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## A Proposal for Modernizing Labor Laws for Twenty-First-Century Work: The “Independent Worker”

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# A Proposal for Modernizing Labor Laws for Twenty-First-Century Work: The “Independent Worker”

*New and emerging types* of work relationships in the online gig economy have raised new questions as to whether online gig workers meet the legal definition of “employee.” Online gig workers provide on-demand services to customers to whom they are matched through online technology and apps. Examples of services they provide include cleaning houses, doing repairs, shopping, cooking, driving, and landscaping. In some aspects, online gig economy workers resemble traditional employees: they provide services that are integral to the businesses for which they work, and the businesses control some aspects of how much they work and how much they charge. At the same time, the workers can choose when and whether to work and can work for multiple businesses at once.

In the United States the employee designation is important because labor and employment laws confer workplace benefits and protections only to those workers who meet the legal definition of employee, as compared to an independent contractor. These benefits range from collective bargaining to civil rights protections. However, as highlighted in recent court cases, there can be uncertainty in existing laws and regulations over whether workers in the online gig economy qualify as employees. The uncertainty arises because today’s laws do not take into account the nature and characteristics of this new work relationship. The legal uncertainty that these workers and businesses face can lead to inefficiencies in the labor market, may stifle innovation, and could result in costly legal battles over whether workers are appropriately classified and thus protected.

In a new Hamilton Project discussion paper, Seth Harris of Cornell University and Alan Krueger of Princeton University propose that, to address this legal uncertainty and to enhance worker protections, Congress, and state legislatures where applicable, enact legislation to create a new legal category of workers, called “independent workers.” These workers would occupy a middle ground between the existing categories of employee and independent contractor; the latter typically are workers who provide goods and services to multiple businesses without the expectation of a lasting work relationship. Based on a set of governing principles to guide the assignment of benefits and protections to independent workers, the proposal would enable businesses to provide benefits and protections that employees currently receive without fully assuming the legal costs and risks of becoming an employer. Such benefits and protections include the freedom to organize and collectively bargain, the ability to pool (e.g., a suite of employer-provided benefits such as health insurance and retirement accounts; income and payroll tax withholding), civil rights protections, and an opt-in program for workers’ compensation insurance. The authors suggest that other benefits should be limited to employees, including overtime benefits and protections, unemployment insurance, and a guaranteed minimum wage protection. Workers in the online gig economy would be the primary candidates for this new classification, but other workers, such as taxi drivers and direct sales workers, may also be affected.

## The Challenge

The existing legal framework in the United States recognizes two statuses for workers: employees and independent contractors. This dichotomy is based on the expectation of a traditional long-lasting employment relationship in which the employee is reliant on the employer for her livelihood. Employment and labor law have evolved to provide protections for employees, such as minimum wage and overtime pay, protection against workplace and labor market discrimination, and unemployment and workers’ compensation insurance. Independent contractors, however, are not reliant on one client for their livelihood and have freedom to choose how and whether to perform work for a client. As such, they generally do not receive the benefits and protections of employees.

In their proposal Harris and Krueger point out that new forms of work have emerged that do not fit neatly into either the employee or independent contractor classification. The most recent, and highly publicized, of this new form of work appears in the online gig economy, in which workers use an Internet-based app created by a business (which Harris and Krueger call an intermediary) to find customers for short-term personal tasks; an example is drivers finding ride-seekers. Much like an independent contractor, the worker can determine whether to work, how many hours to work, and when to work. But much like an employee, the online gig economy worker is typically integral to the business of the intermediary, and the intermediary often controls aspects of the work. The authors maintain that these relationships defy classification under existing employment, labor, and tax laws.

## Legal Uncertainty

The authors explain that existing federal and state laws threaten to inconsistently apply employee or independent contractor status to gig economy workers. The relevant statutes apply different factors, depending on the core purpose, to determine the legal status of a worker. The authors also argue that the statutes, accompanying regulations, and judicial interpretations about how much weight to give each factor lack clarity. For example, the Department of Labor applies what is called an “economic realities” test that focuses on the economic relationship between a worker and an employer, examining factors such as whether a worker provides services that are integral to the employer’s business. In contrast, the Internal Revenue Service uses a twenty-factor test to define an employee and thereby her tax-withholding obligations. It is (at least hypothetically) possible for a worker to be classified as an employee under the economic realities test, which would entitle her to the minimum wage and other mandates, but not under the tax law, which would free the employer from remitting payroll taxes on behalf of the worker. A complicating feature of these tests is that they are collections of factors for consideration rather than clear thresholds or requirements, so a worker identified as falling under one category in one case may find her status changed in subsequent litigation. Varying interpretations across jurisdictions compound the uncertainty caused by the diverse legal framework.

## Labor Market Inefficiency

Harris and Krueger argue that worker classification ambiguity is inefficient both for workers, who do not know which benefits and protections they qualify for, and for intermediaries, who face different sets of costs and obligations depending on how their workers are categorized. The ambiguity of the tests for workers who may not fit into either category creates a barrier to the continuation of relationships that can be beneficial to all parties involved. Workers who are classified as independent contractors do not always have the means to secure many of the protections and benefits that are available to employees. Moreover, they may be able to obtain such benefits, like health insurance, only at a higher cost since employers often have stronger bargaining power with the firms that sell benefits.

The authors point out that some businesses may also classify (or misclassify) their employees as independent contractors to avoid providing benefits and protections. This opportunity for regulatory arbitrage gives businesses that reorganize their work in an effort to save on labor costs an advantage over their competitors, leaving both law-abiding businesses and workers worse off. Specifically in the online gig economy, the authors point to the possibility that intermediaries may gain from, but not pay for, the benefits provided by other companies when they hire workers who hold primary jobs.

## A New Approach

To promote legal certainty and enhance economic efficiency, Harris and Krueger propose that Congress and state legislatures, where appropriate, enact legislation to define and establish a third legal category of workers, which they call “independent workers.” These workers would occupy a specific part of the gray area in the employee–independent contractor dichotomy. To identify independent workers and to guide the determination of the benefits and protections for which they would qualify, Harris and Krueger offer three guiding principles:

1. **Immeasurability of work hours.** The worker classification system should recognize that, in these relationships, the line between work and nonwork can be impossible to measure, and that some work involves hours that cannot be apportioned to a company and measured for the purpose of assigning benefits.
2. **Neutrality.** The worker classification system should ensure that businesses do not have an incentive to organize themselves to fit a certain status to gain an unfair advantage over other employers.
3. **Efficiency.** The worker classification system should enable workers and businesses to maximize the joint benefits that their relationships produce.

## Identifying Independent Workers in the Online Gig Economy

Harris and Krueger contend that independent workers in the online gig economy are those who operate in a triangular relationship with a business (i.e., an intermediary) and customers. Typically, they use a communications channel, such as an app, created by an intermediary to identify customers for their service. Independent workers can work for multiple intermediaries at once, can choose when and whether to work, and will not necessarily develop dependent, deep, extensive, or long-lasting relationships with their employers. At the same time, independent workers may need to comply with certain requirements from the intermediaries, such as criminal background checks, and intermediaries may set the price for the service provided by independent workers. The

intermediary typically receives a predetermined percentage of the fee paid by the customer, via the intermediary, to the independent worker.

Importantly, independent workers are characterized by the immeasurability of their work hours. Most obviously, as illustrated in box 1, because an independent worker can work for multiple intermediaries, it is not always possible to apportion work hours to one intermediary. Also, Harris and Krueger argue that the boundary between work and nonwork can be indeterminate, since independent workers may spend time waiting to engage in work activities and may view that time as hours spent working.

## New Benefits and Protections for Independent Workers

In their policy proposal, Harris and Krueger recommend requiring (or allowing) intermediaries to provide the following benefits and protections to independent workers. Notably, the proposed benefits and protections take into account Harris and Krueger’s guiding principles—immeasurability of work hours, neutrality, and efficiency—and are consistent with their view that independent worker status should fall between the employee and independent contractor classifications.

### BOX 1.

#### Immeasurability of Work Hours: A Hypothetical Example

Suppose a driver has apps for two different intermediaries, iRide and eFood, open on separate electronic devices. She is waiting for a customer who is seeking a ride or someone who needs a food delivery. Two questions arise: (1) Should the driver be compensated for this waiting time? (2) And, if so, who should compensate her?

Under the authors’ interpretation of the Fair Labor Standards Act (FLSA), whether the driver’s waiting time constitutes compensable working hours depends on whether the driver is “waiting to be engaged” or “engaged to wait.” If the driver has enough time and can use the waiting time as she wishes, she is waiting to be engaged and does not qualify to be paid for the waiting time. If she is engaged to wait, however, the employer controls her movement during that time and she is entitled to compensation. In the context of iRide and eFood, Harris and Krueger argue that the driver is waiting to be engaged, in part because she can turn off the apps at will and is not obliged to either pick up a customer or deliver food even with the apps turned on.

But even if she were deemed to be engaged to wait, the question then becomes whether iRide, eFood, or both should pay the worker for this waiting time. The authors believe that existing law does not answer this question because there is no analogy in the employer–employee relationship to a driver simultaneously available for different services with different employers. This situation would not count as joint employment since iRide and eFood are competitors for the driver’s services, rather than co-employers. In the current legal and regulatory framework, the authors contend that the best legal answer seems to be that there is no good answer. The authors’ proposal recognizes this immeasurability of work hours in establishing a new legal and regulatory framework for independent workers.

## Freedom to Organize and Collectively Bargain

The authors propose amending antitrust laws to allow independent workers to organize to negotiate with intermediaries and customers. The ability to organize would increase the scope for independent workers to bargain with their intermediaries over the terms and conditions of their work. The authors highlight how this protection would make independent worker status more neutral with respect to employee status because employers would not face an incentive to misclassify employees as independent workers to avoid collective bargaining situations. The authors hold the view that federal antitrust law is the main legal challenge to providing this benefit to independent workers so they propose that Congress craft an exemption from relevant antitrust laws for independent workers. Harris and Krueger note that covering independent workers under the National Labor Relations Act would provide an alternative way to secure collective bargaining rights.

## Ability to Pool

Harris and Krueger emphasize that an intermediary could provide to independent workers a range of employer-provided benefits at a lower cost and higher quality than the workers could obtain on their own in the private market. Such benefits could include insurance services, tax preparation assistance, auto insurance, disability insurance, health insurance, banking and savings products, retirement products, and liability insurance. Pricing efficiencies in the provision of these benefits arise because there are important economies of scale and risk diversification benefits from jointly administering benefits to a pool of independent workers rather than to individual workers separately.

To enable provision of these benefits, Harris and Krueger propose that intermediaries' provision not lead to classification of their relationships with independent workers as employment relationships. In the current legal environment, intermediaries are hesitant to provide benefits like health insurance due to the risk that courts would consider their workers to be employees and either mandates or penalties could be the result. This clarification would also ensure neutrality with employees as independent workers would have better benefits than would be available to independent contractors, although it would preserve the advantages that employees and employers have under existing laws.

## Civil Rights Protections

Harris and Krueger propose modifying federal employment discrimination laws to cover independent workers. While employees benefit from a variety of protections provided through federal antidiscrimination statutes, independent contractors do not have access to the same protections. For example, independent contractors cannot bring federal claims if intermediaries discriminate on the basis of sex, disability, or age. The authors argue that providing protection against workplace discrimination would help ensure neutrality between employment relationships and independent worker relationships while providing more-expansive protection against discriminatory acts in the workplace and labor market.

## Tax Withholding and FICA Contributions

Harris and Krueger would require intermediaries to provide tax-withholding services, arguing that such a benefit would help ensure neutrality since employees are already provided with tax withholding through their employers. Employers withhold taxes as an advance payment toward an employee's final tax liability, and the IRS refunds any excess. This withholding helps employees to smooth their after-tax income throughout the year, and enables them to avoid the quarterly payments and relevant paperwork filed by other workers. Tax withholding also increases tax compliance, leading to greater revenues for the federal and state governments. Given economies of scale, tax withholding by intermediaries would be more economically efficient and would reduce the administrative burden of paying income and social insurance taxes for workers.

## Roadmap

- Congress and, where necessary, state legislatures will pass legislation to create a third worker classification category between “employee” and “independent contractor,” to be called “independent worker.”
  - The legislative framework would reflect the following guiding principles:
    - **Immeasurability of hours.** The worker classification system should recognize that the line between work and nonwork can be impossible to measure.
    - **Neutrality.** The worker classification system should ensure that businesses do not have an incentive to organize themselves to fit their workers into one status over another.
    - **Efficiency.** Businesses and workers should maximize the joint benefits in their relationship.
  - This category would encompass workers in both online gig economy jobs and more-traditional jobs.
  - Specific federal statutes that the legislation would amend include the Fair Labor Standards Act (FLSA) and the Civil Rights Act of 1964.
  - States will amend employment, labor, and tax laws to follow federal law changes and to address any changes in state antitrust and workers' compensation laws.
- Congress and, where appropriate, state legislatures will apply the guiding principles to assign new benefits and protections to independent workers.
  - Independent workers will have access to organizing and collective bargaining, various forms of insurance, civil rights protections, employer-provided benefits, and tax withholding.
    - Businesses that do not contribute to health insurance for their independent workers will contribute an earnings tax of around five percent of net earnings.
  - Because their hours cannot be readily measured, the legislative framework will not require independent workers to receive workers' compensation, overtime payments, or a minimum wage guarantee.

In addition, to maintain neutrality with employee status Harris and Krueger propose that intermediaries pay half of independent workers' contributions toward the Federal Insurance Contributions Act (FICA) payroll taxes for Social Security and Medicare. The burden of these taxes is likely to shift to workers in the form of lower net wages, just as they do for regular employees. Through this aspect of the proposal, employees and independent workers would be able to compare their pretax compensation more easily.

## Learn More about This Proposal

This policy brief is based on a discussion paper from The Hamilton Project, “A Proposal for Modernizing Labor Laws for Twenty-First-Century Work: The ‘Independent Worker,’” which was authored by

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### Other Benefits and Protections for Independent Workers

While Harris and Krueger propose a variety of new benefits and protections for independent workers, the authors’ guiding principles would suggest that independent workers be treated similarly to independent contractors with regard to some other benefits. In particular, the immeasurability of work hours suggests that benefits that depend on the number of hours worked would be infeasible to extend to independent workers. With respect to other benefits, Harris and Krueger propose that independent workers be treated differently from both employees and independent contractors.

#### *Overtime and Minimum Wage*

Harris and Krueger argue that the immeasurability of work hours of independent workers would make it difficult or impossible to adequately administer certain protections, such as a minimum wage for each hour worked and overtime pay for hours worked in a week in excess of forty. The authors maintain that independent workers could be viewed as having traded some of the employee protections under the FLSA for the flexibility to work only when they want to do so. Additionally, the authors suggest that collective bargaining would help ensure that intermediaries provide efficient benefits where appropriate, and the ease of entry and exit from independent work should provide some protection against substandard wages and exploitative work hours.

#### *Unemployment Insurance*

Similarly, unemployment insurance benefits are generally provided to employees who lose their jobs through no fault of their own, rather than to those who voluntarily opt out of their jobs or who stop working temporarily by choice or are dismissed for cause. Since independent workers control when and whether they will work, this rationale does not apply and they would rarely, if ever, qualify for unemployment benefits. However, Harris and Krueger state that intermediaries should be permitted to pool resources across workers to create a private and voluntary unemployment insurance system if they desire, or if the independent workers bargain for such a benefit.

#### *Workers’ Compensation Insurance*

While the proposal focuses on federal law, one of the benefits—workers’ compensation insurance—is an important aspect of the employer–employee relationship that is governed by state law. Workers’ compensation provides cash compensation and medical benefits to employees who experience workplace injuries or illnesses. The employee is not required

to show that the employer was negligent or otherwise at fault to collect benefits. Employers who are covered by workers’ compensation cannot be sued through personal injury law by their employees in the event of a work-related injury or illness. In contrast, independent contractors use personal injury law to seek compensation for injuries or illnesses that result from their work relationship. This means that their compensation is less predictable and workers cannot receive compensation without establishing fault, but can result in compensation in amounts that are many multiples of what employers pay for any single workers’ compensation claim.

Since independent workers do not generally perform their work on an intermediary’s premises or use equipment supplied by an intermediary, the authors contend that it is unclear whether an intermediary should be expected to take responsibility for injuries, illnesses, or fatalities that may be beyond its control. Instead, the authors turn to the tort system – that is, personal injury law— as the most effective solution for addressing work-related injuries, illnesses, or fatalities when the intermediary is at fault. However, it is possible that in some instances workers’ compensation insurance would be more efficient for an intermediary, so Harris and Krueger propose that intermediaries be permitted to opt in to workers’ compensation insurance policies without transforming these relationships into employment. In exchange for this no-fault insurance coverage, intermediaries would receive limited liability and protection from lawsuits.

### Health Insurance and Affordable Care Act Requirements

Harris and Krueger propose that federal law require intermediaries that do not provide health insurance to pay a contribution equal to five percent of independent workers’ earnings (net of commissions) to support health insurance subsidies in the exchange. The Employer Shared Responsibility provisions of the Affordable Care Act requires that firms with 50 or more full-time-equivalent employees offer health insurance that meets minimum value and affordability standards for their employees. Full-time employment under the statute is defined as 30 or more hours of work per week, so applying this rule to independent workers with immeasurable work hours would be problematic. However, treating independent workers like independent contractors in this respect would allow intermediaries to benefit from the insurance that such workers may receive at other jobs at no cost, which would violate the neutrality principle. Moreover, if independent workers were to turn to exchanges to purchase tax-subsidized health insurance, intermediaries would have an advantage over those employers paying a penalty in similar circumstances. This proposed requirement would solve the free-rider problem and ensure neutrality.

## Conclusion

In the face of new and emerging work relationships in the online gig economy, this proposal aims to reduce legal uncertainty, increase efficiency, and strengthen worker protections. The proposal follows the guiding principles of immeasurability of work hours, neutrality, and efficiency to balance benefits and protections among the statuses of employee, independent worker, and independent contractor. The authors believe that this new worker classification would fill a void, thus enhancing the benefits and protections for workers and allowing innovation to move forward with greater legal certainty.

# Questions and Concerns

## How are independent workers different from employees or independent contractors?

Independent workers are distinct from the current categories of employees or independent contractors in several fundamental ways. According to the authors, they are unlike employees because their relationships are not so dependent or long lasting that intermediaries should be asked to assume responsibility for independent workers' economic security. The intermediary does not require the independent worker to provide services to the customer. These features distinguish the independent worker–intermediary relationship from an employee–employer relationship, even one in which an employee may be allowed to choose flexible working hours or to work from home.

Independent workers are also unlike independent contractors because they have little individual bargaining power with the intermediaries and customers, and do not always have the same freedom to negotiate their compensation or terms of service. Independent workers are also often as integral to the business of the intermediary as employees are to the business of the employer. As such, the intermediary may set certain requirements for independent workers, such as criminal background checks, and may set the price for the service provided by independent workers. Thus, Harris and Krueger argue that independent workers are conceptually distinct from both employees and independent contractors.

## Are independent workers different from other third-party players in labor markets?

Independent workers are not the only workers in U.S. labor markets who find themselves in some form of triangular relationship. Harris and Krueger believe that the application of the proposed independent worker category should not be limited to the online gig economy. For example, some taxi drivers rent or lease taxis from a taxi company branded with the company's name and are dispatched by the company to pick up customers. This relationship closely resembles the triangular relationship between independent worker-drivers, app-based ride services, and the riders. These taxi drivers are generally classified as independent contractors, but some aspects of their work make them look more like employees. Taxi drivers must rent their taxis, but they are not able to use them for purposes other than work for the company, whereas app-based drivers can use their personal vehicle for other purposes. Taxi drivers also have less control than other drivers over which customers they choose when the rides are not hailed on the street, as the company dispatches them to customers. Finally, shifts for taxi drivers are more clearly defined because it is unlikely that a driver would stop working during a shift when she must earn back her investment in the taxi rental. Thus, Harris and Krueger argue that taxi drivers appear to possess at least as many, if not more, attributes of both an employee and independent contractor as does the independent workers identified in the online gig economy.

## Why can't courts or administrative agencies themselves evolve a third legal classification for workers?

While an argument might be made that courts or administrative agencies can take action more quickly, Harris and Krueger maintain that the evolution of an entirely new legal classification should not be left to judges or regulators. The courts do not have the power on their own to ensure that independent workers receive all of the benefits and protections due to them because they are governed at different levels and across different statutes. Similarly, regulatory agencies like the Internal Revenue Service and the U.S. Department of Labor do not have the authority to extend all of these benefits. Harris and Krueger emphasize that a comprehensive solution will necessarily require Congress taking action.

## Highlights

Seth Harris of Cornell University and Alan Krueger of Princeton University propose the creation of a new legal category of workers, to be called “independent workers,” to address the current legal uncertainty regarding whether workers in the online gig economy should receive employment and tax benefits and protections. Their proposal would allow independent workers to gain access to collective bargaining, various forms of insurance, civil rights protections, employer-provided benefits, and tax withholding.

## The Proposal

**Create a New Classification for Independent Workers.** Congress and, where necessary, state legislatures would pass legislation to establish a new classification for independent workers. In doing so, Congress and state legislatures would consider three guiding principles in the new worker classification system to recognize that: work hours are difficult or impossible to measure, businesses should not organize themselves to fit their workers into one status over another, and workers and businesses should maximize the joint benefits of their relationship. The new classification would encompass both new types of work, such as jobs in the online gig economy, and more-established forms, such as taxi driving.

**Assign Benefits and Protections to Independent Workers.** Congress would assign new benefits and protections to independent workers, following the proposed guiding principles. Benefits such as tax withholding and various forms of insurance would be available to independent workers without businesses facing full employment classification, while benefits tied to hours such as minimum wage and overtime pay would be excluded.

## Benefits

This proposal would address the uncertainty that workers and businesses face in the current legal environment regarding a range of legal protections and benefits that employees receive. Harris and Krueger argue that the proposal would increase efficiency in the labor market, enhance worker protections, encourage innovation, and decrease costly legal battles by addressing a key deficiency in current employment law.



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