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On-Demand Employment, Worker Misclassification, and Labor Standards

Abstract

[Excerpt] On-demand platform work, like other forms of contingent and temporary employment, destabilizes industries, undermines worker protections and living standards, and significantly contributes to wealth and income inequality.

Keywords

on-demand workers, gig workers, working conditions, income inequality

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Comments

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On-Demand Employment, Worker Misclassification, and Labor Standards

Cornell ILR
Worker Institute
Impact Brief

Fred B. Kotler

On-demand platform work, like other forms of contingent and temporary employment, destabilizes industries, undermines worker protections and living standards, and significantly contributes to wealth and income inequality.

A recent report from the Worker Institute, “On-Demand Platform Workers in New York State: The Challenges for Public Policy,” includes results from a survey of on-demand platform workers carried out in the summer and fall of 2018. This report is available online at <https://www.ilr.cornell.edu/node/293371>.

The issues raised by the workers in our survey are frighteningly similar to those faced by American workers in the early 20th century. Those workers found themselves trapped in jobs without guarantees of minimum wages or maximum hours, without hope of payment in case of death or dismemberment or even protections against unsafe working conditions. It would take most American workers over thirty years before they gained any sort of basic workplace rights.

From early Progressive era reforms through the New Deal reforms of the 1930s, workers slowly gained these rights and others, such as the right to organize collectively into unions. It would take another thirty to forty years or more before the federal government passed anti-discrimination laws and that long or longer until originally excluded groups such as public employees, farmworkers and household workers began to gain similar rights on a state-by-state basis.

New York state now has an opportunity to shape new laws so that on-demand platform workers will not have to wait thirty years or more before they too gain what we consider today to be basic workplace rights.

On-demand platform employment is but the latest demonstration of destabilizing changes in work, conditions, and labor markets that have developed since the 1980s. Companies have systematically shifted or eliminated jobs formerly done in-house through subcontracting, reliance on third parties, contingent and temporary work contracts, and abuse of “independent contractor” status.ⁱ As with on-demand platform work, the industries most impacted are: transportation, trucking, construction, home health care, janitorial, hospitality, restaurant, household services, clerical, and retail services.

Correct classification of workers is a core issue for labor standards in the “on-demand” economy.

On-demand industry practice, represented by such companies as Uber, Lyft, Postmates, and TaskRabbit, is to hire and dispatch workers as “independent contractors.” These workers are, however, not true “independent contractors”; they are not in business for themselves and cannot freely negotiate employment terms. The Worker Institute’s survey as well as documents obtained through litigation have shown that they are instead subject to employer control over pay, safety, access to information, performance monitoring and evaluation, and discipline and discharge.

This type of misclassification may be mistaken or deliberate. Some employers may mistakenly misclassify workers because the criteria for determining employee status are complicated and unclear. Other employers deliberately misclassify their workers as “independent contractors” as a strategy to cut labor costs and gain an unfair competitive advantage. This shifts workers compensation and unemployment insurance premium costs onto law-abiding businesses. Government, at all levels, is deprived of significant revenues through non-reporting or under-reporting of taxes. And on-demand platform workers are left holding the bag.

In an employer–employee relationship, the employer must withhold income taxes, withhold and pay Social Security and Medicare taxes, pay the unemployment insurance tax on wages paid, provide workers' compensation insurance, pay minimum wage and overtime wages, and include employees in benefits plans.

Employers are not generally obligated to make these payments to, or on behalf of, independent contractors. They may therefore have a strong incentive to avoid having their workers classified as “employees.” Hiring independent contractors instead of “employees” can mean a 30% reduction in payroll and related costs. “Employees” receive unemployment and workers' compensation benefits and are typically protected by a broad range spectrum of federal, state, and local legislation affecting wages, health and safety, health benefits, the right to organize, anti-discrimination, family and medical leave, and pension security.ⁱⁱ

“Independent contractors” are generally excluded from these social safety net programs and protective workforce legislation: they are “on their own.”

A study of several states' insurance funds conducted for the U.S. Department of Laborⁱⁱⁱ concluded that employers will assume the risks associated with misclassification to gain a competitive advantage by not paying workers' compensation premiums — risks they would not likely take for unemployment insurance cost savings alone.

Misclassifying workers as independent contractors reduces liability risks for employers. In an employer–employee relationship, employers are liable for the torts committed by their employees within the scope of their employment under the doctrine of respondeat superior. Employers are, however, not liable for the torts of independent contractors.

The impact of worker misclassification on New York State funds and tax revenues is severe.

Cornell ILR reported on worker misclassification in early 2007. That earlier study, based on audits performed by the NYS Department of Labor Unemployment Insurance Division during the four-year period 2002–05, estimated that

- nearly 40,000 employers each year mistakenly or intentionally misclassified workers;
- 10.3% of the state's private sector workers were misclassified each year including 14.8% of the construction workforce; and that
- \$4.3 billion of unemployment insurance taxable wages were underreported for the audited industries during the four-year period.^{iv}

The use of independent contractor status, by one estimate, grew nationally by 40% between 2005 – 2015.^v The New York State Joint Enforcement Task Force reported in 2015 that,

- Since August 2007 enforcement and data sharing activities have identified nearly 140,000 instances of employee misclassification and discovered nearly \$2.1 billion in unreported wages.^{vi}

The California Division of Labor and Enforcement Standards estimates that worker misclassification costs that state \$7 billion annually with “increased reliance on the public safety net by workers... denied access to work-based protections.”^{vii}



New York’s regulatory structure does not now provide the necessary level of oversight to curb abuse in the on-demand economy so to protect worker, business, and taxpayer interests.

New York State has no uniform criteria for determining “employee” status. A worker may be adjudged to be an “employee” under one statute but an “independent contractor” under another.

Decisions by one agency do not necessarily bind another and agencies are not bound by prior rulings. Agency decisions may be overturned by courts that reach opposite conclusions based on the same or similar facts.

The current structure for enforcing labor standards is complex and confusing that a) often leaves businesses and workers uncertain of proper classification short of costly, extensive litigation; and b) provides wide latitude for abuse by allowing employers to structure and define work to avoid a determination of “employee” status.

New York courts and administrative agencies apply different versions of the “common law test” to determine worker status for claims involving unemployment insurance, workers compensation, wage and hour violations and taxation.

The complex, multifactor common law tests for determining employee status are flawed because they provide insufficient direction to law-abiding businesses and workers pending judicial and administrative intervention; lack the clarity necessary to mitigate mistaken and intentional workers misclassification; facilitate costly and time-consuming litigation; lead to inconsistent outcomes; and do not offer the level of regulatory oversight necessary to protect worker, business and taxpayer interests.

These consequences of misclassification expand exponentially for on-demand platform workers, since the nation’s courts have now made many conflicting decisions about their classification status.

Replacing the Common Law test with the ABC test would help curb misclassification abuse in the on-demand platform industry, as it has in other industries and states.

Sixteen states, including New York, have changed how employment relationships are defined and most states have adopted some form of the ABC test that presumes employee status. These states are:

Delaware; Illinois; Kansas; Maine; Maryland; Massachusetts; Minnesota; Nebraska; New Hampshire; New Jersey; New Mexico; New York; Oregon; Pennsylvania; Utah; and Washington.^{viii}

The California Supreme Court recently [April 2018] rejected the Common Law test in favor of the ABC test. Legislation is now pending in the California Assembly to codify the Court’s decision.

New York’s statutory reforms, as with those of several other states, are industry specific: they are directed at those industries – construction and trucking – where intentional misclassification has, for several years, been particularly severe.

New York State’s Fair Play statutes, enacted for the construction and trucking industries, use the alternative ABC test, the clearest and most sharply defined legal test for determining employee status. These provide the model for new legislation to curb misclassification abuse in the on-demand industry.

POLICY RECOMMENDATION

Provide on-demand workers with statutory rights and protections in the following areas:

- ▶ unemployment insurance
 - ▶ workers compensation coverage
 - ▶ wage and hour protection
 - ▶ family and medical leave
 - ▶ workplace health and safety
 - ▶ withholding of taxes
 - ▶ pension security
 - ▶ anti-discrimination
 - ▶ right to organize and collectively bargain
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Endnotes

- i. Weil, David. "How to Make Employment Fair in an Age of Contracting and Temp Work", *Harvard Business Review*, March 24, 2017; available at: <https://hbr.org/2017/03/making-employment-a-fair-deal-in-the-age-of-contracting-subcontracting-and-temp-work>; also see: Weil, David, "Lots of Employees Get Misclassified as Contractors. Here's Why It Matters," *Harvard Business Review*, July 5, 2017; available at: <https://hbr.org/2017/07/lots-of-employees-get-misclassified-as-contractors-heres-why-it-matters>; Weil, David and Tanya Goldman, "Labor Standards, the Fissured Workplace, and the On-Demand Economy," *Perspectives on Work*, 2016; available at: http://www.fissuredworkplace.net/assets/Weil_Goldman.pdf.
- ii. See Ruckelhaus, Catherine and Celedih Gao. "Independent Contractor Misclassification Imposes Huge Costs on Workers and Federal and State Treasuries." National Employment Law Project, Fact Sheet, September 2017, pp.1; available at: <https://www.nelp.org/publication/independent-contractor-misclassification-imposes-huge-costs-on-workers-and-federal-and-state-treasuries-update-2017/>; Some estimates run as high as 40%: see *The Misclassification of Employees as Independent Contractors*, Department of Professional Employees, AFL-CIO, Fact Sheet 2016; available at: <https://dpeaflcio.org/programs-publications/issue-fact-sheets/misclassification-of-employees-as-independent-contractors/>
- The US Department of Labor Bureau of Labor Statistics reported the following in June 2018:
- Employer costs for employee compensation averaged \$36.22 per hour worked in June 2018... Wages and salaries averaged \$24.72 per hour worked and accounted for 68.3 percent of these costs, while benefit costs averaged \$11.50 and accounted for the remaining 31.7 percent. Total employer compensation costs for private industry workers averaged \$34.19 per hour worked. Total employer compensation costs for state and local government workers averaged \$49.23 per hour worked.
- Bureau of Labor Statistics, "Employer Costs for Employee Compensation – September 2018." U.S. Department of Labor, December 14, 2018; available at <https://www.bls.gov/news.release/pdf/ecec.pdf>.
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- v. Weil, David. "Lots of Employees Get Misclassified as Contractors. Here's Why It Matters," *Harvard Business Review*, July 5, 2017; available at: <https://hbr.org/2017/07/lots-of-employees-get-misclassified-as-contractors-heres-why-it-matters>
- vi. New York State Department of Labor et al., "Annual Report of the Joint Enforcement Task Force on Employee Misclassification." February, 2015, pp.3, Annual Report of the Joint Enforcement Task Force on Employee Misclassification: To Honorable Andrew M. Cuomo, Governor, State of New York, pp. 3; available at: <https://labor.ny.gov/agencyinfo/annualrpt.shtm>.
- The Kogod Tax Policy Center at American University reported in 2016 that its survey results showed that "more than 60% of respondents who worked for an on-demand platform company in 2015 reported that they did not receive a Form 1099-K or Form 1099-MISC for their on-demand platform, which likely means the IRS didn't either." Caroline Bruckner, *Shortchanged: The Tax Compliance Challenges of Small Business Operators Driving the On-Demand Platform Economy*, Kogod School of Business, Kogod Tax Policy Center, May 2016, pp. 15. Available at: <https://www.american.edu/kogod/news/Shortchanged.cfm>.
- vii. State of California, Department of Industrial Relations, https://www.dir.ca.gov/dlse/worker_misclassification.html.
- viii. Deknatel, Anna and Lauen Hoff-Downing. "ABC on the Books and in the Courts: An Analysis of Recent Independent Contractor and Misclassification Statutes." *University of Pennsylvania Journal of Law and Social Change*, vol. 53, 2015. For a full list of statutes, see fn 11 at pp.3.

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ILR Worker Institute

The Worker Institute at Cornell, an institute of the ILR School, engages in research and education on contemporary labor issues, to generate innovative thinking and solutions to problems related to work, economy and society. The institute brings together researchers, educators and students with practitioners in labor, business and policymaking to confront growing economic and social inequalities, in the interests of working people and their families. A core value of The Worker Institute is that worker rights and collective representation are vital to a fair economy, robust democracy and just society.

