Rent-seeking in a unionised monopoly*

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Abstract. A unionised monopoly firm, benefiting from some kind of anti-competitive regulation, and its corresponding trade union have a common interest in spending resources to protect the monopoly rents created by the regulation. In the present paper, a situation in which the unionised monopoly is challenged by a consumer organisation fighting for deregulation is analysed as a standard Tullock rent-seeking contest. With unequal sharing of monopoly rents, the free-riding incentives among the rent-defending players turn out to be overwhelming, in the sense that the unique Nash equilibrium is characterised by zero effort contribution by the player with the lower valuation of the contested prize. This implies that being “strong”, in terms of bargaining strength, is not necessarily an advantage for neither player in a unionised monopoly that is threatened by deregulation.

Key words: contests, rent-seeking, trade unions

JEL classification: D72, J51, L43

1. Introduction

Rent-seeking effort undertaken by firms in order to obtain, or protect, favourable market positions has long been regarded as an integral part of a modern economy. The literature on rent-seeking activities by firms, which was pioneered by Tullock (1967), Krueger (1974) and Posner (1975), highlights the important insight that the social costs of monopolies created by restrictive regulations are likely to be higher than the “standard” deadweight loss.

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1 See Nitzan (1994) for a survey of the theory of rent-seeking.
In an important paper, Ellingsen (1991) broadens the scope of traditional rent-seeking theory by including rent-seeking expenditures by consumers. Indeed, he shows that consumer lobbying against potential and existing monopolies is very likely to be socially beneficial. Other papers analysing consumer participation in rent-seeking contests include Fabella (1993, 1995) and Rama (1997).

In a more general setting, though, it is also natural to include trade unions as independent players in rent-seeking games. Empirically, it is reasonably well documented that imperfect competition in product markets is a major source of rent extraction by unionised labour (see e.g. Rose, 1987; Christophides and Oswald, 1992). Thus, it could be very much in the interest of trade unions to engage in lobbying, or other kinds of actions, directed against regulatory authorities in order to create or preserve various types of market regulations. These kinds of actions are also frequently observed in most industrialised countries. With very few exceptions, though, rent-seeking expenditure by organised labour has not received much attention in the literature.

Following Ellingsen (1991), we can distinguish between two different types of rent-seeking: Rent-seeking by potential producers for a monopoly position, and rent-seeking by an existing monopolist to defend his monopoly position. The effect of unionised labour in rent-seeking contests of the former kind is extensively analysed by Rama (1997), the main results being that the presence of trade unions makes monopolisation less attractive to firms, and more harmful to consumers. Thus, rent-seeking expenditures by firms are reduced, and the probability of regulation is reduced, compared to the non-union case.

In this paper we concentrate on the latter type of rent-seeking contests. As observed by Ellingsen (1991), in most cases consumers launch their campaigns against existing monopolies. Furthermore, trade unions that are already favoured by existing regulations are probably more likely to play an active part in rent-seeking contests.

Our focus is directed towards an existing unionised monopoly that is favoured by some kind of anti-competitive regulation, e.g. protection from international competition. Applying the lottery model of Tullock (1980) we then analyse a rent-seeking contest between the rent-defending players, i.e. the protected firm and its trade union, and an organisation representing consumers’ interests. This is a contest between a group of agents (the firm and the union) on one side, and an individual agent (the consumer group) on the other. In this respect it is a special application of a more general group rent-seeking contest (see e.g. Katz, Nitzan and Rosenberg, 1990; Nitzan, 1991; Lee, 1995).

An important feature of this particular contest is the prevalence of free-riding incentives within the rent-defending group. If the rent-defending players win the contest, and regulation is upheld, the “prize” is shared between the firm and the union on the basis of relative bargaining strength in wage negotiations. However, these prize-sharing “rules” are exogenous to the contest itself, and thus, both rent-defending players have strong incentives to free-ride in the contest by leaving

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2 Contrary to the present paper, Rama (1997) does not consider trade unions as independent contest participants.