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Worker Classification in the Gig Economy: Navigating the Shifting Legal Seas

Independent Contractors

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The ''shared,'' or ''gig'' economy has rapidly grown amidst a legal environment that well preceded it. Indeed, when most worker classification laws and regulations were passed, lawmakers certainly did not give consideration to the unique way that this sector operates using technology since technology platforms did not exist at the time. Consequently, this rapidly growing sector of our economy is largely stuck with rules that don't neatly mesh with its common business model, which substantially relies on freelance workers and technology platforms.

Gig economy workers typically do not operate as employees, and certainly do not operate in the conventional sense of that term. Yet, in the shared economy, freelance workers, who typically work when and where they choose, provide services directly to customers of the gig economy business with which they are associated. This quality has been the subject of legal challenges premised on arguments that the work performed by freelance workers is integral to and not separate from the business, which generally is deemed supportive of an employment relationship. Further, in many cases, the business through which the freelance worker

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provides services may be the worker's exclusive (or at least a primary) source of income, which also is considered more consistent with an employment relationship.

Despite these characteristics, however, contemporary freelance work arrangements have emerged as an entirely new way of working in a new economy that is quite distinct from our broader economy, which historically has been dominated by employment relationships. In this way, gig economy work arrangements are not technically replacing employment relationships, but coexisting in a broader economy where the employment relationship has dominated for decades. Consequently, despite the unique nature of freelance work arrangements in this new economy, the reality is that the relationships are often subject to legal comparison with the employment relationship. The crucial question then for most businesses in the gig economy is (or at least should be), ''are our freelance workers employees under the law.''

Answering this question is extremely important because the stakes are very high. Worker misclassification can subject a business to substantial legal exposure under a variety of federal, state and local laws. On the other hand, implementation of an employment model generally would be entirely impracticable because the freelance work arrangement is a critical component of the gig economy itself.

Despite its importance, however, trying to answer this question can be an exceedingly challenging and complex endeavor that often yields anything but certainty. Even before the gig economy emerged and inserted a proverbial monkey wrench into worker classification, the line separating independent contractor from employee has been far from clear.

Many Factors Determine a Worker's Status

Proper classification of a worker generally requires consideration of a number of laws, and a fact-intensive examination of the relationship between the individual workers and business, the nature of the work performed and a multitude of other factors.

There are many different federal and state laws that embrace various legal tests (most of which are multifactor tests) for determining whether a worker is an employee or independent contractor. These tests vary even within jurisdictions.

For instance, the test used to determine whether a worker is an employee for state unemployment purposes may vary from the test used to determine coverage for state-mandated workers' compensation purposes. Likewise, under federal law, the test used to determine whether a worker is an employee for tax purposes varies from the test used to determine employment status for wage and hour purposes. These challenges are compounded for businesses operating in numerous states, nationally, or in many cases, internationally.

In the gig economy, the challenges associated with worker classification are further complicated by the necessity of operating within a legal framework that was conceived long before its emergence. Thus, applying worker classification law to the gig economy presents unique challenges and often involves ensuring that the tribunal has an understanding of the business operations.

Recognition Seems the Logical Solution

Thankfully, in recent years, with the gig economy now firmly rooted and thriving in the United States, there seems to be increased legislative recognition that it is not only here to stay but is a rapidly expanding segment of the economy that must be more directly addressed under the law. New legal recognition of the gig economy worker seems the most logical solution to addressing what is, in many ways, a *new* type of worker operating in a *new* segment of the economy. Given the importance of freelance workers to the gig economy, expressly recognizing this unique sector of the economy and its relationship with workers could greatly benefit both businesses and workers by providing a higher level of regulatory certainty, stability, and predictability.

Among its many benefits, such an approach could substantially reduce litigation over worker classification and the associated costs. It also could facilitate the provision of safe harbors for gig economy businesses to make available certain benefits and protections to freelance workers without running the risk of inadvertently converting workers to employees by doing so.

To date, transportation network (or ''ride sharing'') companies seem to be getting the most legislative attention in this area. In recent years, many states have enacted legislation specifically relating to this segment of the gig economy and classification of drivers as independent contractors. For example, Michigan's ''Limousine, Taxicab and Transportation Network Company Act,'' which went into effect March 21, 2017, generally establishes that drivers working for ride sharing companies are independent contractors if certain requirements set forth in the statute are met. MICH. COMP. LAWS SERV. § 257.2101; 2102; 2137 (2017).

With regard to broader recognition of the gig economy worker, however, legislation has been, to say the least, sparse. Arizona currently is the most notable example of a forward-thinking jurisdiction in this area. In 2016, Arizona enacted a statute aimed at classification of ''qualified marketplace contractors'' (working on a qualified marketplace platform) as independent contractors under state laws. ARIZ. REV. STAT. § 23-1603 (2017).

The statute broadly defines ''qualified marketplace contractors'' as ''any person or organization, including an individual, corporation, limited liability company, partnership, sole proprietor or other entity, that enters into an agreement with a qualified marketplace platform to use the qualified marketplace platform's digital platform to provide services to third party individuals or entities seeking those services.'' *Id.* It also defines ''qualified marketplace platform'' as an ''organization . . . that both operates a digital website or digital smartphone application that facilitates the provision of services by qualified marketplace contractors to individuals or entities seeking such services'' and ''accepts service requests from the public only through its digital website or digital smartphone application, and does not accept service requests by telephone, by facsimile or in

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person at physical retail locations.'' *Id.* Notably, the law establishes that qualified marketplace contractors shall be treated as independent contractors for ''all purposes under both state and local laws, regulations and ordinances,'' including employment security laws and workers' compensation law where certain requirements set forth in the statute are met, such as a written independent contractor agreement that includes certain specified provisions. *See id*.

Recognition May Present Challenges

Despite the potential benefits of legislative recognition of the gig economy worker, it likely will not unfold without its own challenges for gig economy businesses. Indeed, such legislation would not necessarily tend toward blanket treatment of such workers as independent contractors and could, at least in some respects, mandate treating them like employees.

For example, legislation could provide for certain worker protections (e.g., the right to organize and collectively bargain) and mandate benefits enjoyed by employees, which would come at an economic cost to gig businesses. For example, in January 2016, City of Seattle Ordinance 124968 took effect, giving for-hire drivers the right to collectively bargain with the companies that contract or partner with them.

Additionally, in the State of Washington, a bill has been introduced that would require gig economy businesses to contribute funds to benefit providers for independent contractors. *See* WASH H.B. 2109. In its current form, the amount of the contribution, which must be made at least monthly, must be the lesser of a percentage of 25 percent of the total fee collected by the business from the consumer for each transaction or $6.00 for every hour that the worker provided services to the consumer. *See id*. Notably, the contribution required may be added to the invoice or bill submitted to the consumer. *See id*. Available benefits include health insurance, paid time off and retirement, among potentially others. *See id*. In addition to the added cost and administrative burden, this legislation could be challenging for businesses that currently do not track hours or where workers directly invoice consumers.

New York City's Freelance Isn't Free Act, which went into effect this year, also is aimed at protecting freelance workers. *See* N.Y.C. ADMIN CODE Tit. 20, ch. 10, § 20-927 *et seq*. It imposes certain requirements on independent contractor agreements and generally requires that businesses timely and fully pay freelance workers the originally agreed upon compensation. *See id.* at 20-928; 929. The ordinance further prohibits retaliation against a freelance worker for exercising or attempting to exercise rights under it. *See id*. at § 20-930. More recently, the Department of Consumer Affairs promulgated rules expressly prohibiting collective/class waivers in independent contractor agreements with freelancers. The rules, which went into effect on July 24, appear to prohibit arbitration provisions in independent contractor agreements as well. *See id*. at 20-935.

Further, in Hawaii, a bill was introduced in 2017 that actually would broaden the definition of employee under the ''Hawaii Prepaid Healthcare Act'' to include independent contractors who have been providing services for six consecutive months or more. *See* HI H.B. No. 965.

Rethink 'One-Size-Fits-All' National Model

As demonstrated by the above legislative examples, even with increased legal recognition of the gig economy worker, inconsistencies in treatment likely will persist. Indeed, as has historically been the case with worker classification law, how gig economy worker classification will be addressed by federal and various state and local governments undoubtedly will be highly varied and may be pro-worker, pro-business or somewhere in between. These differing legislative approaches (and their timing) will add a new dimension to an already complex area of the law for gig businesses, especially those operating nationally or on a large regional scale. Further, laws providing for worker benefits and bargaining rights such as those discussed will add a layer of cost and administrative burdens.

In light of this varied and shifting legal landscape for worker classification and its anticipated changes impacting the gig economy going forward, businesses that rely heavily on freelance workers should rethink implementing a broad and categorical ''one-size-fits-all'' national model, that may fall short of complying with the classification laws in all states and cities of operation throughout the United States.

Stated simply, freelance workers may be deemed employees in certain localities, even if such workers would be deemed independent contractors in other jurisdictions. Consequently, measures tailored to varying jurisdictional laws should be taken to try to abate the risk of such classification issues and increase the likelihood that freelance workers will be deemed independent contractors in all geographic areas of operation.

As one illustration, in 2004, Massachusetts amended its wage and hour statute, making it much more difficult to establish independent contractor status. Massachusetts previously had relied upon the ''ABC test,'' to determine whether a worker was an employee or independent contractor. Under that test, independent contractor status could be shown by proving, among other requirements, that the service performed is **either**: (1) outside of the usual course of the business for which the service is performed; **or** (2) outside of all places of business of the enterprise. The amendment eliminated the second requirement, effectively characterizing any worker as an employee absent proof that the service performed is outside the usual course of business of the employer. *See* MASS. GEN. LAWS ANN. ch. 149, § 148B.

As further illustration, last year, a Utah Court of Appeals rendered a decision affirming the Utah Workforce Appeals Board's (''Board'') determination that gig economy workers were misclassified as independent contractors and should have been classified as employees whose wages were subject to unemployment compensation contributions. In *Needle, Inc. v. Department of Workforce Servs., Workforce Appeals Board*, Needle, a software company, licensed its technology platform to online retailers. 372 P. 2d 696 (Utah Ct. App. 2016).

The platform enabled customers visiting the retailers' websites to interact in real time ''chats'' with ''advocates,'' who were workers knowledgeable about the retailer's products and services. Needle provided assistance to retailers in finding advocates to perform the chats. Once approved by the retailers, the advocates

were engaged as independent contractors by Needle. Advocates provided their own computers and internet access and could work wherever and whenever they wanted. Needle did not establish set work hours or quotas or require that a script be followed during the chats. Needle did, however, monitor advocates' performance using criteria established by the retailer. Its platform was programmed to route chats to certain advocates based on prior performance and pre-selected metrics.

In affirming the Board's determination that advocates were misclassified as independent contractors, the court focused on the statutory requirement that independent contractors be ''customarily engaged in an independently established trade, occupation, profession, or business of the same nature as that involved in the contract for services.'' UTAH CODE ANN. § 35A-4-204(3)(a).

This requirement is analyzed using a number of factors identified by the Department of Workforce Services such as whether the worker has made a substantial investment in the tools and equipment necessary to perform the work, whether the worker ''regularly performs services of the same nature for other customers or clients and is not required to work exclusively for one employer,'' and whether the worker ''can realize a profit or risks a loss from expenses and debts incurred through an independently established business activity.'' *See Needle*, 372 P. 2d at 699.

Most notably, the court concluded that the Board did not err in finding that the advocates had not made a substantial investment in the tools and equipment necessary to perform the work because advocates already had computers and internet service and thus did not purchase the tools and equipment in order to provide the services. The court further opined that the Board did not err in placing more weight on Needle's provision of the technology platform, a tool that was imperative to the advocates' ability to engage in the chats. The court also agreed with the Board that Needle failed to demonstrate that the advocates actually performed related services on a regular basis for other clients notwithstanding evidence that advocates were not required to work exclusively for Needle. Additionally, the court declined to disturb the Board's finding that there was ''no evidence that advocates could experience a loss as there were no costs associated with the services they provided,'' and the ''amount of profit they made was determined by the number of encounters they had with customers.'' *See Needle*, 372 P. 2d at 705. As characterized by the court, the Board correctly ''reasoned that it is not enough for a worker to be able to realize a profit or suffer a loss in earnings simply through performing more or less piecework.'' *See id*.

In stark contrast to these examples, other states are comparatively much more business friendly with regard to worker classification. Arizona, discussed above, has specifically recognized independent contractor status for ''qualified market contractors'' who meet the statutory criteria. Further, in South Dakota, when the worker is not an employer or general contractor (and is not covered under a workers' compensation policy), the contracting parties can create a rebuttable presumption of independent contractor status for purposes of South Dakota's Workers' Compensation Act by executing an independent contractor affidavit of exempt status. *See* S.D. CODIFIED LAWS § 62-1-19. The affidavit must be on a form prescribed by the director of the South Dakota Division of Insurance signed by both parties and notarized. *See id*. at § 62-1-20.

These examples of both favorable and unfavorable worker classification laws illustrate the benefits that might be gained from gig economy businesses that take a more targeted and tailored approach to where and how they conduct their operations relative to workers. Routine focus on worker classification and ongoing changes in applicable law is especially important for businesses whose very existence depends upon freelance workers (and maintaining their independent contractor status).

Challenges Will Likely Continue

While a federal classification law with far-reaching preemptive force likely would be the most user-friendly solution to the challenges facing gig economy businesses discussed above, such an outcome is highly unlikely.

Consequently, gig economy businesses undoubtedly will have to continue to grapple with these challenges unless and until more states follow Arizona's lead in passing progressive legislation. As they do so, we offer the following general suggestions:

- Ensure that your terms of use/user agreement includes appropriate and robust independent contractor provisions and does not incorporate provisions or terminology that is more consistent with an employment, rather than independent contractor, relationship;
- Familiarize yourself with applicable law pertaining to worker classification, including the primary tests and factors that courts and agencies rely upon. Doing so can be helpful in evaluating your business practices relative to your workers to help ensure that your organization is not engaging in risky practices that could jeopardize your workers' status as independent contractors;
- Identify and take advantage of any avenues provided by states in which your business operates to create a presumption of independent contractor status for your workers. As noted above, in some states, an affidavit of independent contractor status or similar documentation can help support independent contractor status under the law;
- Identify states in which you operate that have classification laws presenting unique or significant risks and determine whether such risks can be abated by changes to your business model. If such changes are not feasible from a business standpoint, consider whether your organization should, in light of the risks, continue to engage workers in such states;
- Assess your business practices relative to independent contractors to ensure that your organization is not inadvertently treating them like employees. For example, hourly pay, the provision of instructions and training, and monitoring and evaluating work can undermine independent contractor status;
- Consider whether it would be advisable to include arbitration and class waiver provisions in your terms of use/user agreement.

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