29 The Effect of the New Tendencies in Labor Law on the Applicability of Managerial Wages

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29.1 The Emergence of the Demand for a New Direction of Labour Law

In my paper, I present a new and innovative regulatory approach in labour law, along the common interpretation of law and economics. The economic approach to legal studies has become more important in the past fifty years. The economic analysis of law is an interdisciplinary field, which combines the two disciplines of law and economics in order to provide a more complex and complete understanding of both areas. Economics answers lawyers' questions about how legislation imposed by government sanctions changes and influences the behaviour of players on the market. Economics provides behavioural theories concerning the impacts of legislation assessing individual decision-making and behaviour in terms of efficiency and income distribution. As Yale Law School Professor Bruce Ackerman puts it: "The economic approach to law has been the most important development in legal scholarship in the twentieth century." In legal scholarship, the application of economics has brought major changed in the interpretation and practical application of law. This is illustrated by the fact that in recent decades many scholarly publications and several articles have been published that specifically cover the field of the economic analysis of law. Such journals are, for example, the *Journal of Law and Economics,* or the *Research in Law and Economics.* Noted scholars of the new disciplinary field include, among others, *Stephen Breyer, Richard A. Posner,* or *Alex Kozinski.*[1] As far as the presentation of the relationship between labour law and the market is concerned, I rely on the basic assumptions of *Simon Deakin*, professor of law at Cambridge University, still active today. *Deakin*'s research primarily concentrates on the joint investigation of law and social science. Based on *Deakin*'s thoughts, I would like to answer the question of how the new development of labour law can capture the reduction of income inequality by effectively regulating the work-based income of people in executive positions.

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1 Robert Cooter & Thomas Ulen, *Jog és közgazdaságtan* (Law and Economics), Nemzeti Tankönyvkiadó, Budapest, 2005, pp. 9-24.

29.1.1 Why Is There a Need to Broaden the Scope of Labour Law?

I base my argument on two separate, nevertheless related hypotheses:

My first hypothesis is that labour law has been in crisis in the past decades. In the new Millennium, it has become clear to labour lawyers that there is a need to explore new dimensions of labour law, which respond efficiently and with innovative solutions to the rapidly changing global environment. In his 2014 book, "A munkajogi megfelelés ösztönzésének újszerű jogi eszközei" [New Legal Instruments for Promoting Compliance of Labour Law], *Attila Kun* has detailed the reasons why we may speak of the crisis of labour law today. Although this is not the main goal of my study, from the perspective of my topic, I still find it important to briefly present these factors.

The first such factor that contributes to the crisis of labour law is the increased theoretical and practical uncertainty that permeates various segments of labour law (e.g. regulations governing the atypical legal relationship of executive employees, the lack of an exact definition of the managerial contract, etc.).

The second significant problem with regard to labour law is that currently it seems that labour law cannot adapt to the globalizing economic and regulatory environment. Labour law regulations did not keep up with the increasing integration of markets and the emergence of international organizations, as well as the expansion of transnational corporations. This led to a decreasing emphasis on national (labour law) regulations in our internationalized environment. As a result, transactions and the relationship between economic players have become less transparent, precludinghe possibility of effectives upervision.

Last but not least, it is *Bronstein* who unearthed the last crisis factor in labour law. According to *Bronstein*, the root of the problem is the neoclassical ideology, which emphasizes the role of the market, seeking to neglect the role of the paternalistic state. In summary, we can conclude that labour law did not keep up with globalization, international transactions, and ever-increasing international institutional-economic changes. On the international level, the backward response of labour law to the rapid socio-economic changes leads to an inefficient allocation of human resources, which in turn has various unintended effects on the operation of the engine of the economy, generating a loss of

efficiency in the short as well as the long run. With this brief and factual listing of these factors, my goal was to present a clear picture of the fact that labour law is forced to promote the application of new and previously unused instruments besides examining the application of already existing legal norms. Following *Senden,* we call this function of soft law the pre-law function, when soft law is a prelude to the adoption of binding substantive legal norms.[2]

Of course, we also need to see clearly that in the present "world of free competition," in a world where a transnational corporation has almost the economic and political influence of a nation-state, it is difficult to find the middle ground among the labour law regulations. Regulations should not restrict the autonomy of the individual economic players, but at the same time, they also need to effectively serve economic cycles, they should not paralyze market mechanisms, instead, they should have a productive and stimulating effect on the individual and collective interests of each player.[3]

In my paper, I would like to present a new approach to labour law reflecting on the relationship between labour law and the market, that, in addition to classical "*hard law*" instruments, also aims to find alternative self-regulating "*soft law*" instruments that would be a step forward in solving problems of social problems in the 21st century. I find it important to emphasize that I am talking about additional legal norms that can be enforced besides keeping and enforcing positive legal rules and reinforcing effective and socially responsible corporations – *CSR=Corporate Social Responsibility.*[4]

First of all, it is important to take a briefly review the meaning of soft law. It is hard to give a clear definition of soft law or to distinguish it from hard law, because it has different meanings depending on where we situate the – binding or non-binding category. Some authors would say that soft law is not law, because it has misleading concepts, diminishing the line between hard law and legal norms, also weakening the phenomenon of law. In other words, they claim that norms are either binding hard law or non-law.

By contrast, I would say that soft law may be regarded as law, because it has several possible legal relevancies. According to Fabien Terpan[5] we can determine three types of soft law. The first type is "non-binding norms with legal relevance", the second is "bind-

2 Based on their characteristics in the legal system, *Senden* differentiates between three types of soft law. These three types are "para-law," "pre-law," and "post-law" soft law. The "para-law" function of soft law means that soft law norms often become substitutes for conventional legal instruments, and practically take over their functions. As I have mentioned above, the "para-law" function of soft law means that non-binding norms function as precursors to positive law measures by preparing the integration of legal norms into positive law. That is to say, soft law hardens, becomes enforceable by conventional law, and its breach has legal consequences. Finally, the "post-law" function of soft law means that soft law norms often become supplementary to classical positive legal norms, in order to improve the application and interpretation of law. In: Attila Kun, *A munkajogi megfelelés ösztönzésének újszerű jogi eszköze* (New Legal Instruments for Promoting Compliance of Labour Law), Budapest, 2014, L'Harmattan Kiadó, pp. 9-19.

3 Kun 2014a, pp. 9-19.

4 The term corporate social responsibility (CSR) was created by the Green Paper in 2001.

5 Fabien Terpan, 'Soft Law in the Europen Union-The Changing Nature os EU Law', *European Law Journal,* Vol. 21, No. 1, 2015, pp. 68-96.

ing norms with a soft dimension "and the third category includes "binding norms with a soft dimension + non-binding norms having legal norms."

The first type of soft law has a non-binding character, but it still has a strong legal relevance, takes several legal forms and exhibits various features giving a strong law and enforcement character to these soft law instruments. On the other hand, even if the soft law norm has many hard law features (e.g: wording, form) soft law is not legally binding, so it is not considered to be (hard) law. However, it is important to see that soft law can have legal relevance, and may also have the same effect as hard law.

In contrast with the first category, the next group of norms have binding characteristics, but these are not as effective, and do not have a same impact as hard law. Consequently, these norms are similar to hard law, but without any hard, legal enforcement power. These norms can function in a soft way, which also can effectively shape principleprinciples and legal norms.

Finally, in the last category soft law may be determined as a combination of the first and the second type of soft law. This category of soft law is relevant, since it has a role in the vast international soft law dimensions, and in particular, in the practice of EU law.

According to Fabian Terpan's definition of soft law we can see that, to understand and to give a correct soft law definition is challenging and difficult, because these norms have several contradictory practical effects and features. Besides the problems of definition, in international law and EU law, soft law has a significant impact on the application of EU norms and the fulfillment of harmonization goals.

If we take the EU soft law practice, we can see that the EU prefers to use soft law instruments to fill the legal regulatory gap between national law and EU law. Soft law appears to be a good instrument to render harmonization more effective, providing at the same time an "elegant" legal harmonization process. Soft law is often used as a first step to achieve a hard law harmonization. Similarly, to hard law, soft law can be as useful as a binding legal norm, without violating cultural preferences, general principles, and moral convictions. This favorable feature of the soft law makes the it an essential element of EU law. Generally, EU soft law establishes a bridge between national law and EU law, ensuring that EU hard law obligations are better adjusted to the fields of national environmental law, competition law and media law.[6] Principlely these soft law norms are non-binding instruments, which means that the application of these norms is not mandatory for national judges, yet according to the EU Commission these norms should be *"take into consideration."* This sentence is important. It means that soft law should not be regarded as a hard law, but it shall have a legal profound effect at the national level. National judges must attach importance to soft law norms, regardless of their lack of enforcement. This way, soft law has a vertical and external legal effect. More precisely,

6 Petra Lea Láncos, 'East of Eden Hotel – soft law measure on harmful content between harmonisation and diversity', *The theory and practice of legislation*, Vol. 6, No. 1, 2018, pp. 113-129.

the Commission can issue recommendations and "softly force" Member States to apply European principles and adopt them at the national level.

Even if the EU Commission tries to pressure Member States to apply EU principles, results shall depend on national judges' responses. Throughout the *soft governance* process the EU Commission wants to softly, but actively shape and determine national regulations without harming Member State sovereignty. The success of and the key to *intergovernmentalism* is national adaptation and national judicial practice.[7] The "new mode of governance" (NGM) can lead the way forward for future soft law EU measures, offering a soft harmonization process, with "*pre-law functions*." The effectiveness and success of NGM will mainly depend on national judges' willingness to enforce such measures.[8]

All in all, we must recognize that soft law in not a panacea for every case. Also at the international level, there is a need to use soft law as a "hybrid"[9] governmental tool to achieve intergovernmentalism.

Continuing the hypothesis of the relevance of soft law, I consider it important to emphasize the fact that I am talking about additional legal standards that can be enforced under perceived and enforceable legal rules and CSR = Corporate Social Responsibility. In fact, "soft law" instruments can contribute to the voluntary compliance of actors in various ways. As in many cases, soft law measures can be more effective in their own right than classical legal norms. But soft law instruments can also be applied in a preparatory phase, as forerunners to hard legal rules, which may eventually become classical legal instruments. This is also very important from the perspective of legal practice, because we often overlook legal norms that are not "set in stone," although in many cases these instruments provide the framework for effective regulation.

The CSR phenomenon as a new dimension of labour law can effectively fill the legislation gap where mandatory legal rules are missing. CSR instruments also seek to even out the relationship between employees and employers, playing an important role in supporting the idea of SRPP (Socially Responsible Chain Management) and RSCM (Responsible Supply Chain Management) frameworks.

In the last few years the new, global, hybrid labour law was strongly affected by CSR principles. While CSR – as a labour law regulatory instrument – does not have any binding legal consequences, it may be highly effective on multinational levels. We are witnessing many international initiatives and recommendations originating from international organizations with the aim of influencing and changing companies' behaviour. The essence of these soft law rules is to encourage companies to support the ideology of human rights in the field of (labour) law, and to be more socially responsible.

7 Michéle Knodt & Jonas Schhoenefels, *The Role of the Commission in 'Harder' Soft Governance: From Administrator to Policy Sharper by Surveillance,* Peper prepared for the ECPR SGEU Conference, Sciences Po Paris, 13-15 June 2018.

8 Láncos 2018.

9 Terpan 2015, p. 34.

The most relevant and innovative transnational soft law principles are the UNGP (Guiding Principles on Business and Human Rights of the UN) and the OECD Guidelines for Multinational Companies. These two relevant, innovative legal guidelines set high standards for the protection of employee's rights, with the goal to ensure social responsibility within the company and within the supply chain as well. The Principles and the Guidelines are clear international frameworks to be implemented a transnational level in labour- law, business and human rights contexts. Although these standards undeniable have no legal force, they do not exist in a "law-free zone."[10]

Today the concept of responsible corporate governance is interpreted rather widely. Nevertheless, the point can be made that each definition rests on the common element that corporations voluntarily integrate responsible principles of corporate governance into their corporate culture and management leadership. On the long run, these contribute to the profitability of the company through the implementation of environmental motivators in the internal and external environment of the company.[11] In addition to the theoretical dimensions of CSR, we must emphasize the importance of the routine of application, responsible leadership becoming the standard in management. For theoretical initiatives to be implemented, it is necessary to apply the ethical methods companies follow in the transnational and global environment when it comes to setting strategies, making business plans, budgeting, auditing, traceability, and last but not least, developing human resources management.[12]

CSR is a good example for the fact, that in addition to concrete legal norms, a new approach to proactive corporate behaviour has come to the forefront, highlighting that companies do not only need to take into account profit maximalization, but also aspects that are of a social, cultural, internal and external environmental nature. We also have to see that the CSR concept is a very promising additional "soft law" initiative, but not enough time has passed to actually draw far-reaching conclusions about its efficacy. Perhaps we should not expect CSR to renew labour law of the 21st century on it own, but it is undeniable that we can put a lot of faith in it.[13]

Despite the soft law nature of the CSR, it has a very promising "snow ball" and "spillover" effect for the future. Soft labour law standards should be reflexive, responsive in order to have a better chance at producing an optimal legal (hard) overall effect. The question is vast and calls for further investigations.

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10 Attila Kun, 'How to Operationalize Open Norms in Hard and Soft Laws. Reflections Based on Two Distinct Regulatory Examples', *Internatioanl Journal of Comparative Labour Law ans Industrial Relations,* Vol. 34, No. 1, 2018, pp. 23-52.

11 Attila Kun, 'A vállalati szociális elkötelezettség tematizálásának alapvonalai az Európai Unióban' (The Main Lines of Thematizing Corporate Social Responsibility in the European Union), *Jogelméleti Szemle*, 2004/1, 2004.

12 Marc Goergen, Salim Chahine, Geoffrey Wood & Chris Brewster, *Public Listing, Context and CSR: The Effects of Legal Origin,* Henley Business School, University of Reading, November, 2015.

13 Kun 2004.

The *second hypothesis of my study* is based on the fact that the income of executives has risen dramatically in the last decades. There has been some literature and various articles published on this topic in law as well as economics. The book that gets most spotlight today on this subject is probably "Capital in the Twenty-First Century," a book by the French economist *Thomas Piketty*. Undeniably, *Piketty*'s treatise is an outstanding work of his era, that perfectly sums up the features, theoretical background, as well as the historical overview of the income and wealth distribution characteristic of our days. Another significant addition of the book to the field is that it has the richest collection of income and wealth data in scholarship, and it analyzes its dynamics in the long run.[14] In addition, *Thomas Piketty* formulates various paradigms with regards to the distribution of wealth that many other researchers refer to. Thus, we can say that the book serves as a source on income distribution for all social scientists who are doing research on the distribution of income and capital. One may ask the question why is this important? In response, we can quote *Piketty,* who claims that the income inequality of the 21st century is "a new kind of income inequality."[15] According to him, in contrast with the income inequalities of the 19th century, today the wealth of the top one-tenth and 1% of the world mainly comes from income and not from inherited wealth, as in the era of Jane Austen. Another important feature of income inequalities is that the earnings of private sector executives have risen drastically, resulting in a group of first-generation millionaires. It is also important to emphasize, that contrary to what many believe, several societies, including the USA, are not as egalitarian as we would think. Since the 1980s, a previously unprecedented explosion of inequality has taken place in the USA, and has undoubtedly contributed to the instability of the economy, and eventually the economic crisis.[16]

In his theory of "the illusion of marginal productivity," *Piketty* draws attention to the fact, that the main cause of today's wage inequality is the emergence and extreme growth of the social stratum of the so-called *"new salaried rich,"* that has not been stopped by anything so far. *Piketty*'s theory that focuses on the group of executives, whose annual income is between USD 300,000 and USD 1,000,000, claims that the individual productivity of American executives is only based on subjective individual agreements, which cannot be objectively compared to the extent of their income. Determining the income of the executives depends on the decisions of personal and corporate "cronies." This is the phenomenon of the so-called "*cronyism.*"[17] It also follows that the salary of these top executives is not based on objective performance, but on individual decisions,

14 Wojciech Kopczuk, 'What we know about the Evolution of Top Wealth Shares in the United States?', *Journal os Economic Perspective*, 2015/29/1, pp. 47-66.

15 James Pierson, 'Background Facts', in: Tom Church, John B. Taylor & Christopher Miller, *Inequality and Economic Policy,* Hoover Press, 2015.

16 Daron Acemoglu & James A. Robinson, 'The Rise and Decline of General Laws of Capitalism', *Journal of Economic Perpectives*, 2015/29/1, pp. 3-28.

17 John H. Cochrane, 'Why we care about inequality', Church *et al.* 2015, pp. 144-156.

or external effects. He calls the income that is the result of external effects *"pay for luck"* money, which is not based on individual performance, but on external economic circumstances. Based on the above, it is clear that responsible corporate governance unfortunately cannot or will not prevail under all circumstances.[18]

Consequently, I have to conclude that individual interests often play a much bigger role and overwrite written or unwritten legal and ethical rules. In addition, the increasing income of the upper layers of societies contradicts the neoclassical ideology. There is no sign of Adam Smith's invisible hand that would create the market equilibrium, and market failures also continuously point to the need for a direct and indirect regulatory role of the state.

My two hypotheses concern two distinct disciplines, but they are nevertheless closely linked. There is an interconnectedness between labour law and economics. Just as labour law affects income inequality by regulating the income of executives, institutional economics also affects the formation of the framework of labour law. Departing from this joint relationship of the two hypotheses, I intend to analyze the new trend in labour law, and the questions of economic development.

29.2 Executive Employees as a Target Group of Scrutiny

Of the actors of labour law, in this study, I deal with the issues of executive employees from the perspective of HR. The group of executive employees is of great relevance for various reasons, regardless of which approach of the two hypotheses above we take as a starting point.

First of all, if we examine executive employees from the perspective of labour law, we can say that they constitute a special and at the same time very decisive group among employees. The atypical nature of executive legal relationships derives from a number of factors that significantly differ from a typical employment relationship. The position of the executive employee is special because it is based on a relationship of confidence between him and the *team* he leads. The executive should have a number of competences that make him capable of representing the interests of the company, and leading the teams employed to achieve these goals. Thus, the manager has to be able to formulate a proper business policy, coordinate complex tasks, manage the members of the organization in line with corporate goals, and last but not least, he must determine fundamental corporate goals. However, above all, his most important task is to make efficient and profit-oriented decisions to ensure the company's competitiveness.[19]

18 Thomas Piketty, *Capital in the twenty-first century,* The Belknap Press of Harvard University Press, London, 2014, p. 335.

19 Rita Ráczki, 'A vezetés természetének átalakulása' (The Transformation of the Nature of Leadership), *Munkaügyi Szemle*, 2009/4.

In light of all of this, we can say that the company executive is the person who is personally defining for a company, both for its external and the internal environment. Perhaps it would be an exaggeration to say that they need to be spotless, but it is certain that as a leader of an organizational unit, and as the representative of the interests of the owners, they should necessarily be a person who has authority and high moral values for shaping the internal as well as the external environment. Thus, the business and private lives of the managers need to be in line with each other.[20]

The atypical character of managerial roles is also determined by the fact (both in Hungary, as well as on the international level), that there is no precise legal definition of a manager, even though with the burgeoning of transnational companies the term has become widespread in everyday language. In Hungary, it was introduced into the Hungarian terminology via international corporations that emerged during the liberalization process following the collapse of communism. There are no provisions regulating managerial contracts in the Labour Code, thus the exact definition of manager is lacking as well. The legal relationship between the manager and the firm is governed by strict rules, such as confidentiality, loyalty to the employer, and rules regarding conflict of interest. In addition, they can quantify the expectation of strict results in these contracts. In order to maximize profits, managers have a high degree of autonomy, complying with the unlimited liability rules of civil law. Considering the above, we can say that beside its special, atypical labour law nature, the management contract also contains elements of civil law.[21]

The concept of management is not uniform in the different countries. Focusing on the American example, we can say that management contracts do not belong among the labour contracts. The main aim of these contracts is that the contract signed with the manager should ensure the company's effective, competitive operation that is profitable in the long run. Tamás Prugberger[22] states that the American managers do not belong among the employers, but are entrepreneurs, who are permanent representatives of the owner. "Thus the special status of managerial contracts lies in the fact that they are created as a combination of entrepreneurial and mandate contracts. One of the key attributes of management contracts is that they are based on a relationship of trust, thus they are treated very discretely by the contracting parties. One of the key and perhaps the most interesting points of discretion is the fact that the salaries of managers are not public. While common law countries, such as the USA, Australia, Canada or the UK now require that listed companies disclose the salaries of their managers also in the interest of the shareholders, this is only partially fulfilled in real life. As many income payments are not

20 Tamás Prugberger, 'A vezető állású alkalmazottak jogviszonyának egyes kérdései a gazdasági munka világában' (Certain questions of the legal relationship of executive employees in the world of economic labour), *Jogtudományi Közlöny*, Vol. 54, No. 5, 1999, pp. 2016-2017.

21 Emese Törő, *A köz- és a versenyszférában megvalósuló vezetői jogállás kritikai elemzése* (Critical Analysis of the Executive Position in the Public and Private Sector), PhD Thesis, 2005, pp. 124-149.

22 Tamás Prugberger, *Az Európai és magyar összehasonlító munka- és közszolgálati jog* (European and Hungarian Comparative Labour and Public Service Law), 2014, KJK – Kerszöv, Budapest, p. 410.

included in the salary of the managers, their real income may be multiple times greater than what is officially disclosed by the companies. As a result, the statistical data on incomes and their distribution may significantly differ from reality.

Another important substantive element of the managerial contract is the formulation of performance expectations towards the manager, which are often quantified, and are primarily defined by indicators such as the market share of the company, the number of shareholders, the rate of profit growth. These indicators are heavily dependent on the individual performance of managers, which is why they are significant in determining the salary of the manager. Beside the basic wage, the salary package of managers is supplemented by various incentivizing benefits, such as employee shares, performance bonuses, car, etc. These incentivizing benefits make managers interested in increasing the profit of the company (for example, by becoming shareholders of the company), besides rewarding the responsible operation of managers as well as their loyalty towards the company and the owners. The salary of managers may be determined in various ways, depending on the combination and ratio of these factors. These differences are highly influenced by the given country and the culture of the particular organization. As far as American corporations are concerned, the performance-oriented organizational culture plays a greater role, thus, the basis for the competitiveness of the company is the salary based on individual performance. Also as a consequence of their culture, Americans have the need to raise "superstars," "supermanagers," who make up the top one percent of society.[23]

If we look managers' salary trends we can say that American managers have by far the highest income, which has increased further in the last decades. The other two important issues related to the income of the managers is that determining their income depends a lot more on the leadership of the individual corporation, rather than labour law regulations. The person and salary package of CEOs is determined by management. For exactly this reason, there is a kind of back-and-forth close cooperation between CEOs in order to re-elect each other as executives, and in order to establish high salary packages for each other, regardless of their individual performance.[24]

The other important problematic issue is the positive external effects that affect the income of managers. That is, managers' more often than not increases independently of their individual performance, it much rather comes from those external economic and financial actors that affected the competitiveness of the company in a positive way. In recent times, we have seen various examples when corporate management caused serious losses to the company, nevertheless, the income of the executives was not curbed. This is

23 Kevin J. Murphy, 'CEO Pay and Appointment: A Market-Based Explanation for Recent Trends', A*merican Economic Review*, No. 2/2004.

24 Jesse M. Fried, 'Pay without Performance: Overview of the Issues', Harvard Law School, *Economics and Business Discussion Paper Series*, 2005/4-10, pp. 21-34.

well illustrated by the example of the CEO of *Deutsche Telekom,* the whose salary increase was the inverse of the rate of the stock price, representing a nearly 40% difference.[25]

29.3 Income Inequalities and the Regulatory Role of Labour Law

Based on the introduction to the problems described above and their timeliness, we can see that the structure and operation of today's large enterprises must be changed. We cannot simply pretend that, besides the ideologies of market economy and globalization, managers' salaries and the functioning of boards do not violate serious legal, moral, and economic rules. Many critics argue that regulatory actions that would undermine the freedom of players on the market cannot be included within the framework of the idea of market economy. Consequently, the related fields of labour law and constitutional law must be considered separately in the context of other disciplines. Two main directions have been identified in literature to resolve the problem of executives' salaries.[26] One of the proposed solutions is to create and apply stricter rules that will contribute more extensively and more effectively to a more responsible, transparent, and traceable operation of the company. Also providing substantive legal guarantees in terms of legal regulation, the other solution supports the expansion of the rights of shareholders and the accountability of corporate management. According to the supporters of this theory, corporate management often does not serve the interests of the shareholders, but their own individual short-term financial interests.[27] To this end, the supporters of this solution emphasize that there is a need to increase the influence of shareholders, in order to promote the accountability of corporate governance and corporate transparency. One of the greatest costs of high managerial salaries and the "golden goodbye" executive severance payments is the loss of shareholders' and investors' trust.[28] The main question is which method to use.

As a third alternative, as I have already mentioned in my hypothesis, the regulation of executive's income could be a new approach in labour law. By now it has become obvious that labour law has a major effect on the development of economies and on the operation of market mechanisms. Institutions mutually determine labour law rules on a fundamental level. Labour law regulations have a fundamental impact on the liberties of people, thus the achievement of economic growth goals.

25 Törő 2005.
26 Fried 2005, pp. 21-34.
27 Tibor Várady, 'Kommunista piacgondolkodás', *Beszélő Online*, 2007, pp. 12-17.
28 Fried 2005, pp. 21-34.

29.3.1 The Appearance of Soft Law Solutions in Labour Law

Within the framework of labour law, the application of soft law instruments as a new regulatory instrument of labour law has become increasingly common in recent decades. The application of soft law instruments within the framework of the principles of labour law is necessary for the economics of law to increase effectiveness and economic viability, within labour law, since labour law is in crisis. The main difference between soft law sanctions and binding legal instruments is that there are no official national or international instruments to enforce them, and that the violation of these does not result in legal consequences or state sanctions. However, although they cannot be classified as binding legal instruments, indirectly they have a quasi-legal relevance.[29] Thus, soft law sanctions can indirectly influence the behaviour of market players, individuals, through their moral, ethical, social, and cultural normativity. We could also say that complying with these soft law norms is not mandatory, but strongly recommended, for those who breach them may be socially excluded and publicly shamed. While the moral "regulatory" power of soft law instruments is strong, we have to say that they are not enforceable like classic legal instruments. Soft law instruments belong to the grey zone of law, which means that they cannot be clearly categorized either as binding legal norms or non-legal instruments. Thus, soft law constitutes a kind of transition between the two types of norms. Exactly because of this position, instruments of soft law can be precursors to classic instruments of law by hardening into classic legal instruments later. Both soft law and hard law react to social challenges and demands.[30] Soft law has various advantages over hard law. One of these advantages is that it does not particularly require government bureaucratic intervention, so it can more quickly, reflexively react to the changing environment, avoiding legislative difficulties. These alternative means of regulation have emerged particularly in areas which, because of their complexity, have been met with high resistance. Thus, *soft law* can fill in legal gaps that arise between the situation deemed ideal and the reality.[31]

These new self-regulatory mechanisms of labour law provide more market-friendly solutions, and constitute a bridge between market economy and enforceable government regulations. In scholarly literature, the expression "light touch" is often used, referring to how self-regulatory legal mechanisms affect the hard law.[32] The instruments of soft law build upon the self-regulatory behaviour of market players, offering better solutions than the sanctions directly enforced by the state.

In the last few years we are witnessing dynamic regulatory transnational labour law initiatives. The most important aim of these regulations is to provide a reflexive, respon-

29 Simon Deakin, 'The Contribution of Labour Law to Economic and Human Development', in: Guy Davidov & Brian Langille (eds.), *The Idea of Labour Law*, Oxford University Press, 2011, pp. 156-179.

30 Kun 2016.

31 Attila Kun, *A munkajogi megfelelés ösztönzésének újszerű jogi eszköze* (The New Legal Instrument of Promoting Labour Law Compliance), Budapest, 2014, L'Harmattan Kiadó, pp. 9-19.

32 Deakin 2011, pp. 156-179.

sive new horizon, supporting the idea of Corporate Social Responsible business behaviour. Of course, besides its many advantages, soft law also has disadvantages. Critics of soft law mention negative factors such as its potential destructive impact on legislation, infringements that do not have legal consequences, and that the regulatory framework is often not defined clearly, thereby undermining the regulatory and control powers of the state.[33]

29.3.2 The Market and Labour Law

Due to internationalization and globalization trends, state sanctions are often not sufficiently effective. Therefore, the area of labour law is also characterized by governments allowing a high degree of autonomy in the operation of the companies. On the one hand, this is because these companies are transnational, and their economic influence is constantly increasing. On the other hand, paternalistic regulatory actions of states are not compatible with the ideology of the free market and market economies. *Henry Arthurs* is the first to formulate paradigms concerning the relationship of labour law and soft law. According to *Arthurs*, self-regulatory mechanisms of the market have a far more important role in the creation of market labour relations than government intervention does.[34] *Arthurs*' theory leads us to the three fundamental principles of *Deakin,* formulated with regard to the relationship between the market and labour law. The three claims of *Deakin* sorts the relationship between the market and labour law into three groups. *Deakin*'s three categories are the market regulatory function, the market correctional function, and the market creational function.[35]

The first aspect of labour law according to *Deakin* is the "market regulatory function," according to which labour law is not efficient in the economic sense, since the state intervenes into the relationship between the parties with legal sanctions, in order to enforce the interests of the employees. In this role, labour law is one of the important instruments of the paternalistic state in order to achieve redistribution and social goals. In this respect, the classic role of labour law is regulation, where hard law instruments are used to ensure the equilibrium situation on the market. However, many critics believe that this classical role of labour law may result in loss of efficiency within the relationship of the parties, thereby limiting the effective functioning of market mechanisms.[36]

Contrary to the "market regulatory function," an in respect of the "market correctional function" of labour law, *Deakin* claims that that the state has to intervene to protect

33 Attila Kun, 'A puha jog (soft law) szerepe és hatékonysága a munkajogban – Az új Munka Törvénykönyve apropóján' (The Role and Effectiveness of Soft Law in Labour Law – On the Occasion of the New Labour Code), *Pázmány Law Working Papers*, 2012/41, pp. 6-7.

34 Harry Arthurs, 'Labour Law after Labour', in: Davidov & Langille 2011, pp. 13-30.

35 Deakin 2011, pp. 156-179.

36 Id.

the interest of the market player who is in a weaker bargaining position, if the market cannot carry out this correction itself. Traditional, hard legal sanctions of labour law are needed when the self-regeneration mechanism of the market fails, threatening a greater loss of efficiency than the government intervention itself. In this regulatory function, labour law has a social goal.

According to the third category, with regards to the relationship of labour law and the market, labour law also has the function of "creating a market," In this function, besides hard legal instruments, the new soft law instruments of labour law also appear. Here, *Deakin* points out that the goal of positive legal norms as well as soft law is to create an effective regulatory framework, reacting to the challenges of the social, economic environment. In this context, he emphasizes the need for soft law instruments, as he considers them essential to economic development. *Deakin*, like many other social scientists, raises the question of what we mean by development.[37] In the economic sense, we cannot narrow economic development down to just economic indicators, such as GDP. The GDP shows us a lot about the economic situation of a country, but there are many factors it fails to grasp. One such factor to be evaluated can be the free time of people, that refers to the preference of what is the exchange rate between the time they spend working and free time.[38] Economist *Amartya Sen* also points out that the development of economies should not be interpreted narrowly, emphasizing the importance of human capital as the engine of long-term development. *Hayek* compares economic development to a "discovery procedure," as a process where we do not know what is coming.[39] The basis for all of this is ensuring the liberties of the individual. Here there is a contradiction. The government does the most for economic growth if it does not directly attempt to increase the income of the people, but makes it possible for people to exercise their liberty. At this point we arrive at labour law, as a legal factor in employment determined by the state, that ensures important institutional guarantees.[40]

According to *Sen,* capitalism has to face challenges, such as inequality. The solution for these problems goes beyond the institutional framework of capitalist market economies, and raises the question of what other instruments should be used besides clear government sanctions. According to *Amartya Sen,* people have the right to live the life that they want. However, to ensure this, the state must guarantee basic liberties, such as political, economic, and civil liberties. This way, these liberties become the basis for economic development.[41] By political freedom, we mean the characteristics of the election, the selection of political leaders. That is to say, how democratic the process of selection is,

37 Id.

38 István György Tóth, *Jövedelemeloszlás- A Gazdasági rendszerváltástól az Uniós csatlakozásig* (Income Distribution – From the Economic Regime Change to the EU Accession), Századvég Kiadó, 2005.

39 Friedrich August Von Hayek, 'A verseny mint felfedező folyamat' (Competition as a Discovery Procedure), *Piac és szabadság*, Budapest, 1995, pp. 302-311.

40 Deakin 2011, pp. 156-179.

41 Amartya Sen, *A fejlődés mint szabadság* (Development as Freedom), Európa Könyvkiadó, Budapest, 2003.

whether the right to vote is universal, and whether elected officials are accountable. By economic liberty, we mean that the intervention of the government is not extensive, the legal system is stable, the monetary policy is predictable, foreign trade is not obstructed by trade restrictions, and the exchange rate is stable and easy to predict. Civil liberty includes liberties such as the freedom of association, the independence of courts, the freedom of opinion and religious freedom, and all the liberties that determine what kind of life people would like to live.[42] This is why guaranteeing these rights and their relationship should not be neglected. The differences between executive employees, that also appear in labour law, do not only result in economic differences, but also in differences in fundamental rights, that eventually breach the fundamental guarantee of equality.

29.4 The Income of Executive Employees and the Soft Instruments of Labour Law

Sen states that "The basic law of good business conduct is a little bit like oxygen: we are only concerned about it when it is absent."[43] On the basis of the three functions of labour law mentioned above, *Deakin* wishes to establish an equilibrium between market efficiency and social goals. He seeks to further these goals by incorporating new, innovative legal instruments into the regulatory mechanisms of labour law besides keeping the legal framework, so that it would not hinder the incentives of economic development, but support achieving economic goals. The dramatic increase of the income of executive employees is a market failure, a symptom of various deficiencies of the system. Our main task within a democratic framework of global competition is to make ó executive employers interested in having their income determined in a "moral" way on the long run. In order to achieve this, the companies need to formulate an organizational culture that is present not only formally, but in their everyday activities, and by providing positive incentives, can avoid unnecessarily high salaries and severance payments. In my opinion, this can be the result of a long-term process, which changes basic value judgements.

Due to their moral saturation, soft law instruments can be good instruments to avoid failures of responsible corporate government. With the application of soft law instruments, executive employees do not feel that enforcement mechanisms of the government limit their income within the conditions of the market, while their freedom of contract also remains unrestricted. This way, the moral value and ideal that appreciates a rational

42 Pál Czeglédi, Gazdagok legyünk vagy szabadok? Ez a kérdés? (Shall We Be Rich or Free? That is the Question), *Kommentár*, 2014/5-6.

43 Sen 2003, p. 402.

income after work that has been actually done and is deserved, can be achieved within a democratic and self-regulatory framework.

The perspective in scholarly literature that has been presented so far suggests that companies should become law-abiding on their own, without government intervention. With the development of labour law, an innovative self-regulatory corporate governance mechanism can be a solution for income inequalities that have been the consequence of the increased income of executive employees in the 21st century, causing various social, economic problems all over the world.

29.5 Summary

With this short study, I wanted to demonstrate that labour law as well as economy demonstrate that the social responsibility of corporations is a long-term investment with a concrete economic impact, from which both the company and society can benefit, besides contributing to economic prosperity and growth. Labour law has a primary role in shaping the underlying patterns of behaviour. The demand for a new direction of labour law has emerged as a result of the transformation of traditional company structures and the rapidly changing corporate environment.

Consequently, we can say that parallel to the emergence and expansion of soft law solutions, a deregulatory process has necessarily started in labour law, so that labour law would be able to react ever more flexibly, quickly, and efficiently to the changes in the world of labour. Generally, we can designate as a goal in corporate strategy a self-regulatory mechanism, by which companies can become law-abiding and socially responsible without the instruments of government intervention and enforcement. Here, executive employers have a great responsibility, as they are the ones decisively shaping corporate culture.

With regards to the evaluation of soft law, lawyers as well as economists raise many questions in their analyses with regards to the effectiveness of soft law, and the compatibility of government intervention with the idea of a market economy. It is impossible to clearly predict which direction will be effective in the future, as this depends on a number of external influences and the sum of individual decisions. Nonetheless, we can say that the findings of the new dimension of labour law have to be extended to the assessment of the economy, so that corporate executives can become responsible leaders, contributing to the egalitarian distribution of income.