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**Addressing labour  
market segmentation:  
The role of labour law**

**Simon Deakin**

October 2013

Governance  
and Tripartism  
Department

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## Foreword

One of the key features of the labour market developments observed during the past decades throughout the world relates to a phenomenon of labour market segmentation, e.g. the division of the labour market into separate submarkets or segments, distinguished by different characteristics and behavioural rules. To a large extent, these attributes depend on the specific environment in which workers operate. Segmentation may arise from particularities of labour market institutions, such as contractual arrangements (permanent versus temporary employment), their enforcement (and the resulting informality), as well as types of workers concerned (such as migrant, domestic, or dispatch workers).

While the phenomenon is not new, the job crisis has brought an increasing attention to the segmentation/duality issue, especially in Europe. The implications and costs of segmentation are multiple, in both economic and social terms: they include wage gaps between segments, differences in access to training and social security, as well as in working conditions or tenure. Moreover, segmentation implies limited transitions to better jobs. The consequences of segmentation also have macroeconomic implications, such as lower productivity and higher employment volatility.

In this context, and as part of its objective of promoting decent work, the ILO launched, in 2012, a research programme to better understand how labour market institutions affect employment outcomes in both quantitative and qualitative terms. One of the main motivations of the research project is to put job quality at the forefront of the policy debates, informing the main stakeholders in the world of work of the extent of labour market segmentation and its implications for job quality in selected countries. Fourteen country studies on labour market segmentation and job quality were provided by external country experts, as well as thematic papers on job quality in segmented labour markets and the role of labour law, collective bargaining, and improved enforcement. These studies were discussed in a scientific Workshop held at the ILO in December 2012 and used as thematic inputs in a policy-oriented Workshop held at the ILO in April 2013.

The current paper is one in the series of thematic papers. It makes an essential contribution to the discussion on contractual segmentation of labour markets by providing an analysis of theoretical, empirical and normative literature with a view to understanding possible legal causes of segmentation and the role of labour law in alleviating its effects. It does also discuss legal techniques used to address the effects of segmentation and offers a policy perspective on how to approach labour law and labour market reforms.

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## Abstract

Labour market segmentation is problematic because of its links to poor job quality, inequality and discrimination, on the one hand, and inefficiency in resource allocations, on the other. Segmentation is the result of contractual ordering which is often privately efficient but socially sub-optimal. The law largely reflects the economics forces and social norms which give rise to segmentation, but can amplify and perpetuate its effects. The rise of atypical employment in some contexts and of informal employment in others is at least in part a response to the emergence of the standard employment relationship, or SER, as a legal model and normative benchmark for certain aspects of labour law, in particular employment protection legislation. Attempts to counter segmentation and informality by extending the scope of the SER, on the one hand, and accepting atypical forms but aligning them more closely with the SER, on the other, have met with limited success. The most successful strategies for labour law reform are those based on an integrated policy approach in which some flexibilization of employment protection rules is combined with complementary mechanisms for mutualizing labour market risks, including collective bargaining, workplace social dialogue, work-life balance laws, work sharing arrangements, targeted fiscal reforms, and active labour market policy.

## 1. Introduction

This paper analyses the role of labour law in addressing the effects of segmentation in labour markets. Segmentation occurs when the labour market is divided or structured in a way which is reflected in the forms taken by the employment relationship or contract. It is associated with the division between ‘core’ and ‘atypical’ employment in some contexts, and with that between ‘formal’ and ‘informal’ employment in others. In industrialized economies, atypical work takes the form of part-time, fixed-term and temporary agency employment, and casualized forms of work such as zero-hours contracts, task contracts and ‘false’ or ‘sham’ self-employment. These employment categories are said to be ‘atypical’ by comparison to a ‘normal’ or ‘standard’ employment relationship (SER) which is full-time, indeterminate in duration, and based on a stable contract between the individual worker and a single, clearly defined employing entity. In developing economies, segmentation is identified with a distinction between a ‘formal’ sector in which employment is stable and regulated, and an ‘informal’ sector of casualized work relations which are, in varying degrees, undocumented, untaxed, and beyond the scope of collective agreements and legislative protections.

Labour market segmentation is regarded as problematic because of its association with inequality and discrimination. The rationing of high quality jobs to those in a protected ‘core’ or ‘formal’ sector and the resulting marginalization of others is linked to earnings inequality and to the perpetuation of discrimination based on gender, age, and ethnic origin. Segmentation may also have implications for efficiency. Dualist labour market structures may be the result of choices by employers and workers which are privately efficient but socially sub-optimal; in other words, they may maximize the joint product of parties directly engaged in bargaining but impose a net loss on society by virtue of their negative effects on third parties. Dualist structures could also result from institutional rigidities which prevent efficient contracting, and so impose both private and social costs. Either way, segmentation results in the misallocation of resources.

The issue to be considered here is how far the negative effects of labour market segmentation can be counteracted by legal or other regulatory measures. This poses a

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number of prior questions. One is how far labour law itself, as a labour market institution, is responsible for segmentation. Another is how far law can be used as an instrument for addressing a complex, multi-causal social and economic phenomenon such as segmentation. To address these questions, an interdisciplinary approach is required, which can isolate the role of the law in shaping or structuring the labour market, and arrive at an assessment of the possibilities of and limits to legal intervention as a mechanism for promoting job quality.

Section 2 provides an overview of theories of labour market segmentation which variously emphasize its different economic, legal and developmental aspects. From an economic perspective, segmentation is understood as having a number of interacting causes, including employers' organizational requirements (internal labour market theory) and labour-use strategies (efficiency wage theory), the responses of unions (insider-outsider theory), and the impact of the household division of labour on workers' labour supply decisions (feminist economic theory). From a legal perspective, segmentation arises from the tendency of legal regulation to superimpose a set of status-based distinctions on work relations (SER theory). These legal taxonomies, which partition and stratify the workforce, are only partly a response to external economic and political factors; they are also, to a degree, internally generated by the complex and multi-functional modes of regulation which characterize labour law systems (reflexive law theory). Theories of development present a range of views on the phenomenon of informality in emerging markets, which can be variously interpreted as the consequence of delayed development (structural transformation theory), an adaptive response to local conditions (dependency theory), and evidence of over-regulation (legal origin theory).

Section 3 presents an overview of legal techniques for addressing the effects of segmentation. Comparative evidence from a range of countries is reviewed. The legal responses are grouped into three categories. The first consists of changes to the taxonomical categories used to determine the scope of labour law protections. These include legal measures that widen the definition of wage-dependent labour and minimize or remove qualifying thresholds based on wages, hours or duration of employment. The aim here is to ensure that fewer workers are excluded from the 'core' protected category; their effect is purely formal or classificatory, in that the substance of protection is not addressed. The second set of techniques, by contrast, addresses the content of labour law protections. This includes, on the one hand, laws mandating equal (or pro rata) protections for workers in atypical work relationships to those in the 'core' ('levelling up'); and, on the other, laws reducing the protections which apply to the workers in the core, so as to bring them closer into line with those in the atypical categories ('levelling down'). The third set of techniques involves the use of the law to stimulate alternative mechanisms of labour market regulation for addressing segmentation: these include collective bargaining, training policy, and fiscal incentives.

Section 4 analyses the main lines of recent normative debates concerning the SER. The perspectives reviewed here include those of the transitional labour market theory (TLM) and the capability approach (CA), as well as analyses arguing for a re-evaluation of legal concepts associated with the SER, including the concept of the contract of employment and the related idea of 'subordination' as the basis for identifying dependent labour.

Section 5 provides an assessment and conclusion.

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## 2. Theories and models of labour market segmentation

### **Economic perspectives: Efficiency bargaining, insider-outsider effects, and the consequences of the division of labour**

The first 'dual labour market' theories of the 1970s identified a division of the market into a 'primary' segment consisting of stable employment in firm-specific internal labour markets, and a 'secondary' segment of low-paid, unskilled and short-term jobs (Doeringer and Piore, 1971). Employment within the vertically-integrated firm was seen as based on formal, bureaucratic rules and procedures, whereas work in the secondary market was governed by unfettered competition (Edwards, 1979). This was compatible with human capital theory, which had earlier predicted that long-term employment relationships and seniority-based wages would be found in contexts where firms and workers made mutual investments in firm-specific training (Oi, 1962; Becker, 1964). In a similar vein, transaction cost economics identified stable employment with the presence of 'asset-specific' capabilities, in contrast to low-skill and low-discretion jobs which were associated with 'spot contracting' and 'market governance' (Williamson, Wachter and Harris, 1975).

These results were extended by the efficiency wage theory from the early 1980s. The efficiency wage paid by employers in the primary sector reflects external market prices to some degree, but is also based on the firm's need to incentivize its workforce through internal payment systems and job security arrangements. Thanks to asymmetric information, employers cannot fully assess the qualities of workers (Stiglitz, 1986). Where they cannot monitor workers' aptitude and motivation without cost, and where firm-specific investments are at stake, employers will increase wages and other elements of the work bargain above the opportunity or market-clearing wage. As wages in the primary sector do not fully reflect prices, labour is displaced into the secondary sector, where competition is further intensified (Yellen, 1984). On one reading of efficiency wage theory, the effect is to worsen job insecurity in the secondary sector, and to induce involuntary unemployment, as workers are unable to 'price themselves' back into jobs no matter how low the wages they are prepared to accept (Solow, 1990). For employers in the primary sector, this may be a welcome side effect of their own wage bargaining strategies, as the existence of a 'reserve army' of labour in the secondary market enhances the disciplinary threat of job loss for those in the primary sector (Bulow and Summers, 1986).

In these ways, privately efficient behaviour by employers and workers in the primary sector could lead to an overall social cost as the positive effects of higher productivity in the primary sector are outweighed by the negative effects of unemployment and low wages in the secondary sector, and by immobility of labour across the divide between the primary and secondary sectors. Whether there is, in practice, a net social loss from these arrangements is an empirical question. One implication of these theories is that state intervention may mitigate the effects of segmentation in various ways, by, for example, instituting universal vocational education and training systems which counteract the effects of casualization and under-investment in human capital in the secondary sector (Acemoglu and Pischke, 1998). Another way in which the state could reduce segmentation is by mandating unfair dismissal and worker representation laws which may enhance motivation and productivity without employers needing to rely on divisive forms of efficiency wage bargaining (Levine, 1992).

A further development of efficiency wage theory is insider-outsider theory, which uses a similar logic, but shifts attention to the role of trade unions in segmenting the

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labour market. According to this approach, segmentation is at least partly the result of union organizing strategies, which seek to control the labour supply with a view to bidding up wages in the primary sector (Lindbeck and Snower, 1988). The empirical validity of this view has been questioned, as exclusion is by no means the only or even principal strategy pursued by unions; general unions seeking to organize across occupational and sectoral lines would, by the same logic, counteract the effects of segmentation (Sengenberger, 1981). If so, the law has a role to play in mitigating the effects of this segmentation, according to how far it supports inclusive union organization strategies and seeks to extend the protections of collective bargaining to fewer workers in sectors facing obstacles to unionization in the form of casualization and weak employer organization (Rubery and Wilkinson, 1981).

The economic and sociological literature has also analysed a range of supply side factors influencing labour market segmentation. Feminist theory emphasizes the role of social norms governing the household division of labour as a source of segmentation. The traditional household division of labour is seen as entailing a double source of disadvantage for women: within the household, their labour is unpriced and provided at below market cost, while their participation in the labour market tends to be restricted to jobs which do not consistently provide a subsistence wage (Picchio del Mercado, 1981, 1992). The differential labour market experiences of male and female workers work systematically to the advantage of the former; this is reflected in occupational segregation and unequal access to training, job security and employment-related benefits (Walby, 1986). According to this point of view, laws which address inequality between women and men in employment and which aim to break down the gender-based division of labour, such as equal pay laws, discrimination laws and work-life balance laws, can be expected to alleviate the effects of segmentation (Fredman, 1998).

### **Legal perspectives: The SER model and reflexive labour law**

Economic theories, as we have just seen, suggest ways in which specific legal interventions could offset particular aspects of labour market segmentation. Legal theories, in a shift of emphasis, focus on the degree to which the law itself can be seen to be a cause of segmentation, and on the capacity of particular legal mechanisms, as regulatory devices, to address the complex, multi-causal forms of inequality associated with segmentation.

The theory of the standard employment relationship or SER originated in German legal and sociological writings of the 1980s (Mückenberger, 1985, 1989; Bosch, 1986), was then extended to a comparative analysis taking in other systems including Britain (Mückenberger and Deakin, 1989; Deakin and Mückenberger, 1990) and Canada (Vosko, 2000). It has more recently provided the foundation for a wide-ranging programme of research covering a number of developed and developing economies (Stone and Arthurs, 2013). The SER theory was initially formulated in terms which, drawing on institutionalist approaches in sociology and economics, emphasized the functional role of the labour law system in regulating work relations in a market economy. In this approach, the SER is understood as an ideal type or model for legal intervention, rather than an empirical reality, or a specific juridical concept, although it is not unrelated to either. The SER is seen as serving protective, selective and incentive functions. It offers a degree of protection to the individual worker against the power of the employer, but it does so on a selective basis, rationing access to security according to how far work relationships meet the criteria of length of tenure and continuity of service. The incentive to seek and maintain continuous employment is, relatedly, addressed to particular groups in the workforce.

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The SER is the result of a historical process, and its emergence is a relatively recent phenomenon, traceable to the middle decades of the twentieth century (Deakin, 2002). Its form differs according to national contexts, reflecting different national experiences of industrialization and variations in industrial relations frameworks. Thus, in the German context the contrast between the SER and atypical employment forms was expressed within the legal system. In Britain it was, at least in the beginning, more a function of tendencies within the collective bargaining system (Mückenberger and Deakin, 1989), although over time it has assumed greater legal significance in the British system too, as collective agreements have declined as a source of regulation and been displaced by employment protection legislation and other forms of direct legal intervention (Deakin and Wilkinson, 2005).

The early SER literature saw the ‘crisis’ affecting the SER as a largely external phenomenon, generated by changes in the economy associated with outsourcing, subcontracting and the delocalization of production on one hand (Collins, 1990), and changes in family structure associated with rising female participation in employment on the other (Vosko, 2000). The SER was also seen as being challenged by political factors, as manifested in the fashion for policies of deregulation in both product and labour markets from the early 1980s onwards (Mückenberger and Deakin, 1989), and, later, by the removal of barriers to the transnational mobility of goods and capital and the rise of a ‘globalized’ economy (Arthurs, 2010).

By contrast, more recent developments in reflexive labour law theory, which is based on an evolutionary and systemic view of law, stresses the role of factors internal to the legal system in generating segmentation (Rogowski, 1992, 2013). The legal system is conceived as an autonomous social system which coevolves with, and hence is indirectly influenced by, the economy (‘cognitive openness’), but is partially closed off from it (‘operational closure’). For present purposes the main implications of this approach are, first, that the law does not respond immediately to economic pressure, so that changes in the economy to the way in which employment relations are constituted do not straightforwardly translate into changes in legal forms and concepts; the way the law regulates employment is functional in broad terms, but is also path-dependent, and shaped by the internal discourses and processes of the law (Deakin and Wilkinson, 2005: ch. 1). The second implication is that there is limited scope to use law as an instrument of conscious policy change. This is not to say that legal change cannot induce changes in the operation of the economy, but that the effectiveness of the legal system cannot be taken for granted, and is often a question of linking legal regulation to self-regulation on the part of social actors, and, more generally, to the operational elements of other sub-systems. Law becomes ‘reflexive’ in this sense when it recognizes its own limits while, conversely, seeking to harness the capacity for self-regulation in the economy and the industrial relations system (Rogowski, 2013).

From the point of view of theories of labour market segmentation, the significance of reflexive labour law theory lies in pointing to the structural links between the phenomenon of segmentation, and the legal form of the SER itself. The proliferation of distinct atypical employment forms is a response to the problems caused by the emergence of the SER as the paradigm legal form of the employment relationship. The stricter the protections associated with the SER at the level of the legal system, the greater the pressure on the law to permit alternative forms of employment, such as fixed-term work, as an alternative to the SER (Schömann, Rogowski and Kruppe, 1998). At the same time, attempts to regulate atypical work by requiring equivalent or pro-rata treatment of fixed-term or part-time workers by comparison to permanent and full-time workers indirectly validate, and thereby protect, the core SER concept (Vosko, 2010; Rogowski, 2013).

Reflexive labour law theory also offers an account of the limits to, but also opportunities for, legal regulation as a mechanism of governance. On the one hand, it

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points to limits to deregulatory strategies which seek to generate higher employment by lifting the ‘burden’ of regulation. These ‘make assumptions about the permeability of the legal system, and its openness to economic influence in the form of market pricing and similar effects, which run counter to reflexive law theory’. From a reflexive point of view, the success of a deregulation strategy depends on the effectiveness of self-regulation, for example through individual contract or through self-regulation on the part of social actors, in the industrial relations system: ‘reflexive labour law teaches deregulation that it is dependent on the willingness of the targeted social systems to respond to its demands’ (Rogowski, 2013). Relatedly, deregulatory strategies may be insufficient on their own to generate job growth, but may be dependent on the triggering of an alternative regulatory mechanism, such as active labour market policy or collective bargaining, to achieve the desired outcomes. In this sense there is often little to distinguish deregulation from re-regulation: both consist of the ‘regulation of self-regulation’ (Rogowski, 2013).

Reflexive and systemic approaches to labour law adopt an interdisciplinary perspective in which analysis of the internal legal discourse and processes of the law is combined with external perspectives drawn from the sociology and economics of law and empirical research methods which study the operation of the law in practice (Rogowski, 2013). A growing body of empirical research operates by constructing data which are sensitive to the internal dynamics of legal systems, in terms of modes of regulation and in particular the link between legal regulation and self-regulation through collective bargaining (Deakin, Lele and Siems, 2007). These data, when combined with time-series econometric techniques, can throw light on the interaction of labour law with complementary regulatory mechanisms, such as those of company law and corporate governance, in promoting productivity and innovation at the firm level (Deakin and Sarkar, 2008; Acharya, Subramanian and Bhagdi-Waji, 2012a, 2012b; Belloc, 2012).

### **Developmental perspectives: Mechanisms for addressing informality**

In the developing country context, the issue of the SER is somewhat differently framed. The status of the SER as a point of reference for labour law is contentious in settings where the large majority of workers do not have access to regular employment. Under these circumstances, the pursuit of the SER can be seen as an instance of the failed transplantation of legal models from developed economies to those still undergoing industrialization. An alternative perspective stresses the functionality of the SER as a response to issues of coordination and risk management in all labour markets, and predicts an alignment of legal systems with more formal employment patterns as a result of the spread of wage labour in emerging economies.

Development theories offer a range of perspectives on the role of the legal system and of labour market institutions more generally, which turn on the nature of different conceptions of the stages of development (Marshall, 2013). Theories of structural transformation which were influential in the immediate post-war decades saw development as a linear process characterized by the movement from low valued added agriculture to higher value added forms of production based on manufacturing. This view was challenged in the 1950s and 1960s by the dependency theory, which argued against viewing low and middle income countries as primitive versions of industrialized ones. The developmental path experienced by the economies of Europe and North America would not necessarily be replicated elsewhere because of the specificities of post-colonial societies and because of the effect of the uneven terms of trade between the developed and developing worlds. Even with the spread of manufacturing to developing countries, there would be problems in absorbing into the formal economy ‘marginal workers of low productivity’ as well as those employed in ‘precarious employment or

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disguised unemployment' (Prebisch, 1959). This perspective implied a need for tailored forms of state intervention and argued against an assumption of a linear movement from the institutions of pre-capitalist economies to those of mature market-based economies. From the 1980s the debate shifted again, with an emphasis, derived from neoclassical economic theory, on the self-equilibrating properties of unregulated markets, and scepticism towards labour law on the grounds that it was a source of distortions and rigidities. From this perspective, informality resulted from the misguided application to developing country contexts of legal institutions designed for developed ones (Botero et al., 2004).

This view has been challenged by systemic-evolutionary models of labour which argue for the long-run compatibility of market-based economic development with the labour market institutions which are characteristic of industrialized economies, including social insurance and collective bargaining (Deakin, 2011). Elements of the SER may be functional in a developing country context, depending on the extent of wage dependency among its population, the availability of alternative means of subsistence including access to the land and family structures, and the effectiveness of political institutions. In developing country contexts undergoing labour law reform, informality may arise as an 'internal' reaction to the emergence of the SER and the resulting need for flexibility in other employment forms. Mechanisms for addressing informality may include changes to tax law and business procedures aimed at minimizing the complexities of registration in the formal economy, but they will also involve a range of complementary mechanisms, including basic income guarantees (Berg 2011), mutual forms of social assistance (Le Roux, 2013), and support for solidaristic forms of collective bargaining (Fraile, 2009).

### **3. Addressing labour market segmentation through labour law reform**

Since the debate about labour market segmentation began in the 1970s, the problem of dualism has been addressed in various labour law reform initiatives. Three broad types of reform can be identified, which roughly correspond to stages in the evolution of the regulatory response: (i) changes to the personal scope of worker-protective laws, aimed at enlarging the definition of wage-dependent labour and lowering or removing wages and hours thresholds and minimum qualifying periods of service which had the effect of excluding atypical workers from protection; (ii) shifts in the substance of protection, in some cases involving a weakening of the rights of workers in the core, in others the establishment of a legal right to equivalent or pro-rata treatment for those in the periphery; and (iii) the conjoining of reforms to worker protective laws (including some deregulatory ones) to complementary mechanisms of intervention, including active labour market policy, fiscal law, social security law, and collective bargaining.

#### **Changes to the law on personal scope, wage/hour thresholds and qualifying periods**

The early literature on the SER identified its selective effect as tied up with the operation of legal rules and concepts defining the personal scope of worker-protective laws (the employee/self-employed divide) and, within the category of protected workers, further limiting the extent of protection by reference to threshold requirements which excluded workers contracted on an irregular basis, for only a few hours per week, or for a limited duration, from protection against unfair dismissal and rationed other job and income security rights. In response to concerns raised by these exclusionary rules, courts and legislatures from the 1980s onwards sought to widen the scope of protection through changes to the classification of work contracts. This was done, in the first place, by

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complementing traditional tests of employee status based on ‘personal subordination’, which stressed the presence of a formal employment relation based on hierarchy and control, with tests based on economic dependence, which focused instead on the economic risks to which the worker was exposed and thereby brought within the scope of protection workers without stable employment but who were nevertheless economically dependent on the employing enterprise. Casual workers and those with irregular or unstable work contracts, or those affected by ‘sham’ self-employment arrangements, were particularly affected by this process.

In some jurisdictions, such as France, this step was facilitated by the courts, which demonstrated willingness to take greater account of economic criteria in defining the divide between subordinate and autonomous work. The strict French approach was also assisted by the enactment of various statutory presumptions of wage-dependent status for workers in the ‘grey zone’ between employment and self-employment (Freedland and Kountouris, 2011: 280).

In Italy, Spain and the UK, , the legislature took the initiative through the development of new conceptual categories spanning or complementing the traditional binary divide between the employed and self-employed (Freedland and Kountouris, 2011). These were the ‘parasubordinate workers’ in Italian law (1973), the ‘autonomous economically dependent workers’ in Spanish law (2007), and the ‘worker’ concept in English law (1999).

Both strategies had some success in overcoming rigidities in the legal classification of work contracts, but they also encountered difficulties and limits. The strict French approach to the classification of subordinate work, which left little discretion to the parties to shape the nature of their relationship, was challenged on the grounds that it amounted to a restriction on cross-border labour flows under EU law on freedom of movement. The challenge did not lead to a significant loosening of the approach taken by French labour law to the issue of classification, but it is illustrative of concerns of some social actors, including those representing small business owners and consultants, that the law was overly rigid.

The alternative route of developing new conceptual categories allowed ‘quasi-dependent’ workers to get access to certain labour law rights (such as the minimum wage and working time protection) at the expense of creating new complexities, as it was now necessary for the law to define the status of workers in this third group distinctly from those of subordinated employees, on the one hand, and entrepreneurs and other economically independent providers of services, on the other. In some instances, as in the case of the English law ‘worker’ concept, tensions between ‘personal’ and ‘economic’ tests of subordination, which had characterized the earlier case law on the ‘employee’ test, simply reappeared in a modified form (Deakin and Morris, 2012: 174-181). Concerns over the complexity associated with the ‘parasubordination’ category in Italy and the loss of certain protections for workers in that group led to a reappraisal of that model and a shift back to reliance on the normal contract of employment as the basic legal form of the work relationship (Freedland and Kountouris, 2011: 383-4).

Hours-based thresholds which excluded part-time workers from employment protection were mostly removed in EU Member States from the late 1980s onwards as a response to developments in the case law of the European Court of Justice, which characterized these exclusionary rules as a form of indirect sex discrimination. This was based on a recognition that part-time work on low weekly hours was largely associated with female employment, as a result of the unequal division of household labour between women and men. In Britain, thresholds excluding part-time workers from unfair dismissal protection where they were employed for less than eight or, in some cases, 16 hours per week, were abolished by statute following judicial rulings, applying EU law. These judicial decisions called into question the original rationale for these exclusions,

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which was that they reflected the limited commitment made by part-time workers to the enterprise, and also rejected attempts to justify them by reference to their supposed job-creation effects, which empirical research had been unable to verify.

The removal of hours thresholds also had its limits as a strategy for dealing with segmentation. This is because, while thresholds operating within employment law were mostly removed, thresholds operating in social security law and fiscal law, or their equivalents in terms of wage thresholds (requiring employees to earn a minimum weekly salary to qualify for inclusion in social insurance schemes), continued to operate, and operated as an implicit subsidy to employers in the case of low-hours part-time work. This was the experience with UK rules on the operation of thresholds for social security contributions from the 1980s (Dickens, 1992) – the effect of which was only slightly mitigated by changes to national insurance contribution thresholds in the late 1990s – and with German ‘mini-jobs’ in the 2000s (Bosch and Weinkopf, 2008). In both cases, the operation of implicit subsidies operating through the social security and tax system encouraged employers to offer jobs with a low wage and hour threshold, sometimes just a few hours a week. Although this offered a route into employment for some groups, principally married women for whom such work was a feasible option as it enabled them to combine waged work with childcare responsibilities, the operation of the wage thresholds gave rise to new forms of segmentation between full-time and part-time workers, and between male and female workers. In both countries the phenomenon of low-hours part-time work has come to be associated with concerns over low pay, casualization and exploitation of a vulnerable group with limited bargaining power.

Service-related thresholds for unfair dismissal protection, a further source of segmentation identified in early literature on the SER, have also been modified over time, although most systems retain some probation period for job security rights, and the trend is not all one way. The UK has recently reintroduced a two-year qualifying period for statutory unfair dismissal protection. A one-year period was in force from 1999, which itself had replaced a two-year service qualification in effect since the mid-1980s.

Thus, the effects of shifting the boundary between subordinate and independent work to include economically dependent work relations, while removing or lowering thresholds based on wages, hours and length of service, have not been entirely successful in addressing the issue of segmentation. The selective function of the SER remains, in part because of its continuing relevance in social security and fiscal law, and attempts to create distinct categories for quasi-dependent work have resulted in new varieties of segmentation rather than a single employment status for all workers.

### **Aligning the substance of protection for core and atypical workers**

A second set of reforms aims not at extending the scope of the SER, but at aligning the substantive legal protections accorded to ‘standard’ and to ‘atypical’ work. This route involves an acceptance of the legitimacy of atypical employment forms, without fundamentally questioning their ‘non-standard’ nature, since the SER is used as a benchmark for an evaluation of the position of atypical workers. The aims of such reforms include the equalizing costs between standard and atypical forms, thereby reducing the implicit subsidy associated with atypical work, and mitigating the association of atypical work with low pay and casualization. In some cases, similar ends have been sought by a strategy of loosening the protections granted to core workers, or at least, as in the British case, tolerating a low existing standard of protection, which can be thought of as a form of ‘levelling down’ to the standard of protection of those in the periphery.

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The strategy of enhancing the regulation of atypical work through a discrimination-based approach is associated with the three EU directives adopted in relation to part-time work (1997), fixed-term employment (1999) and temporary agency work (2010). These measures drew on certain country experiences. French law introduced a requirement of non-discrimination for workers in atypical work relationships, by comparison with those in full-time, regular and indeterminate employment, during the 1980s. Several other European countries followed suit before the adoption of EU-level measures. A major impact was experienced in systems which did not previously have regulation on fixed-term employment, such as the UK. The transposition of the Fixed-Term Employment Directive in 2001 was accompanied by the introduction of constraints on the power of employers to offer repeated fixed-term contracts and a restriction on the use of individual waivers of unfair dismissal rights. Waivers of rights had previously been valid for fixed terms with a minimum duration of two years.

The British case is distinctive because the implementation of the Fixed-Term Employment Directive resulted in a situation where there was little difference in the legal protections granted to fixed-term employees and those with indeterminate employment contracts. However, this was in part the result of the low level of protection from unfair dismissal of core employees; in particular there are fewer constraints in English law on the employer's power to dismiss for redundancy than in comparable mainland European systems.

A tendency towards stricter regulation of fixed-term employment contracts is observable across EU countries during the 2000s (Rogowski, 2013). In part this reflects the impact of the 2001 Directive, but it also indicates a reappraisal of the strategy of allowing fixed-term contract types to proliferate as exceptions to the SER, which was particularly marked in Portugal and Spain in the 1980s. In both these countries, unfair dismissal regimes for core workers which were highly protective by the standards of other European countries were inherited from the period of authoritarian rule which ended in the mid-1970s. These dismissal regimes were left largely in place in the transition to democracy and the associated recognition of freedom of association rights, but in reforms of the 1980s employers were granted the right to use fixed-term contracts in a wide range of cases. By the mid-1980s over 70 per cent of new hires in Portugal took the form of fixed-term hirings, and a dual labour market was emerging there and in Spain, with younger employees in particular having limited access to permanent work. Reforms in Portugal in 1989, and repeated changes in Spain (1994, 1997, 2001, 2002 and 2006) tried to address the problem by limiting the range of justifications for fixed-term hirings, but there is little evidence of these reforms reversing the tendency towards segmentation (Wöfl and Mora-Sanguinetti, 2011).

The German tradition is one of strict regulation of fixed-term employment, with courts from the 1960s developing the view that a contract would be regarded as permanent or indeterminate if the employer did not provide a good reason for using the fixed-term option. The Employment Promotion Act of 1985 clarified the range of justifications for fixed-term contracts but its liberalizing effect was confined to a narrow set of cases involving particular sectors, such as higher education (Schömann et al., 1998). Empirical research carried out in the late 1980s found that any job creation effect of the reforms was negligible (Büchtemann and Höland, 1989), and a later study suggested that the large majority of German employers valued long-term employment relationships (Fuchs and Schettkat, 2000).

The effectiveness of alignment strategies appears, then, to vary according to the context being considered. In Spain and Portugal, the path-dependent effects of the growth of a dual labour market during the 1980s and 1990s are still being felt, notwithstanding recent efforts to reverse the liberal approach to fixed-term contracting which dates from that period. In Britain, segmentation between permanent workers and those on fixed-term contracts is less marked than elsewhere largely because protections

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for core workers are weaker than in comparable European systems. In Germany, the legacy of strict judicial control over fixed-term contracts continues to shape employer attitudes, and this contract type is of relatively limited significance as a source of flexibility for firms.

### **Coupling labour law reform with complementary mechanisms for alleviating segmentation**

If changes to the scope and substance of employment protection law appear to have had limited success in alleviating the effects of labour market segmentation when adopted in isolation from other mechanisms, there is evidence that more successful results may be obtained from integrated reform packages which combine a degree of deregulation or re-regulation in employment law with complementary regulatory interventions aimed at stabilizing employment in the secondary sector. These complementary mechanisms may include basic income guarantees, active labour market policies, vocational education and training provision, workplace social dialogue, solidaristic collective bargaining, and work-life balance laws.

In the European context, integrated strategies for addressing segmentation and related inequalities in labour markets have been associated with transitional labour market policies (TLM) since the early 1990s (Schmid, 1994; Schmid and Rogowski, 1998). The premise of the TLM approach is that law and policy should be actively developed with a view to promoting transitions between employment forms (unemployment or non-employment; flexible forms of work; and regular, indeterminate employment), and at particular points in the career cycle. TLM is compatible with a reflexive approach to labour regulation (Rogowski, 2013) and with the idea of ‘coordinated flexibility’ (Schmid, 2008). From this point of view, some deregulation of employment protection laws may be justified to reduce employers’ costs, but only if accompanied by measures to support transitions, such as wage subsidies or support for retraining, and by procedural protections. In the TLM approach, ‘the labour and social-welfare legislation governing employment relationships need to be deregulated and re-regulated in such a way that the economic and social advantages of stability are not lost’ (Rogowski, 2013).

Empirical work in on TLM policies identifies a wide range of experimentation with various mixes of regulatory mechanisms. Many of these are associated with the Nordic countries and the Netherlands, where TLM policies and the related concept of ‘flexicurity’ have the most salience (Auer and Gazier, 2002). The Dutch experience during the 1980s was one of growing numbers employed in part-time work, and a rise in fixed-term employment and agency work which was a response to the requirement for employers to obtain administrative approval for redundancies in the case of standard, permanent jobs. In the 1990s there was a switch in policy designed to offset the effects of segmentation. On the one hand, the requirement of administrative approval for redundancies was removed. Hours and wage thresholds affecting part-time work were abolished and the government encouraged the social partners to engage in collective bargaining over the promotion of part-time work and flexitime. A legal right to flexible working was introduced which allowed employees to adjust their contractual working time either up or down, unless the employer could show that this would significantly affect its interests. The Dutch law is more extensive than the right to request part-time work which operates in the UK, for example, which does not amount to a right but is subject only to an overriding enterprise interest, and cannot be used to request a return to full-time employment after a period of part-time work.

In Denmark, paid leave laws have been used since the mid-1990s to encourage a more equal division of household labour and facilitate transitions between employment and family work and from unemployment into waged work. A number of schemes were

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put in place to provide for the right to paid childcare leave, sabbatical leave and educational leave, with the latter two subject to negotiation between employer and worker. The paid leave schemes operate according to a principle of job rotation, under which the job is offered to an unemployed person for the duration of the leave period (Pfau-Effinger, 1998).

In France and the Netherlands, work sharing arrangements have taken the form of job pools which operate as a form of mutual insurance for workers. Often constituted in the form of mutual forms of corporate enterprise, these arrangements operate to allocate workers across a network of clients or users in a given region or sector. Sometimes the pools are organized by temporary work agencies which provide training and professional development in addition to allocating workers to assignments (Rogowski, 2013).

Training and vocational educational arrangements in several countries are increasingly being tailored to support the transition process. In Germany, continuous training and skills upgrading is supported by tax credits and by the social insurance system. The social partners are granted a regulatory role in Germany and the Netherlands in the administration of training and labour market policy while also negotiating on the regulation of atypical work (Visser and Hemerijk, 1997).

In these cases, partial deregulation in employment protection law is coupled with active labour market policy and training measures which allow interventions to be targeted to particular groups facing exclusion and discrimination in the process of transition. The involvement of the social partners through the collective bargaining process is helpful in that it assists in the more effective resolution of distributional conflicts over the allocation of risks, and allows for local conditions to be taken into account in the operation of protective norms, rendering them more flexible.

The European experience of addressing segmentation through TLM-based approaches cannot be straightforwardly transposed to the experience of labour informality in developing countries, but the idea of policy integration and complementarity in regulatory mechanisms is relevant in that setting. The reversal of the trend towards labour informality in several Latin American countries during the 2000s illustrates the role of complementarity. In the case of Brazil, several factors were at play (Berg, 2012). On the one hand, there were deregulatory measures which sought to reduce the costs of business registration for small firms and microenterprises, and to cut the costs of participation in the social insurance system for low paid workers and their employers. Steps were also taken to encourage participation in the tax and social insurance system of previously marginalized groups, such as domestic workers. On the other hand, the transition to more formal work was assisted by basic income mechanisms which provided a low but stable form of income to around a third of the population, and by the use of minimum wage laws and the extension of sector-level collective agreements to stabilize wages. The labour inspection system was more effectively resourced. While a favourable macroeconomic context and a reduction in labour supply – in part as a result of changes to the education system and a related reduction in rates of child labour – also played a part in the growth of formal employment, it is unlikely that the shift to greater formality would have occurred on such a scale had it not been for coordinated policy actions across a range of areas.

Distinctive forms of mutualization and social dialogue are also having a role in addressing segmentation and related informality in South Africa. South Africa has recently experienced a high and rising informal sector and also high unemployment, to which the extension of formal collective bargaining and employment law based on the SER is not seen as providing a viable solution (Le Roux, 2013). Forms of self-organization among informal workers, such as artisans and traders, nevertheless provide some basis for the mutualization of risk and for representation of workers' interests in dealings with employers and public bodies (Theron and Visser, 2009; Bamu and Theron,

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2012). Studies point to the potential feasibility, in the South African context, of a strategy of re-regulation, involving the lifting of some regulatory costs from individual employers, on the one hand, and legal support for worker cooperatives, workplace social dialogue and union-based forms of insurance and mutualization beyond the firm, on the other, to promote stable employment (Le Roux, 2013).

#### **4. Normative perspectives on the SER: Paradigms and models for labour law reform**

There has recently been an active debate over policy responses to labour market segmentation and the future of the SER as a model for labour law. The Supiot Report for the European Commission, published in 1999, argued for a reappraisal of the employment model and for labour law to play a more active role in underpinning training and investment in human capital through the mechanism of ‘social drawing rights’, an idea based on some of the experiments in income guarantees, leave arrangements and mutualization of risk that were developing in mainland Europe at that time. In its emphasis on the need to build labour market capacities, the Supiot Report helped to promote interest in the ‘capability approach’ (CA) as a normative basis for labour law reform. Later work further developing the CA has analysed the role of particular labour law mechanisms – including minimum wage laws, discrimination laws and work-life balance laws – in addressing labour market inequalities, a line of work with implications for the segmentation debate (Deakin and Wilkinson, 2000, 2005; Browne, Deakin and Wilkinson, 2004).

The European Commission Green Paper on the future of labour law in 2006 argued for a somewhat different flexicurity-based approach to labour law reform which purportedly drew on the TLM theory (Commission, 2006). The Green Paper highlighted the high degree of labour market mobility achieved in the Nordic systems and attributed this to the flexibility of employment protection laws in those countries. This perspective arguably neglects the role played by sector-level collective bargaining and high levels of expenditure on active labour market policy interventions in mutualizing labour market risks in the Nordic context (McLaughlin, 2009). The TLM theory, in its emphasis on coordinated flexibility and the need to maintain stability of employment as a goal, has a somewhat different approach to the deregulatory agenda underlying the Green Paper. The TLM and CA approaches converge on the need for regulatory mechanisms to address the underlying causes of inequality in labour markets and for the state to play an active role in policy formation and implementation in order to mitigate market failures and collective action problems (Deakin and Rogowski, 2013).

A number of specific legal proposals have been made with a view to reducing contractual segmentation. In France and Italy, the project for a ‘single contract’ envisages a unique status for wage-dependent workers, removing the formal divide between permanent and fixed-term work, while deregulating some of the protections which currently apply to the indeterminate contract of employment (Cahuc and Kramarz, 2004; Boeri and Garibaldi, 2008). These approaches are consistent with the preservation of the SER in a somewhat ‘flexibilized’ form. A more radical step would involve a shift away from the contract of employment as the basic juridical form of the employment relationship, in favour of a polycentric set of legal forms based on the generic idea of the personal work relation (Freedland and Kountouris, 2011; Stone and Arthurs, 2013).

In developing country contexts, the need for reform of employment protection law and a move away from firm-specific regulation through the SER in favour of community and sector-based forms of mutualization has been highlighted (Le Roux, 2013). Analyses have also stressed the role that solidaristic forms of collective bargaining can play in

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alleviating the effects of informality in emerging markets (Berg, 2012; Hayter and Ebisui, 2013).

So far, neither the single contract approach nor the argument for moving beyond the SER as the focus for employment regulation has had much success in changing the terms of the global debate over labour market flexibility. As part of the response to the global financial crisis, industrialized countries, particularly in Europe, have once again resorted to policies of dualism as a means of inducing greater flexibility. Thus, rules exempting part-time work and fixed-term employment from certain aspects of employment protection legislation have been proposed and, to some degree, adopted as part of the structural adjustment packages agreed by the Troika and EU Member States requiring financial assistance during the Eurozone crisis (Deakin and Koukiadaki, 2013). As these reform packages also involve cuts to minimum wages and restrictions on sector-level collective bargaining, they run counter to the experience of integrated policy design which characterized successful responses to labour market segmentation in the Nordic systems and other EU Member States during the past decade.

## 5. Assessment and conclusion

This paper has reviewed theoretical, empirical and normative literature on labour market segmentation and the related phenomenon of informality, with a view to understanding possible legal causes of segmentation, and the role of labour law reform in alleviating its effects. Theoretical perspectives drawn from the social sciences stress the multi-causal nature of segmentation. Segmentation has been shaped by the interaction of employer strategies, union responses, and social norms shaping the household division of labour. In welfare economic terms, contractual arrangements which lead to segmentation are often privately efficient but socially sub-optimal. The role of the law is, to a certain extent, one of reflecting these wider economic and social forces. However, path-dependencies and institutional rigidities within the law may amplify and perpetuate the effects of segmentation. The emergence of the SER as the paradigm legal form of the employment relationship and the benchmark for the normative evaluation of labour law institutions has generated a dynamic of selection and discrimination in the classification of work relationships which is, in part, internal to the legal system, and can be addressed through legal reforms.

Disentangling the different causes of segmentation, or identifying a role for the law as an instrument of dualism which is distinct from the operation of market forces and social norms, is not a straightforward process. Empirical studies nevertheless point to significant differences in the form taken by segmentation across countries, which are reflected in aspects of the legal institutional framework. In some European countries, such as Portugal and Spain, segmentation is associated with the divide between permanent work and fixed-term work, in part because of the coupling of a highly protective unfair dismissal regime for core workers with a high degree of flexibility over fixed-term contracting. This has resulted in the embedding of inequalities related to age and seniority of employment. In Germany, the Netherlands and the UK, the segmentation is associated with part-time work and with a male-female divide in terms of labour market participation and experiences. In the Nordic systems, contractual segmentation is less evident, partly because of flexibility in the operation of employment protection laws for core workers, and also because of complementary regulatory mechanisms for alleviating the effects of segmentation, including active labour market policy, solidaristic forms of collective bargaining, work-life balance laws, and institutionalized forms of work and income sharing.

Reflexive labour law theory provides a set of models for understanding the complex interrelation between labour law and changes in the social and economic context of

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employment, as well as a conceptual foundation for analysing the different techniques available to policy-makers considering labour law reforms. The reflexive point of view stresses the limits to strategies of deregulation which are not tailored to specific national and sectoral contexts. Simply alleviating employers' regulatory costs through deregulation may have little direct impact on segmentation, and may be counter-productive for core workers, leading to a loss of productivity and innovation at the firm level. The more successful reform initiatives are those which view labour market reform as a process of re-regulation, in which any loosening of employment protection laws is accompanied by complementary measures for mutualizing labour market risks and targeting employment transitions through subsidies and fiscal support. Thus, the solution often lies not in employment protection law reform, or at least not entirely, but in a number of complementary regulatory mechanisms, including active labour market policy, multi-employer collective bargaining, work-life balance laws and work-sharing arrangements, which together form an integrated policy response to segmentation and informality.

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