



T H E   R E V I E W  
O F

*The Institute  
for Economic Freedom*

2000

No. 3

\$5.00  
per copy

Important Issues

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- For a balanced budget
- For the rule of “the law”
- For the privatization of the public corporations
- For a smaller government and lower taxes
- For an efficient justice system
- Against government management of the labor market
- Against a minimum wage
- Against price controls

The Review is published by —

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# Income Redistribution: A Change in Direction

The labour bills that have been tabled by the Government and debated in Parliament include some needed refinements of existing labour law. But more importantly they go beyond. They implement entirely new control regimes that include a costly national labour contract and an occupational health and safety program.

To put this into perspective this article will first discuss economic growth and the changing face of socialism.

## *Economic growth*

Economists like to talk about two things...How a country spends its money and how much there is to spend. Or...How is the economic pie divided and how does it grow.

In this regard the last half-century created an analytical field day. There was the recovery of Japan and Germany from total devastation, the economic emergence of the Pacific Rim countries, the unanticipated sustained growth of the United States and both technological and structural change that can only be described as massive. At the other extreme there was the collapse of the Soviet Union and the Communist Bloc. Here the totalitarian centrally planned and centrally controlled economy proved to be a catastrophic failure. All of this has been thoroughly analyzed. Economists know a great deal about what works and what does not.

A good illustration is a March 2000 study "Growth is Good for the Poor" by David Dollar and Aart Kraay of the World Bank. They studied the link between income of the poor, the bottom fifth of the population, and overall income in 80 countries over 40 years. They found that --

- The income of the poor rises one-for-one with overall growth...a one-percent change in overall growth is matched by a one-percent change in the income of the poor.
- The poverty-growth relationship does not change
- The income of the poor does not fall more rapidly than overall income during economic crisis.
- The effect of growth on the income of the poor is no different in poor countries than in rich ones.
- Policy-induced growth is as good for the poor as it is for the overall economy.

The study confirmed most of what had been previously identified by economists. There is a core set of factors promoting growth... namely...macro stability, fiscal discipline, openness to trade and the rule of law.

The point is --

**If you are interested in the poor, you should know that economic growth really counts.**



## *The changing face of socialism.*

While Russia and the Eastern Bloc were disintegrating as a result of inefficient economic management, the European Union founded in 1957 was moving in the opposite direction. Although it took time, the business/labour partnering solution that developed in some countries was extended to the rest of Europe in the 1990s as were the mandated labour benefits and regulations. The only temporary obstacles to this process were the Margaret Thatcher and John Major governments of Great Britain.

**Classical economic theory concludes that minimum wage legislation, mandated employment terms and health and safety regulations increase unemployment.**

This appears, in fact, to be the case in Western Europe. For instance, measuring employment by using the number of people employed as a percent of the total population (the Employment-Population Ratio), male employment declined materially over a 15-year period in France, Germany and Italy. The male employment ratio dropped from 4 to 5 whole percentage points for men of ages 25 to 54 and from 5 to 17 whole percentage points for men of ages 55 to 64.

In evaluating the legislation, the employment results and its probable causes, two prominent English economists conclude that –

**“The net effect of employment protection and analogous rules on labour demand and supply does seem to be lower employment, greater and longer unemployment for some, and, implicitly, a decline in the speed with which labour relocates from declining**

to growing sectors of the economy. To this extent, the favourable employment and unemployment development in the U.S. would appear to owe more than a little to its lower degree of employment protection."

The point is –

European style labour legislation lowers employment and diminishes growth.

### *The FNM's growth record.*

The Bahamas has had 6-years of prosperity...and particularly in the last 3-years, economic growth adjusted for prices greatly exceeded the population growth. This record of growth contrasts sharply with the economic stagnation that characterized the prior decade.

The FNM Government set a course of improved government efficiency, infrastructure investment and the encouragement of foreign investment. Getting Sun International to build Atlantis was the key and this triggered other investments in tourism, banking and real estate.

But their success went beyond this. The FNM Government attracted two entirely new industries in Freeport, ocean freight transshipment and cruise ship repair. In this regard the Bahamas was a smaller scaled version of Ireland in the 1960s when that country induced the leaders of the computer age to invest in the Irish Republic. This fueled their spectacular growth.

The point is –

**The Bahamas got on the road to becoming the most prosperous Black Country of modern times.**

### ***The labour bills.***

So it may come as a surprise to the reader that the Prime Minister should make labour market regulation what some describe as his "legacy". His logic, however, is very clear. He stated in Parliament that –

- **Business has benefited from the boom, and**
- **"Now is the time for the worker to get his share of those benefits".**

He hopes to accomplish this with the Minimum Wages Act and the Employment Act that together constitute a *de facto* National Labour Contract.

Let's pause for a moment.

Few people are aware of the Dollar and Kraay study. Few may know that policy-induced growth is good for the poor. But every businessman who hires Bahamian labour knows that the worker has shared in the good times. Wages and fringe benefits are up and on-the-job training improved. There is full employment.

One can speculate on the motivation for making this policy decision. But it is clear that with the help of the International Labour Organization the PM has tabled a legislative program that closely follows that developed in Continental Europe. And...that program has its origins in Article 118 of the Treaty

of Rome that created the European Union. It called for close cooperation between member states in "such matters as labour legislation and working conditions, social security, health and safety, employment, and collective bargaining."

It is also clear that the National Labour Contract, as we now know it, will raise labour costs substantially. The change in working hours alone for firms that need five and one-half and six-day workweeks will raise their direct labour costs 17 to 27 per cent. This does not include the increased cost of maternity leave, sick leave, vacation pay, related clerical work and the reduced managerial efficiency caused by the greater complexity in managing labour.

The point is --

**With the proposed labour bills the FNM Government is changing policies. It is concentrating on dividing up the pie rather than growing it.**

The conclusion is --

**This will mean less employment and reduced economic growth.**

## **Misrepresentations in Parliament**

The summer of 2000 could be the beginning of the Bahamian "year of discontent". Old laws relative to two major areas of the economy...labour and the financial services...are being



changed. In the first case there is speculation on the potential downsizing of the banking sector, and in the latter there is uncertainty over the impact of the proposed labour bills.

A "national labour contract", falsely described as minimum standards, includes a minimum wage, shorter workweeks and numerous other mandates altering current employment practices. These will increase labour costs and lead to higher prices in the hotel, construction and other industries and /or reduced employment.

The confusion and uncertainty is not helped by misinformation contained in the parliamentary debates. Regrettably Mr. Tommy Turnquest used a flawed study in his support of the minimum wage. He cited a study by two economists, David Card and Alan Krueger, that examined the effects of a 1992 increase in New Jersey's minimum wage. It showed that a 19 percent increase in the minimum allegedly was accompanied by a rise in employment.

This study has been thoroughly discredited by numerous researchers including Nobel Laureate Gary Becker who stated "the Card/Krueger studies are flawed and cannot justify going against the accumulated evidence from many past and present studies that find sizable negative effects of high minimums on employment." This forced Alan Krueger to state "my comment should not be interpreted as support for the position that increasing the minimum wage is sound public policy."

In the same debate, misrepresentation of facts were made when Mr. Turnquest used National Insurance Board data to state that 22 percent of the 110,072 enrollees are paying National Insurance on wages that are "currently below the proposed minimum wage". He neglected to point out that the

figures quoted do not take into account commissions, bonuses, gratuities and other income not categorized as a "wage". If you wish to make a false impression that a large percentage of the population is living on borderline income, then you ignore numbers that do not support your argument. This appears to be what Mr. Turnquest was doing.

The risk of an economic downturn, the result of blacklisting and labour legislation, is real. It is ironic that Parliament, where laws are made, should be the venue for deception that undermines trust and thereby the rule of law.

## **The Unemployment Bill Raises the Cost of Business**

The wage and benefits portions of the proposed Minimum Wages Act and the Employment Act represent a *de facto* National Labour Contract. The Government has been negotiating this contract in separate meetings with business and labour. The issues are complex and the potential results are costly...they will produce significant business adjustments.

Each element sounds simple but becomes complex when applied to the wide variety of work and compensation systems that have developed over time in the market for labour services.

### ***Paid lunches and hours of base pay.***

The paid lunch and hours of work before the payment of overtime clearly show the cost impact. Some employers

provide a 30-minute lunch break with a free meal while others do not pay for the meal. Still others provide for a 60-minute break.

The payment of overtime also varies. Employees paid on a commission (a percent of sales) or piece rate (a fixed amount for a specific task) get no overtime. In the labour market today overtime can begin after 40, 44 or 48 hours depending on the "market practice". These relationships have evolved naturally over time to provide rewards and incentives.

A good illustration is the mandated reduction in the base workweek from 48-hours to 44 and to 40 and the paid 30-minute lunch period. The following are two examples of labour contracts in two actual companies:

### *Conclusions.*

This construction industry presently uses an 8-hour workday and a 6-day workweek in most but not all of its contracts. A worker is paid only for the hours actually worked and he receives no pay for 30-minute lunch periods.

The following shows the two-stage impact of the proposed legislation on a single employer and his employee as the company moves from the present 48-hour week to a 44-hour and then to a 40-hour week with paid 30-minute lunch breaks.

The example assumes an hourly pay rate of \$10.00 and overtime pay at \$20.00. The Employment Bill tabled in Parliament calls for Double Time as Overtime Pay. It is believed that the Government has agreed to Time and One Half, but this change is not in the presently available "red-lined" version of the Bill.

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	Formula	Weekly Cost	% Change
<b>Present:</b>			
Hours at –			
Base Rate	48 hours @ \$10/hr	\$480.00	0.0%
Overtime Rate	0 hours 0.0		
Cost of Lunches	6 lunches 0.0		
<b>Year 2000 44-hour mandate:</b>			
Hours at –			
Base Rate	44 hours @ \$10/hr	\$440.00	
Overtime	4 hours @ \$20.00 /hr	80.00	
Cost of Lunches	6 lunches @ \$20/hr	60.00	
Total Compensation		\$580.00	+20.8%
<b>Year 2001 40-hour mandate:</b>			
Hours at –			
Base rate	40 hours @ \$10/hr	\$400.00	
Overtime	8 hours @ \$20.00/hr	160.00	
Cost of Lunches	6 lunches @ \$20/hr	60.00	
Total Compensation		\$620.00	+29.2%

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Now if Overtime is set at "Time and One Half" in place of "Double Time", then the increase in "Total Compensation" would be lower...+13.5% instead of +20.8% for the 44-Hour Mandate and +17.5% instead of +29.2% for the 40-Hour Mandate.



## ***Retail.***

This is a company with several stores that has tailored different compensation "packages" for different classes of employees. The following are the calculations for one category of employee.

This group works an 8-hour day and 5-1/2-day week without paid lunch periods. A typical hourly wage is \$6.00 per hour for a sales person with limited experience after 6-months of employment. A table like that on the opposite page would show that –

- Immediately after the bill is passed, Year 2000, the "Cost of Lunches" would raise the "Total Compensation" by +11.4%.
- In the second year, Year 2001, the half-day of Saturday work would be at \$12.00 rather than \$6.00. The "Total Compensation" now would be up +20.5%.

As in the Construction Industry example these increases would be lower if the Overtime Pay is at Time and One-Half. In this case the increases would be +8.5% and +13.1% respectively.

## ***Conclusions.***

**These are just two typical employment contracts. But... the indications are that the increased costs are substantial no matter which overtime provision ends up in the Bill.**

It will trigger changes in the workers employed and the services provided to the customer. The only situation where there will be no effect on employment and company profits is where the

company has a market monopoly. Here the higher costs can be passed on to the customer in higher prices. An example of this is Bahamas Electricity Corporation. Where there is competition the results will be a combination of reduced employment, changed product/services offerings, higher prices and reduced sales.

This analysis does not describe either the piece rate or sales commission systems. Nor does it consider the impact of other features of the National Labour Contract. Those include longer sick and maternity leaves and increased vacations, redundancy and separation payments. Once again only those companies with a market monopoly will escape the employment and profit consequences of this legislation.

### *Note:*

Please refer to the Institute's Website [www.iefbahamas.org](http://www.iefbahamas.org) for a more detailed and accurate determination of these costs. This reference includes easy-to-use Excel spreadsheets.

## **Truthfulness In the Workforce**

The Employment Act dated May 2000 is an updated version of the proposed Minimum Standards Act circulated in January 2000. It has one addition that every businessman doing or contemplating doing business in the Bahamas is likely to find objectionable. That relates to finger printing, the use of lie detectors and any form of screening or testing.

The Act states that no employer shall require --

- "Any person, as a requirement for employment, to furnish a set of his finger prints or take a lie detector test", nor shall he require
- "Any employee to take any form of mechanical, electrical or computer testing or screening" to establish either "his identity or truthfulness."

The businessman will be outlawed from using effective techniques to determine the honesty of an actual or potential employee. Anyone so doing is subject to a fine of \$5,000.

Most business managers consider this outrageous because theft of company assets is such a large problem. Pilferage in the Bahamian retail trade, for instance, is five times that in the United States. The financial community will not discuss their problems in this regard...but...the problem exists. For example, several years ago a Bahamian bank officer...certainly not one of society's downtrodden...apparently stole \$750,000 from the bank's Bahamian employee pension fund. To this day both the criminal and civil cases remain stalled in the legal system.

**How can Bahamian business compete in the global market place if the law of the land protects thieves? This is the question that the politicians should address.**

And there is a profound irony in this because the casinos are exempted from these prohibitions because of Part XI Section 73 of the Lotteries and Gaming Act. These state that --

- Any person seeking an employment permit from the Gaming Board and who makes a statement that is false is subject a fine of not more than \$600, and
- All applicants for work in the casinos must furnish fingerprints.

This just compounds the businessman's puzzlement and/or outrage.

## Health and Safety & The Rule of Law

The proposed Health and Safety at Work Act of May 2000 is intended to secure the health and safety of workers in the workplace. Such an objective seems on the surface to be as correct for the Bahamas as are boiled fish for breakfast and peas and rice for supper. However, this is not quite so since there is a short-term lower cost alternative.

### *The Act.*

The Act will allow the Minister of Labour to appoint a safety representative from a company's employees and will require the employer to consult with that employee on matters of health and safety. Furthermore, it provides for an Inspector Corps with a complete array of powers plus the ability to issue "Improvement" and "Prohibition" notices under penalty of "summary conviction to a fine of five thousand dollars."

These provisions must be evaluated as they stand and also within the context of certain realities.



1. The new bureaucracy will write and enforce detailed standards on how business is conducted. This is costly and complex and comes at a time when the more advanced countries of the world are beginning to appreciate the cost of these regulations. Furthermore, it will diminish the competitive position of the Bahamas in the Global Economy.
2. The Act fosters a needless growth of expenditures at a time when the government appears to be bringing the budget into fiscal balance.
3. There is no reason to believe that the administration of health and safety will be effective. There is an overwhelming lack of managerial and technical skills in the country. In addition, the Government has great difficulty in managing efficiently since politics dominates all decisions rather than business or economic considerations.
4. Private business has a natural self-interest in the health and safety of its employees. A good example of the responsiveness of business to the reality of the workplace is in the area of on-the-job training. A recent Bahamian business survey shows that on-job-training expenditures have risen over 70% during the past 5-years without government intervention of any kind.
5. Such legislation creates corruption opportunities. In practice the proliferation of laws and regulations results in an inevitable growth in "rent taking" by public officials. In countries as India, Italy and Venezuela, for instance, the record is very clear...excessive laws and regulations corrupt

the governmental function and ultimately produce economic stagnation and political instability.

### ***The rule of law.***

At this stage in its economic development the Bahamas would be better served by a major reform of the justice system. Such reform must include major investments in staff, facilities, procedures and caseload management. In the workplace such a reform program would give workers a genuine opportunity to sue for damages suffered as a result of any health and safety deficiencies in the workplace.

One of the truly valuable contributions of economists over the past fifty years has been research on sustained economic growth. Virtually all studies identify an efficient and impartial justice system...the rule of law...as one of the critical elements that sustains economic growth.

In fact, an inefficient politicized justice system is a hallmark of a "third world banana republic" and the blacklisting crisis that the country now faces is the direct result of its existence in the Bahamas. In this case the legal system frustrated and blocked legitimate proceedings under the Mutual Legal Assistance Treaty with the U. S. causing the strong U.S. initiative.

For the economic health of the Bahamas the Health and Safety at Work Act should be quietly withdrawn... and...the FNM Government should make the strategic decision to focus its resources on developing a modern efficient impartial legal system. This would naturally complement the development of a "world class" law school and secure the country's position in the world as a good place to do business.

## The Rule of Law

"The idea that there is no limit to the powers of the legislator is in part a result of popular sovereignty and democratic government. It has been strengthened by the belief that, so long as all actions of the state are duly authorized by legislation, the Rule of Law will be preserved. But this is completely to misconceive the meaning of the Rule of Law.

"The Rule of Law...implies limits to the scope of legislation. It restricts it to the kind of general rules known as formal law and excludes legislation either directly aimed at particular people or at enabling anybody to use the coercive power of the state for the purpose of such discrimination."

F. A. Hayek  
The Road to Serfdom  
University of Chicago Press  
Pages 90 and 92

## *Highlights*

Classical economic theory concludes that minimum wage legislation, mandated employment terms and health and safety regulations increase unemployment.

With the proposed labour bills the FNM Government is changing policies. It is concentrating on dividing up the pie rather than growing it. This will mean less employment and reduced economic growth.

No employer shall require "any employee to take any form of mechanical, electrical or computer testing or screening" to establish either "his identity or truthfulness." How can Bahamian business compete in the global market place if the law of the land protects thieves?

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