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## WHY NOT LET AMERICANS WORK AT HOME ?

### INTRODUCTION

In hundreds of homes, scattered throughout the towns of Vermont, individuals have been earning extra money by knitting ski caps and sweaters for sale in nearby stores and ski resorts. These home crafts have been particularly attractive to the many women who cannot leave the home because of their homemaking and childrearing responsibilities. It is also important to many of the elderly, who turn to homework as a means of supplementing their retirement incomes. This source of income became available to all Americans in 1981 when Secretary of Labor Raymond Donovan concluded that Americans should have the right to work at home. He removed a Department of Labor regulation that prohibited workers in the knitted outerwear industry from working in their homes.

Donovan's action was overturned last November, however, when the United States Court of Appeals for the District of Columbia ruled that he improperly had removed the restriction. This decision was a blow to many Americans because it restricts the rights of citizens to engage in "industrial homework" during difficult economic times, when secondary sources of income are often essential. It was also a blow to the vast potential for Americans to work in their homes at computer terminals. By its decision, the Court probably has impeded the U.S. economy's march into the 21st century and towards the decentralized workplace.

The Court's finding was based on a 1943 regulation promulgated under the Fair Labor Standards Act of 1938, forbidding Americans from doing work at home in seven industries: knitted outerwear, women's garments, embroidery, handkerchief manufacturing, jewelry manufacturing, button and buckle manufacturing, and gloves and mittens. The only exceptions are for individuals who are unable to leave the home because of a physical or mental impairment, those who are caring for an invalid in the home, and those who can establish that they are independent contractors.

The only beneficiaries of the Court's ruling are the entrenched labor unions, which want to restrict the economic opportunities of those who are not its members. This makes the ruling particularly disturbing. It also is troubling because of the implication that reasonable rule changes can be blocked by the courts. In this regard, economist Thomas Sowell's observation about the judicial branch's tendency to supplant the executive and legislative branches' role in the decisionmaking process is particularly relevant: "It is hard to imagine why the writers of the Constitution would have set up a Congress or a President as decorative institutions if they thought there would be nothing for them to do in meeting the evolving needs of the nation."<sup>1</sup>

The ruling blocking the Secretary's action now means that the Administration must take further court action, perhaps even an appeal to the Supreme Court, if it wants to open new employment opportunities and protect the basic rights of its citizens to engage in free exchange. It is important, moreover, that the Administration send a signal to the business community that such restrictions will not be imposed on other industries, such as the rapidly emerging telecommunications field.

If this effort is unsuccessful, the Administration should consider less comprehensive rules changes to minimize the adverse impact of the regulations. These actions may include exempting homemakers with small children or individuals living in rural areas, where factory employment may not be feasible. Meanwhile, legislative changes to achieve these same goals should be considered. Senator Orrin Hatch (R-UT), for instance, has introduced legislation (S. 2145) to ease the barriers to homework, and hearings on the homework issue are scheduled for February 9th, before the Labor Subcommittee of the Senate Labor and Human Resources Committee.

The present restrictions are an anachronism, dating from a period when there was no high-technology and relatively few women were in the labor force. The situation today is very different, and the law dealing with homework should be amended accordingly.

## BACKGROUND

The current debate surrounding homework began in 1979, when the Labor Department's Boston office took action against CB Sports of Bennington, Vermont, for allegedly violating the homework regulation when it purchased ski hats from women who had produced them in their homes. The company claimed that the knitters preferred working at home and that they were independent contractors, not employees of the firm.

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<sup>1</sup> Thomas Sowell, Knowledge and Decisions (New York: Basic Books, Inc., 1980), p. 294.

After examining the details of this controversial case, Labor Secretary Donovan proposed the abolition of all homework restrictions. Opposition from organized labor, however, led him to reverse this decision for all but the knitted outerwear industry. But even this concession failed to satisfy the International Ladies' Garment Workers' Union. It joined with some unionized manufacturers to file suit in federal court to overturn the regulation.

Among the key issues in the case was whether or not the knitters are employees of a company or independent contractors--and therefore free to knit ski sweaters and hats in their homes. The Court's primary concern was that it would be difficult to enforce the minimum wage, overtime compensation, and child labor force provisions of the Fair Labor Standards Act for such homeworkers. The Court acknowledged the union's concern that the payment to homeworkers of wages below the minimum set by law would put employers complying with the Act at a competitive disadvantage, and would adversely affect the wages of all employees in the industry.

The Labor Department replied that maintaining restrictions on homework within the knitted outerwear industry would have a negative impact on employment in the industry. Moreover, the knitters themselves argued that they wanted the flexibility associated with working in their own homes and setting their own hours.

#### THE CASE AGAINST THE RESTRICTIONS

The Court of Appeals in Washington rescinded Secretary Donovan's decision to lift homework restrictions, calling it "arbitrary and capricious." Yet its own ruling disregards individual freedom and seriously misunderstands the basic laws of economics. The decision is likely to have a devastating impact on the many Americans who prefer to work at home. If the ruling stands, or is not superseded by a change in the law, it will shut down many successful home-based businesses. This would be a serious blow to thousands of women seeking financial independence.

#### Independent Contractors

The primary issue in cases such as this is whether the homeworkers are employees of a firm or independent contractors. Traditionally, independent contractors have been considered those who provide their own place of employment, set their own hours, supply their own equipment, supervise their own work, and are under either a verbal or written contract. Independent contractors usually do not receive from their clients unemployment insurance coverage, workers' compensation insurance, vacation, or the other benefits a company normally provides to its employees.



In the major homework cases that have come to court, the individuals forbidden from working at home had supplied their own sewing machines and completed the work without any outside supervision. Contracts specifically stated that the women were not employees and were responsible for their own time and equipment. Moreover, the homeworkers also contracted their services to other businesses and individuals. The women were paid a fixed price for each piece and no deductions were withheld because the Internal Revenue Service considered them to be independent contractors.

### Employment Effects

In its opinion, the Court noted that, "The employment 'benefit' of the rescission might simply be a shift in employment from factories to homes, with no net increase in employment opportunities."<sup>2</sup> The facts, however, argue just the opposite. Rather than having an adverse effect on employment, as the Court and the unions allege, rescinding the restrictions on homework would generate thousands of new employment opportunities. The main reason is that homework lowers overhead costs in an industry by allowing individuals to work in their homes, instead of in a costly factory. This reduction in costs is reflected in a lower price for the final product, stimulating a greater demand for the products and raising the number of workers needed. Prohibiting homework, by contrast, forces firms to invest relatively more money in plant and equipment and less on labor than they otherwise would; this costs jobs. If firms can no longer operate with the optimal mix of production factor inputs, efficiency declines, costs rise and employment falls.

The underlying problem with the Court's reasoning is that the judges based their economic theory on a static model rather than a dynamic one, and thus ignored economic feedback effects within both the affected industry and the economy as a whole.

Unless the prohibitions on homework are rescinded, the adverse impact on employment will be exacerbated in the future. It has been estimated that by 1990 as many as 15 million jobs could be performed at home.<sup>3</sup> The University of Southern California's Center for Future Research, for instance, projects that in ten years' time there could be 5 million Americans working at computer terminals in their own homes at tasks ranging from data processing to accounting.<sup>4</sup> This development could be an enormous boon to females heading households, to the handicapped, and to the many other Americans in some way restricted in movement.

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<sup>2</sup> See the decision in International Ladies' Garment Workers' Union, et al. v. Raymond J. Donovan, et al, U.S. Court of Appeals for the District of Columbia Circuit, November 29, 1983.

<sup>3</sup> The Washington Post Magazine, December 26, 1982.

<sup>4</sup> See Marguerite Zientara, "Telecommuting Banned by Service Union Board," Computerworld, July 11, 1983, p. 7.

Unfortunately, unions already are taking steps to curb this. The Service Employees International Union, representing about 780,000 chiefly clerical and health workers, has passed a ban preventing its members from doing computer homework. Unless action is taken to guarantee the freedom of homeworkers, telecommuting may be stillborn. There is no industry lobby as yet to plead the other side of the case. And firms will not undertake the large-scale capital investment needed for this type of work arrangement to develop without some assurance that the government will not step in, under pressure from the unions, and change the rules in the middle of the game.

### Labor Opposition

While organized labor claims that allowing homework would make it difficult to enforce the Fair Labor Standards Act, their real concern seems to stem more from a desire to protect their members from competition. Unions lobby for such restrictions because the rules increase the costs of nonunion competitors. This raises the demand for union labor and pushes up wage rates. The rules also allow the unions to exercise their strike threat more forcefully, since there are fewer competitors to threaten their jobs.

### Homework and the Minimum Wage

Union leaders claim that if women were allowed to work at home in these seven craft industries, they would be paid below the minimum wage. According to Rudy Oswald of the AFL-CIO: "Women need protection to ensure they get paid basic minimum wages for hours worked, including overtime...That's the basis for the regulation."<sup>5</sup>

According to the Department of Labor hearings, however, there is no evidence that such protection is necessary today.<sup>6</sup> But even if it were, wage rates below the statutory minimum would not be as harmful as the unions insist. A basic principle of economics is that the wage rate equals the marginal productivity of labor. When a minimum wage is established at a level above that market level, employment opportunities disappear for the least productive workers, because their services are priced out of the market. The minimum wage alters the relative prices of labor and other inputs by making low-skilled labor relatively more expensive, therefore inducing the substitution for low-skilled labor of other inputs, such as machines and more productive labor. This artificial and inefficient mix of resources leads to increased production costs, reducing output and lowering the total demand for labor.

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<sup>5</sup> See Glenn Emery, "Women seek to stop U.S. from banning jobs sewing at home," The Washington Times, February 23, 1983.

<sup>6</sup> The hearings were held in January and February of 1981.

Thus, the alternative for those homeworkers making less than the minimum wage is likely to be no employment at all. If the workers are not productive enough to find a job in a factory, or live in an area without factories, or have family responsibilities that preclude them from leaving the home, then homework restrictions mean a reduced family income and possibility of falling into the welfare trap.

Homework restrictions can also prevent some women from obtaining the skills necessary to command higher wages. While many women doing homework initially may not be productive enough to earn the minimum wage, they could acquire the skills needed to raise their incomes. In December 1981, for instance, a Green Bay television station charged that some Laotian women supplying clothing to the Silent Woman, Ltd., company appeared to make less than the minimum wage. The owner of the company pointed out, however, that since the women could not speak English, there were difficulties involved in training them to operate sewing machines. Unfortunately for the Laotians, the publicity forced the firm to cancel its contract with the women. Since fully trained sewers normally command far more than the minimum wage, the action meant that the newly arrived immigrants could not receive the training necessary to become self-sufficient. Although the current restrictions on homework have been rationalized by the argument that they protect vulnerable citizens, the reality is that they do just the opposite--by denying them economic opportunity and upward mobility.

## ENFORCEMENT

The Appeals Court's ruling against homework also was based in part on the difficulty in enforcing industry conditions on homeworkers. It noted problems in identifying workers and obtaining data on the hours worked and the effective wage rate paid. Despite these difficulties, however, it would be improper for the government to ban homework simply because some workers may violate the provisions of the Fair Labor Standards Act. Doing so punishes all workers for the infractions of a few. The burden of proof should be on the government to show significant violation of the Act. Moreover, illegal homeworkers are hardly "protected" by a ban, since they are in no position to go to the Department of Labor to submit a complaint.

### Fringe Benefits

Union supporters of the homework restrictions sometimes allege that "the people who are doing the homework don't have any benefits, vacation, job security and so on, and are directly substituting for people who would have those more decent working conditions were they employed directly by an employers."<sup>7</sup>

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<sup>7</sup> See Zientara, op. cit.



This reasoning is flawed. In the first place, defining "decent" working conditions involves a subjective judgment. Many would consider their home to be a far more decent workplace than a factory. Moreover, independent contractors do not have to accept the standardized work and compensation package typically offered in unionized factory employment--where pay scales are usually based on seniority rather than productivity. Instead, homeworkers receive the full monetary value of their output, allowing them to purchase privately the package of benefits they desire.

There are other advantages of working at home: lower travel and child care expenses, additional time with one's children, and flexible work schedules. Homework also allows women who cannot work full-time to earn extra income while at home.

Even if a homemaker received a lower wage than a factory worker, therefore, the "net" wage (deducting taxes and work-related expenses) may actually be higher for the homemaker. And even if a pay differential still existed, the congenial surroundings of a home could be sufficient to overcome this difference. For homeworkers, in other words, the "compensating differential" associated with working at home may be large enough to make higher paid factory employment less desirable.

#### Special Circumstances

Allowing women to work at home is particularly important for those with small children. Over the last several decades, the female labor force participation rates have risen dramatically. The percentage of mothers with children under age 18 who are in the labor force has increased from 40 percent in 1970 to almost 60 percent in 1983--and the rate for married women with children under age 6 increased from 30 percent to 50 percent.<sup>8</sup> About two-thirds of these mothers work full time. According to MIT economist Mary Rowe: "The future child-care issue for children of this age may not be availability of care but rather accessibility and affordability."<sup>9</sup> Removing restrictions on homework could alleviate this problem considerably by enabling mothers to work, yet take care of their children without incurring enormous costs. Caring for a child, particularly of preschool age, can be as much of a problem to women trying to find employment as caring for an elderly family member or an invalid--yet the law allows an exemption only for the latter groups.

In addition, factory employment may not even be a practical option for Americans living in rural areas. The scarcity of employment opportunities and lack of adequate transportation may

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<sup>8</sup> Sheila B. Kammerman, "The Child-Care Debate: Working Mothers vs. America," Working Woman, November 1983, p. 132.

<sup>9</sup> Ibid.

pose serious problems. For many, homework is an ideal solution; the only problem is that it is now forbidden by Washington.

The Appeals Court did note that Labor Secretary Donovan failed, in his decision, to consider alternatives to complete rescission of the existing restrictions, such as providing additional exemptions for those with child care obligations, or distinguishing between rural and urban areas. These modifications would be a step in the right direction, but groups not exempted would still face serious problems.<sup>10</sup>

### Voluntary Exchange

Union leaders often call homework inhumane and oppressive. They claim that it putatively "exploits" individuals working at home. What this ignores is that the contract between the homemaker and the company is voluntary and is made by adults. Homeworkers make such a contract because they obviously prefer working at home to working in a factory. They do so, apparently, because they want the benefits from working at home. Eliminating the homework option would deny some workers the opportunity for training and self-sufficiency. Moreover, individuals now in restricted industries have the choice of joining a union and taking a factory job--unless unions restrict entry into such employment, in which case it is exploitation on the union side.

Although unions and government officials often invoke the "public good" when justifying restrictions in such cases, they do not weigh the social benefits against all of the costs. In particular, no account is taken of the losses suffered by those affected by "protective" rules: the homeworkers unable to work and the companies prohibited from purchasing these products at the least cost. A government restriction against homework is nothing more than a transfer of wealth from one segment of the population to another achieved by the government violating one of America's founding principles--freedom of contract.

### Judicial Activism

In its ruling, the Court of Appeals did not find that the homeworkers today were in violation of the Fair Labor Standards Act. It simply said that Secretary Donovan, in issuing new rules, had not used "reasoned decisionmaking" in studying the options available short of complete rescission of the homework ban. If the Court's ruling stands it means that the Administration will have to obtain congressional approval before altering rules within one of its own agencies. The homework statutes, however, are not congressionally approved legislation but the Department of Labor's own restrictions. An analysis by the

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<sup>10</sup> In fact, the exempted groups would probably have even less recourse than before because they would have to compete not only with unionized factory workers, but the homeworkers as well. It would therefore probably be more equitable to exempt all groups.



Center on National Labor Policy, a legal foundation, points out that "The effect of his decision is to create a de facto reduction in the capacity of agency officials to make regulatory changes without the supervision of the entire Congress."<sup>11</sup> And if one Administration cannot reverse the regulations of another, then the power to promulgate regulations invites serious abuse.

### Legislation

The problems arising from the homework restrictions stem from the fact that the 1938 Fair Labor Standards Act is out of date. Two important recent trends make the restrictions against homework out of step with the times. First, the dramatic increase of the female labor force participation rate indicates a growing desire for women to earn additional income. This can be frustrated by their inability to find adequate child care. Second, the advent of the home computer means many jobs can be done at home. Unless businesses see a strong commitment by the nation's leaders to protect homeworkers, however, they may be unwilling to risk spending their own money to promote this development.

On November 18, 1983, Senator Orrin Hatch (R-UT) introduced S. 2145, "The Freedom of Workplace Act." The bill would repeal the restrictions on homework by amending the Fair Labor Standards Act so that homework is not prohibited for any occupation and special permits would no longer be required. It requires, however, that such workers be paid at least the minimum wage.

### CONCLUSION

In evaluating any policy, the results are much more important than the intentions. Desiring that homeworkers receive a decent wage is a noble objective, but it is clear that restricting homework is of no benefit to those supposedly being protected, and serves only to benefit politically powerful groups interested in curbing competition. With unemployment still high in the United States, the government should not be stifling job creation by such restrictive rules. More important, a free society should not allow some to use the coercive powers of government to enforce special interest laws at the expense of others who lack this power.

George Mason University economist Walter Williams notes that the "government cannot create a special advantage for the American citizen without creating a special disadvantage for another American."<sup>12</sup> So it is with bans on allowing workers in certain industries to work at home. Any additional employment of factory

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<sup>11</sup> Contact Lee Bellinger at The Center on National Labor Policy, Inc., 5211 Port Royal Road, Suite 400, North Springfield, Virginia, 22151.

<sup>12</sup> Walter E. Williams, "Minimum Wage--Maximum Folly and Demagoguery," The Journal of the Institute for Socioeconomic Studies, Winter 1983-1984, p. 33.

workers, supported by the monopoly bargaining position of their unions comes at the expense of the homeworkers who become unemployed, and the consumers who must pay more for products.

Allowing homework adds to the options of working Americans, giving them greater employment flexibility. As more and more women enter the labor force and new technology enables more work to be done at home, this flexibility is of critical importance.

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