INDEPENDENT CONTRACTOR LAWS AND THE SHARING ECONOMY

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The sharing economy, also called "the gig economy," is changing the nature of employment for millions of Americans. On the one hand, working as an independent contractor in the sharing economy appears to offer great flexibility in terms of hours, frequency, and duration of work. But, on the other hand, earnings are so low and the ability to earn more is so acutely tied to terms and fees established by the hosting company that flexibility is really nothing more than an illusion. Because of the level of control and financial dependency, many workers in the sharing economy are claiming they are misclassified as independent contractors.

In the United States, individuals performing work are either independent contractors or they are employees. If they fail to meet the test for an independent contractor, they are employees. In some states, workers are presumed to be employees by state law unless proved otherwise. Sharing economy host companies are now facing lawsuits from workers across the country. The results of these lawsuits vary from state to state, in large part because there are different independent contractor tests being used, but also because the applicable independent contractor precedents were developed long before the sharing economy was conceived. It is likely that new legislation will be adopted to resolve how these workers should be classified. But for now, we must try to apply old law to this new class of workers.

WHAT IS THE SHARING ECONOMY?

The sharing economy is an economic system in which assets or services are shared between private individuals, either free or for a fee, typically by means of the Internet, through a host company. Thanks to the sharing economy, you can easily rent out your car (Turo), your home (VRBO, Airbnb), your bike (Spinlister), or even your WiFi network (Fon). Most notably, the sharing economy has transformed on-demand transportation. Under the sharing economy you can quickly pick up an electric scooter (Bird, Lime) on just about any corner in a major city, and you can summon a car with a driver from anywhere with a tap of your finger (Uber, Lyft). Each segment of this sharing economy has sparked legal debates over how to handle these modern transactions under old laws, including employment laws.

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CLASSIFICATION OF WORKERS

To understand how to classify people working in the shared economy, we need an understanding of the existing framework. Currently, workers in America are classified as either employees or independent contractors. An employee is a person who performs work, where the company/employer has the power or right to control and direct the employee in the material details of how the work is to be performed. The employee performs work for a specific wage or salary, under an implied or written contract. Depending on the state, there may be other factors that are balanced to determine employment status. Most workers in America are classified as employees. An independent contractor is a worker who individually contracts with companies to provide specialized or requested services on a project basis. This individual is free from control and direction of the performance of his or her work, and the individual is customarily engaged in an independent trade, occupation, profession, or business. The Internal Revenue Service (IRS) applies a 20-factor test to determine whether an individual qualifies as an independent contractor for federal tax purposes.

WHY CLASSIFICATION MATTERS

From a legal perspective for the worker, independent contractors are generally outside the coverage of laws that apply to the employer-employee relationship. For example, independent contractors do not have access to benefits and protections that employees are entitled to by law, such as the minimum wage, overtime compensation, family and medical leave, and employer-paid unemployment and disability insurances. Thus, for example, true independent contractors injured on the job while working are responsible for medical expenses and resulting income losses. From the hiring company's perspective, hiring an independent contractor

has significant benefits; however, misclassifying an individual as an independent contractor can be a costly mistake, especially when it comes to wage-and-hour law. Employers can owe back wages with penalties and interest, and be subject to tax assessments and penalties, as well as civil fines, or worse, allegations of intentional fraud. In addition, they risk denial of insurance claims or loss of coverage, attorney fees, and litigation. When a company has misclassified a large group of employees, it can face a class-action lawsuit, which can multiply these costs to business-ending proportions.

EMPLOYEE VS. INDEPENDENT CONTRACTOR

There is no single legal standard for determining if a person is an independent contractor or an employee. In fact, the U.S. Supreme Court has indicated that there is no single rule or test for determining whether an individual is an independent contractor or an employee for purposes of the Fair Labor Standards Act (FLSA), and that is only one of many bodies of law that require distinguishing between independent contractors and employees. An individual can be classified as an employee for some purposes, such as workers' compensation, but not others, such as unemployment insurance, depending on the standards under state laws. Nevertheless, most courts agree the most important factor is the right to control, although there are a variety of factors that should be used in the analysis.

Among the factors that courts have considered significant are:

- the extent to which the services rendered are an integral part of the principal's business;
- the permanency of the relationship;
- the amount of the alleged contractor's investment in facilities and equipment;
- the nature and degree of control by the principal;
- the alleged contractor's opportunities for profit and loss;
- the amount of initiative, judgment, or foresight in open market competition with others required for the success of the claimed independent contractor; and
- the degree of independent business organization and operation.

In applying its analysis, the IRS evaluates factors that provide evidence of the degree of control and independence in three categories:

- **Behavioral.** Does the company control or have the right to control what the worker does and how the worker does his or her job?
- **Financial.** Are the business aspects of the worker's job controlled by the payer? (These include things like how the worker is paid, whether expenses are reimbursed, who provides tools/supplies, etc.)
- **Type of relationship.** Are there written contracts or employee-type benefits (e.g., pension plan, insurance, vacation pay, etc.)? Will the relationship continue, and is the work performed a key aspect of the business?

Businesses must weigh all these factors when determining whether a worker is an employee or an independent contractor. Some factors may indicate that the worker is an employee while other factors indicate that the worker is an independent contractor. There is no one factor that stands alone in making this determination. Also, factors that are relevant in one situation may not be relevant in another. This array of the applicable legal standards and the variation of facts of each case make the determination of whether a worker is an independent contractor or an employee challenging—not only for the worker and the hiring company, but for the courts that are tasked with making the final call.

The most important factor distinguishing an employee from an independent contractor is the right to control.

APPLICATION OF THESE TESTS TO SHARED ECONOMY WORKERS

The independent contractor status for shared economy workers has been subjected to legal challenge nationwide. Despite this trend, case law varies on this issue for several reasons. For example, many misclassification lawsuits have been diverted to arbitration, without the court resolving the question of whether shared

economy workers are employees or independent contractors (*Richemond v. Uber Technologies, Inc.* (S.D. Fla. 2017) 263 F. Supp. 3d 1312, 1318; *Singh v. Uber Technologies Inc.* (D.N.J. 2017) 235 F. Supp. 3d 656, 669, and FN7; *Lamour v. Uber Technologies, Inc.* (S.D. Fla., Mar. 1, 2017, No. 1:16-CIV-21449) 2017 WL 878712; *Bekele v. Lyft, Inc.* (D. Mass. 2016) 199 F. Supp. 3d 284, 313, aff'd (1st Cir. 2019) 918 F.3d 181). The shared economy's hosting companies benefit from these arbitration provisions because, if the companies do not prevail, the rulings do not result in precedential opinions. What's more, to further avoid bad legal precedent through arbitration, the hosting companies tend to settle these disputes before reaching the legal questions or a final verdict. For example, leading up to its initial public offering, Uber disclosed to the U.S. Securities and Exchange Commission that it reached agreements to "resolve the classification claims of a large majority" of 60,000 U.S. drivers who filed, or expressed intention to file, arbitration demands. Uber set aside $146 million to $170 million for settlement payouts. Further, Uber reserved $132 million for misclassification settlements in December 2018 and listed classification suits as a risk factor in its earlier S-1 filing. Similarly, Lyft has paid out multiple settlements for misclassification lawsuits, including a $27 million settlement in 2017 and a $12.5 million settlement in 2016. These tactics have resulted in a limited body of case law on this subject.

While the courts have been punting this question to arbitration and the hosting companies are settling the claims, governmental agencies are issuing opinion letters on the topic. In April 2019, the Department of Labor (DOL) issued an opinion letter that concluded certain workers in the shared economy are to be classified as independent contractors for purposes of the FLSA (tinyurl.com/y6fwv5t3). The DOL arrived at this conclusion using an "economic reality" test applied by the U.S. Supreme Court in *Rutherford Food Corp. v. McComb* (1947) 331 U.S. 722, 729. In the same month, the National Labor Relations Board (NLRB) issued an opinion letter finding that drivers providing personal transportation services for Uber are independent contractors (tinyurl.com/y33dombd). The NLRB arrived at this conclusion by applying the common-law agency test set out in its opinion in 2019 in *SuperShuttle DFW, Inc.*, 367 NLRB No. 75 (Jan. 25, 2019). The two federal agencies used different tests but arrived at the same conclusion that shared economy workers are independent contractors. Thus, while the facts of every working relationship are different, a shared economy worker bringing a misclassification claim before a federal agency will have a slim chance of success.

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Although the federal government appears to be holding firm on the independent contractor status of these workers, some states are moving toward classifying these workers as employees. Oregon, which has an independent contractor statute defining the requirements test, put Uber on notice that drivers would be classified as employees under its law in an advisory opinion from its Bureau of Labor and Industries on October 14, 2015. Several other states have statutes that address employers who misclassify employees as independent contractors. California has also proposed legislation that would classify most of these workers as employees and uses a test similar to Oregon's. Specifically, the California legislature has presented AB-5, which expands the California Supreme Court decision *Dynamex Operations W. v. Superior Court* (2018) 4 Cal. 5th 903, reh'g denied (June 20, 2018). The ruling and AB-5 institute the "ABC Test." Under the ABC Test, to properly hire an independent contractor, the business must prove that the worker: (a) is free from the company's control; (b) is doing work that isn't central to the company's business; and (c) has an independent business in that industry. If the business fails to meet a single element, the worker must be classified as an employee. Following the *Dynamex* decision, the U.S. District Court for the Northern District of California approved a $20 million settlement between Uber and a class

of 240,000 drivers claiming to be misclassified (*O'Connor v. Uber Technologies, Inc.* (N.D. Cal., Mar. 29, 2019, No. 13-CV-03826-EMC, 2019 WL 1437101). Further, the California Labor Commission found that an Uber driver was misclassified as an independent contractor under the factor-based test in *S. G. Borello & Sons, Inc. v. Dep't of Indus. Relations* (1989) 48 Cal. 3d 341. Uber appealed the matter to superior court, but it was settled and dismissed without a final decision from the court (*Uber Technologies, Inc. v. Berwick*, CGC 15-546378). But whether or not California's AB-5 passes, *Dynamex* and *S. G. Borello & Sons, Inc.* remain law of the land in the state.

NEW CLASSIFICATION FOR SHARED ECONOMY WORKERS?

Shared economy workers have some characteristics of independent contractors, but unlike a typical independent contractor relationship where the contractor has a specialized skill and negotiating power, these shared economy workers are frequently lower-educated, unskilled workers who are in a substantially subservient economic position to the hosting company. This imbalance of power is what has some jurisdictions, such as California and New York, favoring more protections.

The U.S. District Court in California said it best: "At first glance, Lyft drivers don't seem much like employees. . . . But Lyft drivers don't seem much like independent contractors either" (*Cotter v. Lyft, Inc.* (N.D. Cal. 2015, 60 F. Supp. 3d 1067, 1069). The court went on to recognize that "The test the California courts have developed over the 20th Century for classifying workers isn't very helpful in addressing this 21st Century problem. Some factors point in one direction, some point in the other, and some are ambiguous. . . . [A]bsent legislative intervention, California's outmoded test for classifying workers will apply in cases like this. And because the test provides nothing remotely close to a clear answer, it will often be for juries to decide" (*Id.* at 1081–1082). This will continue to be true for other states as well, as most apply common law tests established by case precedents.

This is a new class of workers that does not fit into the old dichotomy of employee versus independent contractor. Maybe it is time to create a new classification of workers under a system that *both* provides minimum protections and compensation to the workers while maintaining the reasonable cost controls and flexibility for the shared economy host companies.

Other countries, such as Canada, Spain, and Germany, already have an intermediate classification called "dependent contractor" for freelancers who work mostly for one business. These workers receive some protections but not as many as full-time employees. In these countries, to qualify as a dependent contractor, the worker must earn a minimum percentage from a single source (Canada: 80 percent; Spain: 75 percent; Germany: 50 percent). Thereafter, the worker is entitled to some minimum protections that vary by country but generally exclude wage-and-hour protections and provide unemployment and workplace injury protections.

THE FUTURE FOR SHARED ECONOMY WORKERS

The future for shared economy workers is uncertain. While states such as California, New York, and Oregon are leaning toward an employee-employer relationship, the federal government appears to be holding firm on the independent contractor status. Thus, absent national legislation, whether these workers will be considered an employee or independent contractor depends heavily on what state they are in and whether they file their claim with a federal or state agency or a court.

Shared economy workers in more progressive locations are slowly gaining narrowly tailored protections. For example, effective January 2019, ride-hailing companies in New York City, which include Uber and Lyft, are required to pay their drivers a guaranteed minimum pay rate of around $17 an hour. Seattle is considering similar pay and labor protections in conjunction with existing city ordinances that regulate taxis and ride-sharing services and give drivers the right to bargain with companies collectively if they choose. Workers in less progressive states, however, should enter these working relationships with open eyes. ■

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