

Employment Regulations and Small Business Entrepreneurship Research Review

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Chapter 2: Literature Review

This chapter reviews the past literature on the impact of federal and state employment regulations on small businesses and entrepreneurship. It has been divided into the following subsections: strategy for identifying applicable research; reputability and extensiveness of the literature review; literature of the theoretical framework or conceptual framework; review of the seminal literature; review of the core literature; review of the practitioner literature; and application of the literature.

Strategy for Identifying Applicable Research

A systematic approach has been adopted in this literature review to study the impact of federal and state employment regulations on small businesses and entrepreneurship. In order to conduct the online research, various groups of words were used in combinations such as (a) federal law, state law, employment regulations, state labor laws, major laws of the Department of Labor, employee right, federal employment and labor laws, an overview of employment laws affecting labor rights, employment and labor laws 2017, (b) entrepreneurs and entrepreneurship defined, small businesses, number of employees, restrictions and (c) innovation, similarities, differences, impact, consequences, effects, results, connection, link, impression, influence, policy. Different search engines and electronic databases, including Taylor & Francis, Springer, Wiley, Economic Papers, Social Science Research Network, JSTOR, SAGE's, Science Direct, PsychLit, EconLit, ERIC, Google Search, Google Scholar, and Elsevier, were used for empirical research.

Reputability and Extensiveness of the Literature Review

Literature of the Theoretical Framework or Conceptual Framework

Review of the Seminal Literature

The term seminal means something related to seeds or semen. While studying literature on any topic,

seminal indicates the most recent work from the relevant field. The seminal literature on the impact of federal and state employment regulations on small business and entrepreneurship has provided comprehensive information concerning the trends in the field. The literature over the years exhibits that there exists broad recognition that governmental regulations impact small businesses differently than large businesses. In fact, small businesses oftentimes decide to stay small in order to avoid the consequences of the effect of regulations on big businesses. It is suggested that this phenomenon stifles entrepreneurship. Although several studies have reviewed the impact of regulations on private businesses, there has not been a comprehensive study on the subject of the impact of employment regulations on small businesses.

Review of the Core Literature

The most important piece of core literature on the discussion of the impact of federal and state employment regulations on small business and entrepreneurship in the United States has been provided by Dixon et al., in 2006. It is a working paper that covers various laws, including employment regulations. The regulatory environment with respect to employment has been subdivided into four groups (Dixon et al., 2006). The first group of the set comprises the regulations governing acceptable employee behaviors in past, current and future workers (Dixon et al., 2006). The second group comprises the rules and regulations governing the employee behaviors in past, current and future workers (Dixon et al., 2006). The third group includes regulations on workers' compensation. Primarily, this group includes an administrative compensation program that covers the remunerations and incentives of the employees who would become sick or injured during the course of their work (Dixon et al., 2006). The last group includes rules and regulations concerning the unemployment insurance system, which is the system for compensating individuals who lose their jobs and become unable, at least temporarily, to find another job for one reason or another (Dixon et al., 2006).

The group of rules and regulations covering the labor unions has not been part of this discussion by Dixon et al. (2006) because this class is primarily seen as the labor laws. Although such labor laws have great importance in defining the relationship between the employer and his employees, they have not been considered in this discussion for three major reasons (Dixon et al., 2006). Firstly, a relatively small number of employees and workers are now becoming a member of labor unions, especially in the context of the private sector. Therefore, they are less likely to impact the employment laws and small businesses (Dixon et al., 2006). Secondly, simultaneous to the private sector, a small number of workers are being unionized among the small businesses. As a matter of estimation, according to the Current Population Survey data, only four of the ten employees in a small business are likely to form a union or become a part of a union (CPS, 2003). Lastly, the labor laws have been relatively stagnant in comparison to the employment laws and regulations concerning other parts of the field (Dixon et al., 2006). For these reasons, the attention of this paper has been kept focused on the other four groups of rules and regulations on employment.

- Administrative Enforcement of Government Regulations

Coming back to the topic of this dissertation, these four groups of rules and regulations on employment have been studied by researchers and practitioners such as Dixon et al. (2006) in order to find their relationship with small businesses. It has been found that firms of all sizes are at risk of harming their employee during the course of business activities and consequently may have to face civil action in this regard as the individuals, private groups, and organizations might take against them. The risk of the creation of a government agency authorized to take legal actions on firms' behavior after investigating them has been increased due to federal, state and local regulations. Such restriction implies that small businesses would have to face a lower risk of actions due to their inability to pass the employment threshold. The regulations are fairly vague, and therefore, more legal actions are to be taken, i.e., the risk is higher. Therefore, small businesses are likely to promote development and growth in an attempt to achieve the high employment threshold, particularly in the arena of anti-discrimination.

The reasons behind such behavior lie in the fact that these small businesses tend to avoid the threats of fines and legal actions in the case of failing to complete the reporting criteria (Dixon et al., 2006). Information-gathering burdens are also imposed on small businesses by administrative enforcement in addition to the legal risk if they are above a certain size threshold. The costs of these information-gathering burdens impose certain fixed costs on the firms, and thus, they tend to avoid them by every possible means, including the desire to remain below the reporting threshold limit (Dixon et al., 2006). Furthermore, it has been found through past literature, such as Bennett & Passmore (1985) and Mendeloff & Kagey (1990), that the fatality rates are much higher among small businesses in comparison to other businesses. Moreover, it has also been found that the cost of responding to health and safety regulations is not much higher for unionized and larger businesses in comparison to small businesses (Peek-Asa et al., 1999). This finding is consistent with the hypothesis that compliance with Health and Safety regulations increases the burden of fixed costs of a business. On the other hand, research has also indicated that larger businesses are better at implementing and regularizing the health and safety regulations in their firms instead of the small businesses because they are more profitable for them (Bartel & Thomas, 1985).

- Court Enforcement Policies and Regulations

Firm size does not explicitly play a role in the court enforcement policies and regulations.

However, the litigation process can have a differential impact on the businesses depending upon their size. For instance, the level of resources each firm spends on the process of litigation, either as plaintiff or defendant, primarily depends upon the size of the firm. These resources tend to influence the prospects of the larger businesses in the tort system. Large firms have deep pockets. Therefore, employees initiate actions such as violation of employment contracts, wrongful discharge and discrimination against these firms because such decisions are prompted by the lawyers as well (Dixon et al., 2006). On the other hand, in such litigation, the larger firms have the motive of spending

aggressively on such cases in order to mitigate future litigations (Dixon et al., 2006). Such an aggressive response deters the employees from involving in any further litigations with the larger firms because they are more likely to lose at the trials (Dixon et al., 2006). However, the initiatives taken by the firms, such as violence of trade secret units and non-compete agreements, are likely to have a strong financial back. The larger firms are willing to spend money on cases while seeking redress from employees (Dixon et al., 2006). Again, they have the strong motive of deterring the employees in an attempt to avoid any future litigations. To be specific, in the situations where the actions are initiated by the firms, they have the motive of deterring the employees from violating the trade secret units and non-compete agreements (Dixon et al., 2006). Moreover, due to their size, small businesses are more likely to go for the option of bankruptcy because the process requires lots of financial input. Simultaneously, small businesses are more likely to be involved in breaching the trade secret units and non-compete agreements because the entire business structure might be built on that one trade secret. Based on this theory, small businesses are more likely to take legal action against the breach of the agreement despite the risks and costs, including bankruptcy, involved in the process.

Finding out the impact of the restrictions on the employees' behaviors on the size of the businesses is currently difficult to assess. There is also a lack of indication that small businesses do not use non-compete agreements due to the restrictions imposed on them by the employment rules and regulations (Dixon et al., 2006). However, small businesses may face a burden in the imposition of such a clause due to the fact that the agreements can only be enforced through a clause. Larger businesses, on the other hand, may lose more than small businesses if such an agreement is breached (Dixon et al., 2006). Furthermore, labor supply is impacted due to the non-compete agreements, which predominantly means that small businesses are likely to be impacted more than larger businesses (Dixon et al., 2006).

For instance, a new start-up is being created and the workforce is being employed; there are chances that the workforce may include a pool of individuals who have previously worked with larger businesses in the same industry. If these employees have signed the non-compete agreements with their employers, then it is not possible for them to legally leave their current jobs and begin a new start-up in the market that might become a competition of the company in the future they are currently working with. Such an agreement might also hinder the ability of these employees to hire workers with past experience with larger firms in the same industry because they have worked with a competitor in the past.

In conclusion, there exist contradictory forces under the economic theory when it comes to the discussions of the court enforcement policies and regulations and the size of the firm. The exact point of link and the exact link between the size of the firm and the impact of the court enforcement are not easy to determine (Dixon et al., 2006). Therefore, the question of whether the lawsuits put more financial burden on the small businesses in comparison to the large businesses remains unsolved and goes unanswered under the current discussion, which has largely been based on the past literature from the field. It is also difficult to conclude who bears more of the legal costs as well (Dixon et al.,

2006). According to a recent study, the per-dollar cost of a lawsuit has a more aggressive impact on small businesses as compared to large businesses (Pendell & Hinton, 2004). According to the findings of the study, small businesses that have at least one employee in addition to the owner and ten million American dollars in annual revenue bear sixty-eight percent of the business tort liability costs, whereas only twenty-five percent of the business revenue (Pendell & Hinton, 2004).

Very small businesses, on the other hand, are the ones with twenty-six percent of the business tort liability costs and only eight percent of the business revenue. They are defined to have less than one million American dollars in annual revenue (Pendell & Hinton, 2004). The authors have found that as the revenue category increases, the tort liability cost per one thousand American dollars in revenue steadily declines (Pendell & Hinton, 2004). Therefore, the cost per one thousand American dollars in revenue is approximately sixteen dollars for businesses with an annual revenue of greater than fifty million American dollars, whereas it is approximately one dollar for businesses with less than one million American dollars in annual revenue (Pendell & Hinton, 2004).

- Responses to Workers' Compensation System

The size of a firm and the workers' compensation have a differential relationship despite the relative uniformity of coverage. Employers are required, by law, to cover potential workers' compensation losses by purchasing insurance or to get self-insured for the purpose of demonstrating sufficient financial resources (Dixon et al., 2006). Larger businesses are more likely to be benefitted from this situation. Larger firms self-insure their benefit payments due to the fact that they have the ability to bear the risks involved in the compensation claims of their workers, which often results in large payments within a single period. This ability reduces the expected costs of compensation of the workers for the larger businesses and firms because it bypasses the insurance system with two possible sources of inefficiency (Dixon et al., 2006). Firstly, the expected value of insurance payouts is often exceeded by the premiums due to a lack of perfect competition in the workers' compensation insurance market (Dixon et al., 2006). Secondly, insurers use a tool, i.e., experience rating, for adjusting the premiums based on previous claim history. The tool is imperfectly applied when it comes to the implementation of specific safety measures. It is an important tool because benefits from investments in safety are reaped by the insured firms (Dixon et al., 2006).

However, it brings a relative disadvantage for small businesses because it results in a less reliable experience for the firms to use as a base for premiums. Small businesses would still find it an expensive method despite the absence of bias in the application of the process because there are substantial fixed costs involved in it (Dixon et al., 2006). Moreover, small businesses have fewer workers; it indicates that these businesses do not have many workers to smooth the fixed costs. The incentive to promote workplace safety is further reduced if the small businesses are imperfectly experience rated (Dixon et al., 2006). On the base of this discussion, it can be concluded that the cost of insurance is difficult to bear and carry for small businesses in comparison to larger firms. Simultaneously, for the smaller firms, the outcomes for the injured workers are worse in comparison to the larger businesses (Dixon et al., 2006).

The workers are expected to suffer more injuries and workplace related illnesses if the business has lesser ability to implement health and safety regulations and fewer incentives to pay (Dixon et al., 2006). Similarly, the workers are expected to face greater severity of the outcomes at the smaller firms as well. On the other hand, larger businesses have the ability to modify their work in order to accommodate the injured workers. They also enjoy the ability to return to work (Dixon et al., 2006). Thus, the larger firms are less likely to have to suffer the long-term impact of disability (Reville et al., 2001; Peterson et al., 1997). These programs are also a cost saver for the larger firms because these businesses can negotiate the wages due to their ability to implement the health and safety regulations. Based on this discussion, it can be concluded that small businesses, in comparison to larger firms, are more likely to have disadvantages while responding to the workers' compensations.

- Responses to the Unemployment Insurance System

The responses to the unemployment insurance system are not likely to vary drastically among small and large businesses because there is no opportunity to self-insure when all employers are covered by the unemployment insurance system. As a rule, the tax paid by the employer is equal to the number of employees of the business (Dixon et al., 2006). Therefore, any disparities between the businesses due to their size on the grounds of taxes have been eliminated. As a matter of fact, the amount of tax for the employers depends on the experience rating of the unemployment faced by the business. The rate of tax changes in accordance with the number of layoffs and the stability of the labor force that they experience because the new employers are assigned a flat rate (Dixon et al., 2006). For example, in California in 2002, the maximum tax rate was 5.4 percent, the minimum was 0.7 percent, and the base rate was 3.4 percent for employers. Such rates are more likely to benefit the larger firms in comparison to the smaller businesses due to the fact that the former has the ability to response to changing economic conditions (Dixon et al., 2006). Thus, the larger firms have the chance to avoid increases in their payroll taxes because they can avoid some layoffs. The costs of the workers, when faced with higher costs or lower demands, are not bearable for the smaller businesses; they are unable to absorb the shock (Dixon et al., 2006). Therefore, these firms have to bear the full brunt of unemployment taxes. However, suggesting the strength of this impact is an empirical matter that would need future research.

References

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