# TOC- Enforcement PIC

## 1NC

#### CP Text: Aff actor should require employers to pay a living wage, but shouldn’t punish employers who don’t pay a living wage.

#### Solves the aff because firms will still be incentivized to participate in the formal sector- net benefit is greater economic output and lower unemployment because small firms are able to operate without increased labor costs

#### ROGERS AND SWINNERTON 04 [Carol Ann Roger (Econ professor at Georgetown) and Kenneth A. Swinnerton (U.S. Dept of Labor, Bureau of International Labor Affairs), “A Model of Informal Sector Labor Markets” December 3, 2004, DDA]

A small and growing literature questions these presumptions, by showing that formal firms may voluntarily choose formality so as to receive some positive benefit, and that the informal sector has some intrinsic value to the economy.2 Alec R. Levenson and William F. Maloney (1998) develop a model in which allowing informal operation encourages the start up of new business. Over time, the most productive of these new firms grow and the least productive shut down. Growing firms evolve into formal firms as the benefits of formality - - such as access to various legal protections for increasingly complex business relationships - - become more important to them. Yoshiaki Azuma and Herschel Grossman (2002) develop a model in which allowing an informal sector to opt out of paying taxes may increase government revenues and aggregate output. In their model, there is a distribution of productivity across firms and each firm has strictly private information about its own productivity. A high tax coupled with the provision of government services only to firms that choose to pay can be Pareto superior to a lower tax forcibly levied on all firms. Our paper expands this literature by showing that when labor regulation is coupled with voluntary compliance that allows firms to self-select without penalty into the formal and informal sectors, this can lead to Pareto-improving market outcomes. We work with a simple search model. It is a known feature of search (e.g., Kenneth A. Swinnerton, 1996; Gerard J. van der Berg, 2003) and other models giving firms some degree of labor-market monopsony power (e.g., George Stigler, 1946; V. Bhaskar and Theodore To, 1999), that the imposition of universally enforced labor-cost-increasing regulation can have beneficial effects on aggregate welfare. What has yet to be clarified is the fact that there are instances when allowing firms to choose—without penalty—about whether or not to comply with this regulation can yield an even greater benefit. In our model, firms differ in productivity, and there are diminishing returns to labor. Random search in the labor market by homogeneous workers implies that in the absence of any labor standards the most productive firms face chronic labor shortages. The government sets labor standards and publicizes the identity of firms that choose to comply with the standards. The government does nothing to penalize firms that do not comply. This combination of labor standards and an “enforcement policy” of identifying the firms that comply can raise aggregate output and employment through two channels. First, the most productive firms will choose to comply, because doing so relieves the labor shortage they face. Once they have been identified as formal firms, workers will look for jobs with them first. This will increase the average productivity of the workforce, as a greater number of workers will go to the more productive firms. Second, the enforcement policy allows less productive firms, which do not face labor shortages, to opt out of compliance. For these firms, the increased labor costs associated with compliance with labor standards would have the typical neoclassical effect of reducing employment and output. These firms provide “fall-back” jobs for searchers who have yet to find formal- sector jobs. Allowing the terms of this employment to be less desirable than at formal- sector firms is better from an aggregate standpoint than regulating the informal sector away by enforcing 100% compliance with labor standards.