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Deregulation of dismissal law and unjust dismissal in Korea

Joonmo Cho^{a,*}, Kyu-Young Lee^b

^a *Sungkyunkwan University, Seoul, Republic of Korea*

^b *Department of Economics, University of Kassel, Kassel, Germany*

Abstract

Using data of Korean court cases, related to the unjust dismissal claims between 1987 and 2000, this paper examines how the deregulation of Korean dismissal law in 1998 affects the incidence of unjust dismissals. Logit estimation to identify the determinants of unjust dismissal rate in Korea shows that deregulation of the dismissal law led to a higher incidence of unjust dismissals. Reasons for this empirical result were explored. These included misinterpretations of the law on the part of employers, due to the disorderly process of legislation and poor coordination in industrial relations, changes in court's adjudication criteria influenced by socio-economic factors, and finally misalignment of law and economic conditions.

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1. Introduction

The legal rule governing unjust dismissal is an important component of labor law in any country. It is difficult to compare the scope of legitimate dismissals in a particular country with that of other countries, because comparative studies on labor law require proper knowledge of historical background and socio-economic factors.

* Corresponding author.

E-mail addresses: trustcho@skku.edu (J. Cho), sherrleeky@hotmail.com (K.-Y. Lee).

The level of employment protection in Korea had been very strong prior to the 1990s. The Korean Labor Standards Act (hereafter LSA) had limited the power of employers to break employment contracts at will, and has stipulated that an employer can dismiss an employee only with justifiable reason.

In 1997, Korea experienced a financial crisis that necessitated a “bail out” by the IMF. Due to pressure from the IMF, the new dismissal law was legislated in 20 February 1998. The adoption of this new law intended to relax pre-existing limitations on employers’ use of discretion in relation to employment adjustment (IMF, 2004). This legislative change certainly allowed for increased flexibility in the Korean labor market, which could in some instances “even reduce job security.” Employers fully supported this trend in deregulation, argued that greater freedom to making employment adjustments creates more jobs, and thus eventually benefits employees.¹ As expected, labor unions strenuously opposed this trend, and argued that due to this legal transition, unjust dismissals would become more prevalent and the labor market more unstable.

Regarding the regulation or deregulation effects of employment protection, there are two-key OECD studies. In the first study (OECD, 1996), rank correlations are provided between job turnover, unemployment inflow/outflows and long-term unemployment. They are not statistically significant except in the case of long-term unemployment and unemployment inflows. The second study (OECD, 1999) confirmed the results of the first study with a visible and significant improvement for the overall measure of employment protection. Furthermore, Addison and Teixeira (2003) summarized the previous literatures on the effect of employment protection on the labor market. They suggested that the employment protection seemed to work in predicted manners to reduce both flows into and out of employment and to increase jobless duration.

This study empirically analyzes how the deregulation of dismissal law in 1998 has affected employers’ unjust dismissals, using dismissal court cases since 1987. The *ceteris paribus* analysis controlling personal, institutional and socio-economic factors assesses how this legal change affected the incidence of employers’ unjust dismissals.

Various aspects in legislating dismissal law cause the trend in increased unjust dismissals. First, the disorderly process of law-making may result in design failure, which is to be seen in vague standards that fail to establish clearly the scope of legitimate dismissals (Büchtemann & Walwei, 1996) and thereby give rise to employers’ erroneous interpretations. This may cause a trend of increased unjust dismissals. Second, the court itself may change the substance of applicable law when considering the societal and economic environment in fixing the terms of the new dismissal law. This may cause a new trend of unjust dismissals. Third, the misfit between dismissal law and economic conditions could be seen as a reason for increase in the rate of unjust dismissals. The new dismissal law would have enhanced flexibility to a certain degree in a particular historical moment like the 1998 financial crisis. However, it may cease to do so when economic circumstances change. For instance, more

¹ Employer’s groups do not always advocate liberalized dismissal law. In contrast to Korean employer’s groups, US employer’s groups supported the adoption of a more protective dismissal law. Krueger (1991) explained the intriguing process of US unjust dismissal legislation and suggested that US employer groups, responding to the threat of large and variable damage awards imposed by the judicial system, eventually support unjust dismissal legislation in order to clearly define property rights, reduce uncertainty, and limit employer liability.

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