ITIF | INFORMATION TECHNOLOGY & INNOVATION FOUNDATION

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COMMENTS OF ITIF

Before the

United States Department of Law

Washington, D.C.

In the Matter of:	)	
	)	
The proposed rescission of the 2021 Independent Contractor Rule	)	MB Docket No. 2022-21454
	)	

December 9, 2022

CONTENTS

INTRODUCTION AND SUMMARY

The Department of Labor (DOL) is proposing to rescind the January 2021 Independent Contractor Rule concerning employee vs. independent contractor status as it relates to the Fair Labor Standards Act (FLSA).[1] The FLSA (among other things) guarantees a minimum hourly wage and an overtime wage premium (1.5 times the hourly wage for more than 40 hours of work in a week) to employees but not to independent contractors.[2]

ITIF recognizes that some companies have abused independent-contractor status to deny workers certain rights and benefits codified in labor law and that these instances of misclassification should be addressed. However, ITIF is also concerned that the recission of the 2021 rule without a clearer, more modern framework to replace it threatens misclassification with respect to the fast-growing gig economy, where gig workers risk being incorrectly classified as employees rather than independent workers. This threatens the flexibility innate in online gig-economy platforms like Uber and TaskRabbit and the development of any further labor-market-related innovations. Evidence suggests that workers highly value this flexibility and would significantly cut back on their hours worked without it. Instead, the DOL should uphold the current framework while working with lawmakers to create new labor laws fitted to the modern digital economy.

BACKGROUND

Prior to the 2021 rule, courts determined employee or independent contractor status based on a "totality-of-the-circumstances" approach, which typically considered five or six primary factors (with the number of factors being considered and their relative importance varying from case to case and court to court):

1. The nature and degree of the employer's control over the worker
2. The permanency of the worker's relationship with the employer
3. The worker's investment in equipment or labor for the task

1. "Employee or Independent Contractor Classification Under the Fair Labor Standards Act," *Federal Register*, October 13, 2022, https://www.federalregister.gov/documents/2022/10/13/2022-21454/employee-or-independent-contractor-classification-under-the-fair-labor-standards-act.

2. "Wages and the Fair Labor Standards Act," *U.S. Department of Labor*, https://www.dol.gov/agencies/whd/flsa.

4. The skill required to perform the task
5. The worker's opportunity for profit or loss
6. The importance of the worker's service to the employer's business

For more than 80 years prior to the 2021 rule, these factors served as a form of "subregulatory guidance" on the part of the DOL—that is, these factors were not codified in regulation or legislation but were a suggested framework based on legal precedent.

The 2021 rule proposed five factors to be considered instead, with the first two being "core" factors:

1. The nature and degree of the employer's control over the work
2. The worker's opportunity for profit or loss
3. The amount of skill required for the work
4. The degree of permanence of the working relationship between the worker and the employer
5. Whether the work is part of an integrated unit of production

This fifth factor is different from the prior "importance of the worker's service to the employer's business." As the Society for Human Resources Management describes it, this fifth factor may suggest employee status "when the worker depends on the overall process to perform work duties."[3]

As core factors, the first two factors carry more weight than the others. The employer's control over the work consists of elements such as control over scheduling, the ability to assign tasks, and supervision over the work. The worker's opportunity for profit or loss depends on the worker's potential for profit or loss based on either managerial or investment decisions made by the worker—that is, if the worker stands to make a profit or loss based on either of these types of decisions, this factor suggests the worker is an independent contractor.

At the time, the DOL argued that these core factors are more likely to indicate employer or independent contractor status than the others and therefore should receive more consideration. Though this need not always be the case, if the two core factors point in the same direction—i.e., either they both suggest employee status or independent-contractor status—it is highly unlikely that the other factors will overrule the classification.

When proposing the rule, the DOL asserted that the limitations and misconceptions of the existing framework were becoming more apparent in the modern digital economy, particularly with the rise of online platforms that match service providers with customers. The DOL argued that the 2021 rule—thanks largely

3. Allen Smith, "DOL Clarifies Who Is an Independent Contractor in Proposed Rule," *SHRM*, September 22, 2020, https://www.shrm.org/resourcesandtools/legal-and-compliance/employment-law/pages/dol-independent-contractor-proposed-rule.aspx.

to its establishment of a hierarchy of factors—would clarify employee vs. independent contractor classifications.

The DOL is now proposing that the 2021 rule be rescinded and replaced with a return to the totality-of-the-circumstances approach that considers each of the following factors, with no factor automatically receiving more weight than any of the others:

1. Opportunity for profit or loss depending on managerial skill
2. Investments by the worker and employer
3. Degree of permanence of the work relationship
4. Nature and degree of control over key aspects of the work
5. The extent to which the work performed is an integral part of the employer's business

Specifically, "nature and degree of control" includes control over aspects of the relationship like scheduling, supervision, and price/wage setting. Barring a replacement of the 2021 rule with this proposed framework, the DOL suggests that the 2021 rule still be rescinded with a return to the pre-2021 framework.

DISAGREEMENTS AND CONCERNS

A reversal of the 2021 rule is primarily based on four misguided arguments: The first is that restored consistency with past precedent will increase understanding of the legal difference between an independent contractor and an employee. The second is that the increased weight applied to the control and profit-or-loss factors reduces clarity since it is unclear when these factors can be overridden by the others. The third is that the previous totality-of-the-circumstances approach has proven adaptable over the past eight decades and therefore can accommodate the contemporary labor market. And the fourth argument is that the 2021 rule increases the risk that employees are misclassified as independent contractors and are therefore denied the benefits they are due under the FLSA.

With respect to the first and second arguments, a return to the totality-of-the-circumstances approach does not necessarily restore consistency and clarity. Rather, an explicit hierarchy of the factors (where some of the factors always carry more weight than others) increases clarity since relative weighting is known from the outset. Specifically, if a worker or employer can be confident that the two core factors in the 2021 rule point toward the same classification, that will be the determined classification. The past precedent, in contrast, is an inexact and variable consideration of the factors. The relative importance applied to the factors can vary from case to case and court to court. This obviously makes it difficult for employers to be certain that their business model defines workers as independent contractors or employees, a consideration that is crucial to their investment and employment decisions. Moreover, it makes sense that these two factors carry more weight than the others with consideration to FLSA coverage. The FLSA's two relevant provisions are that it ensures a minimum hourly wage and overtime pay. If these are the benefits in question, then clearly an employer's control over workers' productivity and scheduling should be a primary factor in considering whether these benefits should be extended: If an employer must guarantee a minimum wage, then it should have some control over how productive its workers are; and if an employer must pay its workers a premium for any work beyond 40 hours in a week, then it should be able to specify whether and when workers can exceed this threshold. And if a worker, through his or her own judgment and decision making, can affect their payment, expenses, and time required to complete the task, it does not follow that he or she should be guaranteed a base wage and overtime pay.

The third argument, that the previous framework has shown itself to be adaptable over the last eight decades, ignores the rapid rise of the gig economy—especially through online matchmaking platforms—and how this differs from past labor markets. Today, millions of workers use online platforms that match customers with service providers, such as Uber and Lyft for transportation, Instacart for grocery shopping, or TaskRabbit for various services. These platforms ultimately transform the relationship between the entity buying the service and the service provider. It is difficult to look at the fierce debates about whether Uber and Lyft drivers qualify as employees since the companies' inception and determine that the existing framework was clear and applicable to the modern gig economy. Indeed, this is the driving reason behind the 2021 rule in the first place. A framework should be judged on its suitability to current circumstances and not those of the past.

The fourth argument has merit to the extent that we should be concerned about employees being misclassified as independent contractors and not receiving the benefits of the FLSA. However, it seems the current DOL has paid little attention to the costs of going too far in the other direction—that is, misclassifying independent contractors as employees. As mentioned, if an employer must pay a worker a minimum wage and a premium for overtime, the employer will demand greater control over worker productivity and scheduling, as well as the worker's ability to simultaneously work for other employers, especially competitors. Gig workers can largely choose when and how much they work as well as whether to accept a job based on the offered wage. If these workers are misclassified as employees subject to FLSA protections and benefits, this would threaten the flexibility that so many have come to value in the current gig economy. A recent paper published by the National Bureau of Economic Research analyzing a dataset of over one million Uber drivers estimates that Uber's real-time labor flexibility doubles workers' labor surplus (the difference between the wage received and the minimum wage the worker is willing to accept) and that without this flexibility, drivers would reduce the hours they drive by more than two-thirds.[4] Moreover, part of this flexibility is that workers can work for multiple, competing platforms at once. Gig drivers often work through Uber and Lyft interchangeably throughout their shifts, which forces greater competition between the two platforms, thereby increasing drivers' wages. Employment status almost certainly means that this choice is abolished since employers obviously do not want employees simultaneously working for competitors and if an employee is working for multiple employers during a shift, it becomes extremely difficult to determine which employer foots the wage bill (or shares thereof). Without this choice, gig workers' flexibility is severely diminished, as is real-time competition between competing platforms.

4. M. Keith Chen et al., "The Value of Flexible Work: Evidence from Uber Drivers," *NBER Working Paper Series*, no. 23296 (June 2017), https://www.nber.org/system/files/working_papers/w23296/w23296.pdf.

RECOMMENDATION

This is not to say that the 2021 rule is perfect. As ITIF has argued in the past, the DOL should work with legislators to establish a regulatory framework suited to the modern economy.[5] This means, first and foremost, recognizing that the rise of the gig economy has shown the past framework to be inadequate. A discrete "all-or-nothing" approach—wherein workers are either fully independent contractors or fully employees and therefore either receive the bare minimum of benefits and protections or the full gamut—should be replaced with an approach that recognizes the increasingly continuous and fluid nature of the customer-employer-worker relationship. Such a framework would facilitate the development of new, innovative service platforms and employer-worker relationships. However, until this is accomplished, the DOL should maintain the 2021 rule.

Thank you for your consideration.

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5. Joe Kennedy, "Three Paths to Update Labor Law for the Gig Economy," (ITIF, April 2016), https://www2.itif.org/2016-labor-law-gig-economy.pdf.