must be considered in developing investigation plans. An eating and drinking initiative should, for example, include not only investigations of outlets with violations, but also of other units owned by the particular franchisee. It would also include a systematic analysis of all other investigations of the franchisor (brand) in question to detect the presence of multiple instances of violations at other franchisees. Finally, it could entail contacting the brand itself regarding the results of these investigations if it was clear that significant violations extended beyond the boundaries of any one franchisee or owner group.

Specific outreach could be geared to major brands depending on their prior records of compliance. Major brands in those industries with good employment reputations and a positive record of system-wide compliance could be approached to work with the WHD to be a leader in the industry and help ensure compliance with workplace policies across their systems of franchisees (or similar subordinate businesses). This would require generating clear, replicable criteria about positive employment practices. These could include transparency in human resource policies, wage and benefit policies that exceed industry averages, and objective evidence of worker satisfaction such as turnover levels below industry averages. A cooperative agreement could include a commitment by the brand to cascade information through its company-owned properties and outlets, and to its franchisees, as well as a commitment to review employment practices with franchisees when other franchise standards are being reviewed — with the intention that such efforts could be a model for other progressive brands.

The flip-side would be to target several major brands that had a documented history of systemic violations among its franchisees. These brands could be identified through evaluation of past investigation records. For example, in the fast food sector, Ji and Weil (2011) find significantly higher back wage violations among particular brands, even after statistically holding constant other factors that might also explain noncompliance. In particular, compared to typical outlets of McDonald's (which had the best overall compliance record among the top 20 branded companies studied), Subway, Domino's Pizza, and Popeyes Chicken all had back wages per investigation that were more than $8000 higher.

Once identified, workplace agencies could undertake broad and coordinated investigations in multiple parts of the country and across multiple franchisees, in order to establish the level of system-wide violations, and pursue statutory penalties for those violations. In some industries, they could draw on the 'hot goods' provisions of the FLSA that allows the WHD to embargo goods engaged in interstate commerce where there have been violations of standards at some stage of production process. This has proven a powerful tool where used to alter supply chain behaviour (Leonard 2000; Weil 2005).

Equally important to a 'top-focused' strategy is developing different mechanisms to improve systemic compliance in fissured employment structures. As part of its process of resolving violations, the WHD could negotiate a comprehensive agreement with the lead firm covering all outlets/properties. Such an agreement would entail outreach, education, and monitoring. These types of monitoring arrangements, built on a combination of public enforcement pressure and private monitoring systems, have proven effective methods of improving compliance with minimum wage and overtime standards (Weil and Mallo 2007).

Fissured employment also requires changes in enforcement practices so that they better support an objective of changing employer behaviour rather than focus on recovery of back wages. Because of the inherently limited resources available to stimulate behavioural change, enforcement activity must be thought of in the context of their deterrent effects on lead firms and the network of employers who work with them. It would include the selection of investigation targets, coordination of investigation activities across employers in a fissured industry, use of penalties, publicity surrounding activities, and the choice of legal strategies including settlement agreements. This is not easy. Traditional enforcement — focused on short-term recovery of lost wages and on a particular firm (or more often individual establishment) — entails a very different set of policies and activities than a behaviour-focused approach that seeks more systemic change in the operations of firms and industries. Changing enforcement strategy therefore requires reforming the structure of enforcement.

Harnessing Transparency to Forge a New Balance

An alternative (or complementary) strategy is to use transparency — and hence also public accountability — to act on one of the key components underlying fissuring: brand reputation. Business strategies based on reputation and the maintenance of quality standards have become pervasive. They make good business sense; by creating strong consumer allegiances or by assuring tight quality standards (or the combination of the two), businesses can expand market share and create margins through higher pricing . This is a legitimate aim that is often beneficial to the consumer.

However, these business strategies lead, in a growing number of cases, to great sensitivity to any form of threat to image or disruption of carefully crafted standards. Threats to these systems — private, public, or otherwise — lead to businesses putting in place private systems to pre-empt the loss of reputation among consumers or, more ominously, more onerous public interventions. Whether one looks at Nike's response to accusations that its shoes are being made in sweatshops or at Wal-Mart's responses to any number of labour, environmental, or consumer campaigns, lead businesses are sensitive to reputational attacks.

Targeted transparency — the disclosure of standardised information about organisations regarding their performance to serve a regulatory purpose — has become widespread (Fung, Graham, and Weil 2007). Disclosure of information regarding workplace practices in fissured industries could use the power of transparency to create incentives for the creation of alternative methods to address problems arising in fissured industries.

An interesting example of a public policy revealing variations in the performance of a franchisee is the impact of transparency on restaurant hygiene in Los Angeles County. Jin and Leslie (2009) show that, prior to the imposition of mandated restaurant disclosure, franchisees within a brand had worse hygiene performance than company-owned outlets in the same brand. Ji and Weil (2011) show similar kinds of differences in FLSA compliance between franchisees and company-owned outlets of the top 20 fast food brands in the eating and drinking industry. In 1998, LA Country required restaurants to publicly post grades, based on restaurant hygiene inspections, on their front window. Along with improving overall compliance with hygiene practices and a reduction in restaurant-related hospitalisations, this public disclosure system led to a narrowing and ultimately elimination of these discrepancies between franchisee and company-owned behaviour within brands.

Reputation can therefore be a powerful source of regulatory pressure — even without recourse to direct legal efforts to make lead firms liable. Since investigation records collected by the government are matters of public record, agencies already make such information available. The information from WHD investigations, for example, could be mapped to indicate the relationships of the workplaces that were inspected to the lead companies that had an overarching role in their activities. Reports could be provided both to the lead entity as well as disclosed on an ongoing basis via the Web. The report might also benchmark one brand against other major brands in the same industry, based on similar investigations over the same time period. The results could be linked to other, similar reports on a publicly available web-page regarding the sector-based initiatives. Although the disclosed information may lead some consumers with particular interest in working conditions to avoid companies with poor records, this need not be the only channel through which disclosure operates. If violations are perceived as indicators — or reasons — for compromised food or service quality, disclosure creates incentives for lead firms to change practices in order to protect the brand. This includes preemptive responses, which are frequently the result of mandatory disclosure policies (Fung, Graham and Weil 2007).

Such an effort — particularly if coupled with well targeted enforcement efforts where clear lines of responsibility were illuminated — could engender lead firms to rethink relationships with subordinate companies, from simply providing more information and training to them on responsibilities at one end of the spectrum to creating monitoring systems or perhaps even pulling certain operations back within the lead firm on the other. In the longer term, the use of transparency and strategic enforcement could change the dynamics of how parent organisations relate to lower-level organisations, leading these businesses to take a greater role (and perhaps pay a higher price to subordinates) in assuring adherence to both brand standards and compliance with workplace responsibilities.

Longer Term Policy Responses: Rethinking Employer Responsibility

A fissured employment relationship requires first and foremost serious reconsideration of how we think about responsibility for workplace conditions. There is a large body of legal precedent, rulemaking, and academic debate on the question of joint employment and its interpretation under existing laws (see Ruckelshaus 2008; Rogers 2011; Stone 2004; Zatz 2009). A reexamination of definitions of these questions — particularly under the *Fair Labor Standards Act* which includes a broad definition of 'employ' — is warranted.

The FLSA provides a broad definition of the word 'employ'. Goldstein et al. (1999) argue that the Act's definition, that 'employ includes: "to suffer or permit to work" ', not only covers direct employer-employee relationships (i.e., the master-servant relationship described in the Common Law), but is a broader definition that ' … required only that the business owner have the reasonable ability to know that the work was being performed and the power to prevent it. Thus, work performed as a necessary step in the production of a product was almost always suffered or permitted by the business owner' (Goldstein et al.1999: 984). This broader definition of employer responsibility has been used in the past as the basis for creative policies in agriculture and garment.[8]

But the spread of fissured employment goes beyond past debates about joint employment in part because it reflects market and organisational developments that were unforeseen by the crafters of many federal and state workplace laws. A clear example of this is the common law doctrine of vicarious liability. Vicarious liability refers to liability imposed upon one party because of the actions of another (Arlen and MacLeod 2005). Vicarious liability affects the degree to which, in a principal-agent relationship, the principal attempts to influence behaviour by asserting more direct control on the agents' activities.

This leads to some very complicated and sometimes contradictory incentives. As Arlen and MacLeod (2005: 4) note,

> … far from encouraging organizations to assert control, vicarious liability often discourages organizations from controlling their agents, even when it would be efficient for them to do so. Vicarious liability discourages the efficient exercise of control because organizations which exert control over agents are likely to be deemed 'masters' and thus face liability for their agents' torts.

Reluctance to monitor behaviour of contracted entities can lead to profound workplace problems. For example, in a study regarding the petrochemical industry, Rebitzer (1995) found that a series of major petrochemical explosions and worker fatalities were linked to the use of independent contractors. Major petrochemical companies used these contractors to undertake dangerous 'turnaround' operations (which allow a plant to switch from one type of end product to another). In order to reduce their exposure to liability claims, the petrochemical companies distanced themselves from training and supervision of contractors despite the potentially devastating impact of improperly performed work.

Several recent articles call for addressing the broader question of liability in changing incentives that underlie outsourcing of work. Rogers (2010), building on the hot goods provision of the FLSA and state legislation that emulates it, puts forward a proposal based on a broad expansion of a duty-based test that would expand employer responsibility to end-user firms who fail to exercise due care in assuring that suppliers have complied with labour standards. Glynn (2011) goes a step even further, arguing that the nature of 'disaggregated' employment requires abandoning fine grained arguments over immediate or extended employer liability. He argues (2011: 105), instead, that '… commercial actors would be held strictly liable for wage and hour violations in the production of any goods and services they purchase, sell, or distribute, whether directly or through intermediaries'.

Given the current political climate in Washington, sweeping changes in liability or even more modest changes to definitions of joint employment seem unlikely for the foreseeable future. In the longer term, however, addressing the question of whether companies legally can have it both ways seems fundamental to changing the calculus underlying fissured employment.

Obama Administration Efforts in the First Two Years

In its first two years in office, the Obama administration has pursued strategies in the US Department of Labor and the WHD in particular to address many of the challenges discussed in this article. It signaled its intention to do so through a number of initiatives, four of which bear particular emphasis.

First, it dramatically increased the number of investigators at the Wage and Hour Division by 250 on a base of 730 and increased agency resources for enforcement from $82 million at the end of the Bush administration to $91 million in the first year of the Obama administration. Subsequent budget proposals called for additional increases in agency resources.

Second, as part of its long-standing planning process along with the larger strategic planning process for the Department, it explicitly targeted industries with large concentrations of vulnerable workers, including many of the industries discussed in this article. The justification for this focus is based, in part, on the propensity of those industries, given their organisation to be tilted towards non-compliance (US Department of Labor 2010a). The 2012 budget proposal includes appropriations for additional investigators to work with state governments to address misclassification of employees as independent contractors, a particularly pernicious form of fissuring (US Department of Labor 2010a).

Third, the WHD has emphasised a variety of enforcement policies aimed at enhancing deterrence. This includes an effort to increase use of the penalty authority granted by the FLSA. There has also been an effort to use related policies such as liquidated damages that raise the expected costs of non-compliance. The FLSA provides that employers can be liable for liquidated damages in an amount equal to the back wages. Unlike civil money penalties, liquidated damages are paid directly to the affected employees. As well, the WHD has been reviewing the use of criminal sanctions for egregious violations of the law. The FLSA provides for criminal prosecution for wilful violations. A conviction can result in a fine of not more than $10,000, imprisonment for up to six months, or both. Imprisonment is only upon a second conviction, however. Finally, there has been coordinating of investigations across WHD offices for targeted initiatives in specific industries (US Department of Labor, Wage and Hour Division 2011).

Finally, as a part of its broader 'open government' initiative, the Obama administration has actively encouraged all regulatory agencies to post more of their data regarding ongoing investigations on the Web and to make the information user friendly (Office of Management and Budget 2010). The Department of Labor has been one of the most active departments in providing such information on its Web site and in allowing users to link information across regulatory agencies.[9]

It is too early to gauge the impact of these policies on patterns of compliance in fissured industries. However, another feature of these initiatives is their explicit evaluation in targeted industries through the use of benchmark evaluations of compliance and subsequent surveys to gauge the impact of various interventions (US Department of Labor 2010b).

Changing entrenched regulatory routines is difficult in the best of circumstances (Bardach and Kagan 1982). The very contested political environment facing the Obama administration makes movement towards more aggressive enforcement policies all the more difficult. Nonetheless, the initiatives provide promising steps in terms of changing the orientation of enforcement from a short term focus on back wage recovery to a longer term emphasis on changing the underlying incentives for compliance in targeted industries.

5. Conclusion

The literature on outsourcing and related forms of restructuring focuses almost exclusively on the cost side of the equation, viewing outsourcing as a strategy that seeks to minimise labour costs by moving activities formerly undertaken inside the boundaries of an organisation to labour markets located outside of the organisation. Fissured employment arises from a coordinated strategy that businesses have increasingly chosen to take. This is rooted in both the revenue and cost sides of their income statements. In particular, these strategies use branding and other avenues for securing allegiance by customers to a company's products or services in order to generate, for themselves, more inelastic demand and hence price premiums. The lead company then focuses only on activities related to core functions, while allocating to other entities the production of products or provision of services. Lead firms thereby become the coordinators of other organisations rather than the vertically integrated company that most employment laws assume.

The coherent strategy underlying fissured employment makes it clearer why it is often difficult to alter the decisions made by companies in this regard. Since fissured employment is a reflection of larger integrated strategies, enforcement that responds to the effects of them as if they were only an expression of labour cost avoidance will be unsuccessful. Unwinding the labour cost strategy might be difficult without affecting the revenue side strategy.

On the other hand, by understanding that fissured employment rests on a desire to balance the benefits of branding with the benefits of shifting employment responsibility, a whole range of policy options reveal themselves. Interventions that can affect the tipping point of lead firm decisions may have the best chance to impact the underlying drivers of compliance behaviour and change them in significant and lasting ways.

Notes

1. This article draws on a series of studies examining how industry structures affect the way employers behave and, in particular, their likelihood to comply with the important provisions of the *Fair Labor Standards Act* (FLSA). Research contained in this article arose from the collective work of a Boston University research team over a number of years. I am particularly grateful to Amanda Pyles, Rae Glass, Min Woong Ji, Anne Klieve, Tucker DeVoe, and Claire Gerson. The central findings of this larger research effort are summarised in Weil (2010). The conclusions and recommendations discussed in this article reflect the views of the author and are not meant to be an official or unofficial statement of the policies of the US Department of Labor or its Wage and Hour Division.
2. These estimates are based on comparisons of Osterman's (2008) estimates of the distribution of low-wage workers with the distribution of total employment in 2006. Osterman defines low wage work based on the relation of earnings to the federal poverty level and uses the Current Population Survey (CPS), Outgoing Rotation Group, to make his estimates. The CPS is based on a household survey conducted by the Bureau of the Census for DOL's Bureau of Labor Statistics. See Weil (2009) for a complete discussion of these comparisons.
3. For example in 2009, Burger King reported an operating margin that was 19.6 per cent of total revenue, whereas the operating margin of Carrols Corporation, its main franchisee, was 4.2 per cent (United States SEC Form

10-K: Burger King Holdings, Inc. FY 2009 and Carrols Corporation. FY 2009, available http://www.sec.gov [accessed February 2010].

4. Pub.L. 75-718, ch. 676, 52 Stat. 1060, June 25, 1938, 29 U.S.C. ch.8. The Wage and Hour Division also enforces a number of other laws pertinent to labour standards for agricultural workers, workers employed by private contractors to the government, and wages on federally funded construction projects. We focus only on the FLSA here.
5. Numbers from *Budget of the U.S. Government*, various years, for reported spending for enforcement by the Wage and Hour Division of the Employment Standards Administration (ESA).
6. This is an annual estimate based on investigations conducted over the period 2006–2008 by the Wage and Hour Division, and the number of establishments in those industries for 2006 as reported by the U.S. Bureau of the Census in its publication *County Business Patterns*. The detailed estimates are available from the author.
7. The estimates focus exclusively on compliance with the minimum wage and overtime provisions of the FLSA. It does not include child labour violations or findings under other laws enforced by WHD such as the Migrant Seasonal Protection Act that sets standards for farm workers. Accordingly the estimates cover investigations that have reported FLSA findings (including FLSA findings of 'no violations.'). The cases included in the analysis are those registered from fiscal year 2003 to 2008 and concluded by end of fiscal year 2009. They do not include cases that are resolved over the telephone between the employer and staff of the WHD ('conciliations') which almost always involve a single worker.
8. For the definition of employ, see the *Fair Labor Standards Act* of 1938, Pub. L. No. 718, § 3(d), (e), (g), 52 Star. 1060, 1060 (1938).
9. See, for example, the web-site created for the major workplace regulatory agencies of the US Department of Labor: http://ogesdw.dol.gov/.

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