Contract and Organisation:
Legal Analysis in the Light of Economic and Social Theory

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Introduction

What does the law learn when it is confronted with its own consequences? Is it this feedback loop from legal norms to social consequence to legal norms which probably constitutes the most important contribution of social science thinking to legal argument? There is a tradition in legal methodology, the so-called teleological approach, which is very similar to this kind of argument. Legal norms are interpreted in the light of their purpose and one important consideration in the teleological interpretation is the question of whether the purpose has been actually reached or not. However, the teleological methodology is still an imprecise legal device. It relies on the legal norm to the legal set of purposes, but in the legislature's good. In the judge's reformation of the legal purpose, it cannot simply unite extra-legal modes of analysis and feeds them back into the legal argument. The basic argument has the following elements: (1) What is the basic legislative or judicial social purpose of the norm? What are the intended social effects on social behavior and social structure which are expected to follow the enactment and implementation of the legal norm? (2) To what degree have these goals been reached in the social reality? What are the side effects, what are the unintended consequences of a legal norm in social reality? (3) How does one re-formulate the legal norm in the light of its social consequences?

For this type of legal argument, there are no limits to academic specialty of the information involved. Social science information in the broadest sense is needed, if it is sociological, economic or psychological nature. However, there is a special branch in legal sociology developing which could be in the position to develop common standards of argumentation: "Legal Effect Research" (Rechtswirkungenforschung) is concerned with the question what difference it makes if social facts are regarded by formal legal norms. This is an autonomous field of legal sociology. It becomes part of a broader sociological independence, if the selection of criteria for this type of research is guided by legal regulatory intentions and if the results of that research are used for a reformulation of legal norms.
Empirical findings and theoretical insights are likewise used to evaluate this kind of legal reasoning. In the following I am going to use empirical materials as well as theoretical construction to show how social science research on social effects of legal regulation can inform the law about what it is doing. I will concentrate on one of the many requirements to change the character of organizations by means of law, the example of industrial democracy.

There are many roads to "Industrial Democracy." A lively academic discussion in which a number of experiments reveal a wide variety of approaches: Via work place participation, work councils, board representation, representation of public interest of the firm, collective bargaining systems, workers' self-management, socialization of empires. One road, which the German labor movement has chosen, leads via labor legislation and the legal process (e.g. CARMÖ and Steurer 1940). Guided by national law and experience I want to follow the German road to Industrial Democracy and to describe some of the promising kind it leads to as well as the darker area it surpasses, its potential and limits, its direction, its traps, its dooms. If we are interested in successful road construction works, what lessons can we learn from the peculiar German experience? The German road is peculiar, even extreme, in two respects. First, it does not lead through the somewhat mildly lower levels of workplace participation, but rather finds its way through the lofty heights of corporate hierarchies: work councils at the middle echelon as counterweight to management authority and representation of workers' interest at the top level of the corporation. Secondly, on this road we do not meet a spontaneous, eruptive, anarchic, unstructured flow of social and political movements but a highly disciplined traffic governed by complicated traffic rules and many, many traffic signs. A high degree of jurisdiction of labor interest representatives is the most conspicuous trait of German co-determination. Thus, one should attempt to exploit the German experience and ask the following questions: What are the actual social functions of legal co-determination as opposed to official goals and political ideologies? What is the actual role of the law in strengthening participation, power equalization and industrial democracy?

I have two tentative answers to those questions which I will elaborate in this paper. The material I rely on is some empirical evidence about the factual consequences of co-determination and about some pieces of theory on interorganizational communication in industrial relations.

1. Social functions: The official debate, co-determination contributes to "economic democracy" through workers' participation is an excellent example for political rhetoric. The main function of co-determination lies rather in individual reinforcement of their political status as economic citizens. Rather, we have to look for relevant effects on the interorganizational and interorganizational level. Co-determination changes interorganizational power relations resulting in a new form of co-management among capital and union elites. In addition, co-determination changes interorganizational relations since it contributes to a specific form of political ("own corporation") organization in the relation between the economic and the political system.
The findings are contradictory and ambivalent, however, and together they suggest a rather skeptical assessment.

These findings show the following picture: In general, workers have a rather positive attitude towards co-determination. However, if it comes to details, the attitude becomes more ambiguous. As the relationship between co-determination and satisfaction is concerned, Tannenbaum et al. found that in countries where workers' representatives had more influence, the workers did not have more satisfaction, and vice versa (Tannenbaum 1974). In addition, the attitude of workers as to the effects of the decisions is positive. In a recent cross-national comparison, less than fifty percent of workers and supervisors in each country showed a positive evaluation of the functioning of representative bodies (IDB 1982: VII, 15). Rather than to democratize the worker's situation, the representative bodies are perceived to function as part of the control structure of the organization (IDB 1982: VII, 14). In more detail, it turned out that rank and file employees do not know much about the work of their representatives. Their attitude to personal involvement is lack of interest, indifference or even apathy. They assess the influence of the representative bodies as rather marginal. Streeck (1984) concludes as follows: "Workers under patrii co-determination were as much subject to hierarchical control as workers everywhere else, the organization of their work continued to be determined by impersonal mechanisms beyond their influence and understanding, and their attitude toward their work did not differ in any perceptible way from that of workers in other industries".

If we contrast these somewhat depressing findings to the high aspirations connected with co-determination, we have to admit that in this respect, political goals and actual social function do not coincide. Due to the large social distance between individual interaction in the workplace and organizational decision making in the corporate hierarchy, co-determination through worker representatives in corporate bodies is clearly not a suited means to achieve the goals of participatory democracy. There are other means which may have some success on the individual level: job enlargement, autonomous working groups, rotation systems, and other ways of direct workplace democracy. In vain, however, we will look for democratizing effects of co-determination on this level. Its main social function should instead be identified either on the intra-organizational and intra-organizational levels. Thus, co-determination law should give up this orientation toward a non-rational purpose and concentrate its regulatory power on the other.

2. Organizational Effects

Co-determination law plays a much more important role in the complicated power relations of intra-organizational decision making. Co-determination law seems to change considerably the distribution of power and influence, the goal structure of the organizations and the structure of the capital labor conflict.

2.1 Power and Influence

At first sight, co-determination law does not seem to matter very much. Although complicated rules, procedures, competences and conflict resolution bodies are created these institutionalized patterns are only rarely used. Open, formalized conflict with decision by vote is only seldom. For example, Leg
demeyer (1973: 188) reports that most of the supervisory board decisions were taken unanimously. And the Bischendorf report (1992:13) contains data according to which only very rarely the "neutral" member of the board had to give the decisive vote. Thus, it might seem that the new legal machinery is not accepted and utilized for the labor interests. Does law only have symbolic functions?

Looking closer to the real decision making processes, the picture changes drastically. Indeed, open conflict is seldom, the legal machinery for conflict resolution is only used as a last resort. However, what happens is a change of informal negotiating processes. And there we can identify the most important albeit indirect effect of the law. The formula is "bargaining in the shadow of the law" (Minkovits and Konrath 1979). Management and labor representatives deal with each other by anticipating the power distribution in formal conflicts. The legal rules of co-determination have changed these power relations drastically. The increase of formal decision making power from practically all to party positions for the workers influences considerably the actual day-to-day behavior of management and labor. It does so not directly by the new procedures and rules, but by the changed formal positions which are anticipated in the ongoing negotiations. Matters of political conflict are discussed in informal meetings between labor and management before the formal board meeting takes place. And many issues even do not reach that stage of informal negotiation since management tries to adapt to anticipated labor positions in order to avoid conflict (Legdemeyer, 1973: 126).

Finally, labor representatives are often consulted even if legally it is not required (Streeck, 1984:25).

In a recent empirical study the direct and indirect effects of law in changing the actual power and influence structure has been scrutinized in a comparative way (IDB, 1982:VI). Economic organizations through all the countries are highly hierarchical. Co-determination does not abolish the hierarchy, but it modifies the power-distribution in a considerable way. It does so directly by granting a legal "meta-power" through the re-distribution of control rights and, indirectly by restricting the power of competing groups. Granting legal power to representatives bodies does not only increase their influence, but diminishes at the same time the power of top management.

It seems that the indirect effects of co-determination law (changes in negotiation power) are much more important than the direct effects (installation of a conflict resolution system). This impression is strengthened if one looks to the effects which co-determination had on the union's position as a whole. Streeck (1984:9) has argued that co-determination law has an indirect effect of strengthen- ing the positions of unions the respective industries in regard to direct aspects (1) Union control over the personnel department made it possible to recruit union members in a way very similar to a closed shop. As a consequence
the density ratio of union membership had increased drastically in the coal and steel industry. (2) The presence of a full-time union official on the supervisory board strengthened the collective voice of the workers and made the workforce more unified. (3) Under conditions of parity co-determination, there occurred a functional division of the works council along the "united" union. These indications of a relative improvement of the unions' bargaining position through low wages suggest that one indeed should concentrate the attention on indirect effects of co-determination law.

Moreover, if we attempt to compare and evaluate the relative influence of legal norms on power distribution in opposition to structural and organizational variables, the IWE-nahly configurations form a rather surprising result. Social scientists occupied with worker participation had to expect a rather minimal influence of formal legal norms. For example, personal variables like high

education of the workers are currently treated as crucial for organizational participation (E. Isak, 1989, 127). Moreover, technology and organizational structure are seen as the main predictors for power distribution in the organization (Even 1987). Others stress organizational factors like the size of the organization (Rino and Schoenheier 1973). Quite in contrast to these expectations, the authors of IWE conclude "that institutional norms relating to medium term decisions seems to be the most important instrument of power equalization and of further democratization of those workplaces...". All or the other contextual variables - personal attributes of employers (skill, education, qualifica-

tion), technological contingencies (automation, complexity), organizational contingencies (diversification, decentralization, conflict, economic and environmental contingencies - tend to undermine the much less influence on power distribution within the organization. It seems the law has only two serious competences in changing effectively the power structures: "mobilization" of workers; their active participation in unions, labor actions and workers represent-

ative bodies and, second, strong outside influence within supervisory boards. The policy lesson to be learned is a more "voluntarist" approach to industrial democracy. It seems to be conditioned much more by human action - law, mobilization, outside influence - than by exogenous technological, structural and economic conditions.

2.2 Goal structure

Quite apart from those effects on power structures, co-determination law has a different function which we can call the "internalization of external conflict" (Todtling, 1978/82). Without co-determination, workers' interests are mainly channeled through labor market structures and inter-organizational negotia-
tions. In the collective bargaining systems, labor-management conflicts are a matter of external relations. Similar to co-determination, the worker's decisions and conflict resolutions to inter-organizational boards with labor representation, the industrial conflict becomes internally unified into the economic organiza-
tion itself. This changes the medium of communication: The collective bargain-
ing system works via economic market mechanisms - in Hirschman's termin-

ology via "exit" mechanisms - while co-determination leads to a politicization of the conflict, to the dominance of "voice" mechanisms. Moreover, the goal structure of the organization changes considerably. Workers' interests like job security, control of work, cohering of rationalization are no longer exclusive cost factors which must be minimized but a legitimate goal for the inter-

organizational decision process itself (Luhmann 1986/84a). This change in the goal structure leads to the partial internalization of the labor market into the organization and by its transformation into organizational manpower planning and the creation of internal labor markets in large organization. Since labor shortages arrived at a more prominent place in the goal hierarchy, management was put under constraints to develop mechanisms that would reduce the incursion of labor to the fluctuations of the external labor market. Streck (1982/83) argues that in this respect co-determination has not only created a problem for enterprises but also offered a solution. The new solutions, manpower planning and internal labor market were possible since co-determination "has provided the organizational instruments to cope with such rigidity without major losses in efficiency" (Streck, 1984).

2.3 Capital-Labor Conflict

Thus, co-determination has changed the conditions of the labor-capital conflict. The great ideological battle on societal issues is transformed into inter-class struggles which have to be dealt with in a rather trivial basis of day-to-day arrangements. And it creates a conflict solving mechanism which a German scholar has labeled as a "social ethics of modern social systems" ("Gerecht-
twicklung der sozialen Systeme", Litter 1982/87): the "dual loyalty" of interest representatives. While many empirical studies analyze the amount of frustration and alienation on the side of work councils, labor board representa-
tives and labor directors, who suffer psychologically from the role tensions they are exposed to, one should not forget the other side of the coin. It is an old sociological insight that inter-role conflictions can serve as a link between highly divergent social interests (e.g. Streeker, 1949; Debendorf 1986). The structural conflict is "personalized", is transformed into a mundane personal problem and the dual loyalties compel the individual to search for - socially and psychologically - bearable solutions, compromises and temporary arrangements. Thus, we can generalize about the role the law is playing in this respect. The law which has created this conflict situation can, in a way ease the role tensions without abolishing them. By granting formal power to the representatives it legitimizes the ambiguous position he occupies and his desire to "balance-

amongst interests".

The effects of co-determination law in this respect are, however, even more pervasive. They are not confined to change the conditions of conflict from antagonistic confrontation to stabilized compromise, they change the very structure of management. In the long run, the role of labor is not limited to the role of a pressure group influencing management by negotiations and threatening with sanctions backed by social power. Rather, the very combination of the
work council system, the supervisory board representation and the collective
bargaining system leads to mutually reinforcing effects and results in a kind of
co-management between capital and labor. Tegtmeier (1993:152) concludes
that the main consequence of co-determination is a “joint and integrated decision-
making process”. The effect of the law is for capital and for labor a reciprocal
incorporation of interests with the objective of a “mutual incorporation
of capital and labor by which labor internalizes the interests of capital just
as capital internalizes those of labor, with the result that works council and
management become subsystems of an integrated, internally differentiated sys-
tem of industrial government which increasingly ‘oversets’ the traditionally
dualistic factory-based system of industrial relations’.

3. Economic and Societal Effects

If we change now the system from reference from the organization to the
economic system, in its interaction with other functional subsystems – especially poli-
cy and law – we realize that co-determination stands in strong contrast to principles
of economic rationality. Co-determination relies on voting procedures, on
prevailing policies, on bureaucratic hierarchy, on negotiating and power balancing
mechanisms, which are not compatible with economic principles of profit
maximization, with market structures and with money as the economic communi-
cation mechanism.

3.1. Contraaction to the Prevaling Orientation

This politicization of the economy through law is the conspicuous target for
fundamental critique. Either, co-determination is supposed to destroy effectively
economic rationality (Pongs 1976) or co-determination is said to be one of the
last tricks of capitalism: corruption of labor through participative (Hippke 1989).
Both positions are met by the reasoning from practical aspects of co-determination. Indeed co-determination firmly contradicts pure
economic principles. Both in the case of the state and with the results.
Indeed, co-determination changes the attitude of labor, from ‘costliness’
strategies to “cooperative” ones. Again, the question is only to what degree and with
what effects, but positions in a way render ‘real use’ to one’s interests and
observation of “market corruption” or “labor corruption”. However, they fail to
solve the potential and limits of those phenomema by a closer analysis of the
relation between market and organization.

If the relations between market and organization are defined by conditions of
perfect competition, co-determination does not matter. Under perfect competi-
tion the concepts of the market on the organization are so strong that there is
only one best solution, without the least influence of market imperfections –
competition, oligopolization – those constraints become weaker and manage-
ment gains a considerable discretionary power in its decisions (eg. Lindholm, 1979:152).
And precisely this discretionary power is the main target of co-
determination. Again, it is precisely the range of discretion which gives a limited
justification to the liberal and to the leftist critique. Economic rationality is
impaired, however not by co-determination, but by the very existence of
management discretion which is due to market imperfections. On the other hand,
labor gets “corrupted” (to use as labor representants have been to economic
constraints, but this is only true for decisions outside the room of discretion.
Thus the management has gained discretionary power, labor with a strong
formalized position within the enterprise possesses the power to make “non-
corrupted” demands for the workers interest. From the perspective of organisa-
tion’s non-market relations it becomes clear that a description co-determination as a
total politicisation of the economy is just as inadequate as describing it in terms of
cooperation of authentic labor interests. The crucial point is paternity.
Economic rationality remains the prevailing principle, however it is modified to
a certain degree by counteracting institutions which work as “built-in” con-
tractions to the prevailing orientation (Luhmann 1966:45).

3.2 Neo-Corporatist Coordination Mechanism

What then is the social function of co-determination if it represents a built in
contradiction to economic rationality? It is our thesis that function of co-
determination can be understood only in terms of differentiation and integra-
tion. Co-determination serves as one of the main integrative devices in a society which
is characterized by extreme functional differentiation. The most conspicuous
trait of differentiation processes is the high degree of functional autonomy the
economic system has gained. This gives rise to the peculiar problem: How can the
societal integration of the economy be carried out without losing the advantages
of high differentiation. Even more: Do we have to conceive the relation between
differentiation and integration as a zero-sum game, where winning for one part
means losing for the other? Or is there a possibility of integrative devices which
not only maintain a given degree of differentiation but which support even
increasing differentiation? (Billig 1978:228; 1983).

The interesting point about co-determination is in its indirect control
methods as opposed to interventionist direct control. It is the specificity of co-
determination to establish such a “co-determination law that the state does not interfere with external controls, for
example with regulations of the market structure, with instruments of global
capitalism, with legalization of corporate behavior, or with direct politicisation
of economic action. Rather it relies on indirect means of control, as an external
totalization of internal self-regulation. The crucial point is that state law changes
the internal structure of the corporation by redistributing property again,
however by maintaining the economic principles of corporate autonomy and
decentralized coordination. In this respect, co-determination represents one
possible answer in how to integrate economic large scale organization politically
without sublating them to direct state control which would end in different
tendencies.

Viewed in this perspective, co-determination has its main function clearly
beneath the level of individual participation, but on the intra-organizational
level of labor-management-relations, but on the societal level as a re-integrating
mechanism. It is not only a peculiar element of company law, but forms part of a whole - a whole of coordination mechanisms. Co-determination is the lowest level in a system of coordination mechanisms for which political scientists have coined the term "neo-corporatist syndrome" (Schmitter, 1974; Alemann 1984). This is a form of political organization in which organized business and organized labor are directly involved in state decisions and at the same time serve as implementation mechanisms for governments' economic policies.

New corporate arrangements should clearly be distinguished from "state corporation" on the one side and "interest group pluralism" on the other side. In a Brinley's term, pluripluralism can be defined as a system of interest mediation in which the constituent units are organized in an unspecified number of multiple, voluntary, competitive, hierarchically ordered and self-determined to type or scope of interest" categories that are not specifically licensed, recognized or otherwise controlled in leadership election or interest articulation by the state and do not exercise a monopoly of representational activity within their respective categories. Corporatism can be defined as a system of interest intermediation in which the constituent units are organized into a limited number of singular, compulsory, non-competitive, hierarchically ordered, and functionally differentiated categories recognized or licensed (if at all) by the state and granted a definite representational monopoly within the respective categories in exchange for observing certain controls or their selection of leaders and articulation of demands and supports.

While these definitions show the difference between pluralism and corporatism, the difference between state corporatism and societal corporatism can be shown in the elements of both. In state corporatism, the institution of number, the singularity and the compulsory character of the collectives are due to social processes, through competition, corporatism, social processes and interorganizational arrangement. In contrast, state corporatism means that the elements are replaced by deliberate government rules, state-imposed criteria of membership and through means of the law. Again, the non-competitive and hierarchical character, their functional differentiation, under conditions of societal corporatism are produced by internal processes of oligarchization and bureaucratisation and not by state-imposed regulation of their internal structure and their external relations. Finally, societal corporatism produces differentiation by the state and representative monopoly by imposition from below upon public officials, and not as privilege granted from above by the state as a condition for association formation and continuous operation. In more abstract terms of differentiation and integration, the differences can be caught in the following way. Both of them represent attempts of integrating a differentiated society. Due to its pervasive utilization of society through state-dominated organizations, state corporatism tends however to decrease differentiation and autonomy of social subgroups while societal corporatism is based on state-independent social power resources tends to maintain or even increase social differentiation and sub-system autonomy.

Co-determination should be understood as an important mechanism of neo-corporatist structures which permeate on different levels of coordination be-

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tion in co-determination models. If neo-corporatist coordination is to work successfully, it has to be made sure that a coordination exists between coordinating mechanisms. If this can be achieved by close integration or contrary by an increasing separation again is an open question.

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