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Misclassification, the ABC test, and employee status

The California experience and its relevance to current policy debates

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What this report finds: Employer misclassification of workers as independent contractors is a longstanding, pervasive problem affecting millions of workers and costing government agencies billions of dollars each year.

To combat employer misclassification, many states have adopted what is known as the ABC test, a strong, protective test for determining employee status. Federal legislation—the Protecting the Right to Organize (PRO) Act—would establish the ABC test in federal labor law to better protect workers' right to organize and collectively bargain.

California adopted the ABC test in 2019. Up to 1 million California workers stand to directly benefit from the law. Unfortunately, due to a corporate-funded ballot initiative, ride-share drivers and delivery drivers who work for app-based companies like Uber, Lyft, and Instacart are now exempted from AB5. This has deprived workers of important rights and protections, and created financial pressures on companies that properly treat their workers as employees. The companies are trying to win similar exemptions in other states, and are opposing the PRO Act.

Why it matters: Misclassified workers are deprived of rights and protections under federal and state labor and employment laws, including wage and hour protections, anti-discrimination protections, workers' compensation, unemployment benefits, and the right to organize. By misclassifying workers as independent contractors, employers shift the financial burden of payroll taxes onto workers that employers ordinarily cover, and they avoid paying workers' compensation and unemployment premiums on workers' behalf. Workers lose pay, federal and state governments lose revenue, and law-abiding employers who properly treat their workers as employees are at a cost disadvantage relative to employers who cheat by misclassifying workers.

What can be done about it: Federal and state policymakers should adopt the ABC test in their labor and employment laws to ensure workers are not misclassified, and are covered by important workplace rights and protections. This includes passing the PRO Act to establish the ABC test for purposes of organizing and collective bargaining rights.

Strong enforcement and full funding of enforcement agencies must go hand in hand with a strong legal test. Experience has shown that strong statutory language, standing alone, is insufficient to ensure that workers are not misclassified and deprived of their rights.

SECTIONS

Introduction

The determination of whether an individual performing services is treated as an employee or an independent contractor carries significant consequences for workers, businesses, and governments. In the United States, workers who are classified as independent contractors:

- are not covered by worker protection laws such as wage and hour laws, anti-discrimination laws, and laws providing collective bargaining rights
- do not receive unemployment benefits when temporarily jobless
- do not receive workers' compensation when injured on the job
- are responsible for paying the full payroll tax contribution to federal Social Security and Medicare programs

In contrast, employers are responsible for covering payroll tax and social insurance costs, and providing these worker protections, for workers classified as employees. Thus, classifying workers as independent contractors both deprives these workers of workplace protections and imposes significant costs, resulting in considerable cost savings for employers, as they are able to shift these costs onto workers and avoid making payments to government tax and social insurance programs.

Misclassification of workers as independent contractors is a pervasive and extensive problem in the United States. According to a report commissioned by the U.S. Department of Labor, as many as 30% of employers, and perhaps more, have misclassified some workers, affecting millions of workers, disproportionately workers of color. Workers are misclassified by employers in many occupations and industries, including janitorial services, trucking and transportation, retail, hospitality, home care, and construction.

To address the misclassification problem and ensure workers are not deprived of important protections, many states have adopted the ABC test—a strong, protective legal test known for its three interlocking parts ((A), (B), and (C))—for determining whether an individual is an employee or independent contractor. The ABC test establishes a presumption of employee status unless an employer can meet three factors and show the individual is truly an independent entrepreneur. Adoption of the test has reduced misclassification in those states using it.

In 2019, the California legislature adopted, and the governor signed, Assembly Bill (AB) 5, which codified an earlier California Supreme Court decision holding that the ABC test applies for purposes of determining whether an individual is an employee covered by state Wage Orders. The law took effect on Jan. 1, 2020. Even before it took effect, Uber and Lyft announced a multimillion-dollar campaign to win passage of Proposition 22, a ballot initiative to exempt from AB5 platform-based drivers. Proposition 22 passed in November 2020. The measure's proponents immediately announced they would be pushing to have platform-based drivers excluded from employment laws in other states, and federally.

Debate continues in Congress and in executive branch agencies over the proper test for employee status under various federal labor laws. The Protecting the Right to Organize (PRO) Act, which adopts the ABC test for purposes of federal labor law establishing organizing and collective bargaining rights, has passed the House of Representatives and is pending in the U.S. Senate. Appointees of President Trump rolled back protections for workers at the U.S. Department of Labor and the National Labor Relations Board, and weakened the long-standing federal test for establishing employee status, and new Biden administration appointees are confronted with restoring workers' rights. States continue to face issues of misclassification and employee status.

EPI and Friedrich-Ebert-Stiftung (FES) have prepared this report to provide background on the experience in California under AB5 and Proposition 22. By understanding more fully the impacts of AB5 and Proposition 22 on California workers, policymakers can see the importance and benefit of establishing a strong, protective test, and the downside of depriving workers of employee status. We hope this report can inform the ongoing active debate in the states and in Washington, D.C., over employee status and the appropriate legal test for determining it.

In addition, the issue of legal protections for so-called "nonstandard workers," including independent contractors, as well as platform-based workers, continues to be a focus of discussion in the European Union. In the face of aggressive employer misclassification of entire workforces as noncovered "independent contractors," international labor organizations have called for strengthened protections for workers engaged in nonstandard forms of work, including independent contractors (ILO 2019). As for platform-based workers, different EU countries have taken different approaches to the issue of employment protections for these workers, with some countries treating these workers as employees, while employee status is less clear in other countries. Thus, in the EU and Britain, as in the United States, the issue continues to be a focus of policymakers, worker advocates, and employers.

Lack of employee status means lack of worker protections in the United States

The determination of whether an individual providing services to an employer is an employee or an independent contractor carries significant consequences for both the individual and the employer in terms of job protections, tax obligations, and eligibility for employment-based benefits and protections. As **Table 1** shows, individuals who are classified as independent contractors are not covered by federal or state wage and hour, anti-discrimination, health and safety, collective bargaining, or other worker protection laws. They do not receive employment-based health insurance or retirement benefits, and they do not qualify for paid sick or family leave in places where those benefits are statutorily prescribed. Nor are independent contractors eligible for unemployment insurance when temporarily unemployed, or workers' compensation when injured on the

Table 1

Comparison of workplace legal protections for employees and for independent contractors in the United States

Labor standard	Employee	Independent contractor
Minimum wage	√	X
Overtime pay	√	X
Unemployment insurance	√	X
Workers' compensation	√	X
Paid sick days	√	X
Paid family leave	√	X
Health and safety protections	√	X
Right to a union	√	X
Discrimination and sexual harassment protections	√	X

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job. This leaves independent contractors in a far more vulnerable status, as compared with employees, when it comes to securing basic rights and protections on the job.

At the same time, individuals classified as independent contractors are responsible for the payment of employment-based taxes that go toward Social Security and Medicare, currently 15.3% of earnings (IRS 2021a). Employers are required to make the employer portion (50% of total FICA tax, i.e., 7.65% of wages) of these payments on behalf of employees. They also are required to pay premiums for unemployment insurance and workers' compensation coverage, as well as short-term disability benefits in some states. These costs, when combined with the cost of employee benefits, can add as much as 30% or more to a worker's total costs.

To avoid paying these additional costs, employers misclassify workers as independent contractors. This widespread and pervasive problem affects millions of workers in numerous industries and occupations, including home care, delivery, driving, janitorial services, hospitality, construction, and other industries. The U.S. Government Accountability Office (GAO) reported that in 1984, 15% of employers misclassified workers, and 3.4 million workers were misclassified as independent contractors (GAO 2009).

Misclassification is rampant in low-wage, labor-intensive industries where women and people of color, including Black, Latinx, and Asian American/ Pacific Islander (AAPI) workers, are overrepresented (Alexander 2017). According to one study, seven of eight high-misclassification occupations are held disproportionately by women and/or workers of color. Four of these occupations—hairdressers, maids and housekeepers, teacher's assistants, and door-to-door sales workers and street vendors— are disproportionately women and workers of color (Alexander 2017).

The pervasive problem of misclassification

Employers routinely misclassify workers. A 2000 study commissioned by the U.S. Department of Labor found that between 10% and 30% of audited employers misclassified some workers, and that up to 95% of workers who said they were misclassified as independent contractors were reclassified as employees following review (Planmatics 2000). A recent report by the National Employment Law Project (NELP) contains even starker findings: In California, nine out of 10 employers inspected in 2017–2018 were found to be out of compliance with the state's laws against misclassification (NELP 2020). According to a study by University of California, Berkeley researchers, 23% of truck drivers in California are classified (or misclassified) as independent contractors (Sinroja, Thomason, and Jacobs 2019). Nineteen percent of contracted-out janitors were classified (or misclassified) as independent contractors. All of these industries have workforces made up disproportionately by people of color (Sinroja, Thomason, and Jacobs 2019).

Other states similarly confront significant problems with misclassification, as summarized by the National Employment Law Project's recent review of state investigations in 30 states (NELP 2020). Washington state and Massachusetts are just two states where workers and state coffers are bearing heavy costs from misclassification. In Washington state, misclassification increased from 5% of employers misclassifying some workers in 2008 to 14% of employers misclassifying workers in 2017, with construction workers, clerical workers, and hotel and restaurant workers the most likely to be misclassified (Xu and Erlich 2019). (See "The Massachusetts story" below for more on that state's struggles.)

Misclassification takes a real toll on workers and states

Employers misclassify employees as independent contractors to save on paying for employee benefits, employment taxes, and workers' compensation and unemployment insurance premiums which, as previously noted, can add up to 30% on top of wages. A related and significant problem, but one beyond the scope of this report, is paying workers off the books in cash to avoid any record of employment whatsoever. Together, these payroll fraud practices undermine worker protections and deprive government programs of important revenue.

For an example of the heavy toll exacted by misclassification, consider the construction industry, where misclassification is rampant.[1] A recent report by the Midwest Economic Policy Institute describes the impact of payroll fraud in the construction industry on worker pay, benefits, and state revenue (Goodell and Manzo 2021). The study looked at misclassification and "off the books" construction work in Illinois, Minnesota, and Wisconsin. Specifically regarding the problem of misclassification, the study found that 10% of construction workers across these three states were misclassified as independent

Table 2

State revenue lost in 2018 due to construction worker misclassification in select states (in millions)

	Illinois	Minnesota	Wisconsin
Income taxes	$12.7	$4.2	$5.0
Unemployment insurance premiums	$15.5	$3.1	$5.2
Workers' compensation premiums	$69.3	$13.9	$23.2
Total	$97.5	$21.2	$33.4

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contractors—13% in Illinois, 5% in Minnesota, and 9% in Wisconsin—for a total of 55,784 misclassified workers. Independent contractors in construction in these three states earned 18% less than workers classified as employees—an average of $45,292 for independent contractors, compared with $55,463 for employees. Construction workers classified as employees received an additional $24,100/year in benefits, including paid leave, health care, retirement, Social Security premiums, Medicare, unemployment insurance, and workers' compensation. By classifying (or misclassifying) construction workers as independent contractors, employers reduce their labor costs by 29% in Illinois, 36% in Minnesota, and 31% in Wisconsin.

The lost revenue to the state is significant. As seen in **Table 2,** the Midwest Economic Policy Institute study estimated that the three states together lose $152.1 million annually in income tax payments, unemployment insurance premiums, and workers' compensation premiums from employers misclassifying construction workers as independent contractors.

Other states also experience high levels of misclassification in construction. A report by the Economic Roundtable found that in 2011, 19% of construction workers in California were misclassified as independent contractors (Sinroja, Thomason, and Jacobs 2019). Researchers found that between 12% and 21% of construction workers in the U.S. in 2017 were misclassified or working off the books (Ormiston, Belman, and Erlich 2020). About one-third of construction workers in the U.S. South were estimated to be misclassified (Weil 2017).

As previously explained, workers who are misclassified as independent contractors lose out on many important employment-based protections, including minimum wage and overtime protections, anti-discrimination protections, health and safety protections, and the right to organize and collectively bargain. The impact on workers' wages is significant, as shown by the millions of dollars of lost wages recovered when federal and state authorities sue employers for misclassification.[2]

Workers in California have lost millions of dollars in wages because of misclassification. For example, according to the California Legislature's labor committee report on AB5 (detailed below), the state cited a framing and drywall subcontractor for misclassifying more than 1,000 workers and depriving them of the minimum wage, overtime and rest

breaks on construction projects throughout the Los Angeles region.[3] The state ordered the company, RDV Construction, to pay more than $11.94 million in back wages and penalties for violations between 2014–2017. In another case, Calcrete Construction was cited for $6.3 million for cheating 249 construction workers out of their wages. The California labor commissioner regularly brings misclassification actions against California employers, recovering millions of dollars in back wages on behalf of affected workers (Calif. Lab. Com. 2018).

Long-standing misclassification of port workers

Port drivers at the Ports of Los Angeles and Long Beach have faced misclassification by their employers, among other workplace abuses, for decades. Drivers and their advocates have filed more than 1,000 wage claims, resulting in findings that the companies owe drivers more than $60 million in stolen wages and penalties.[4]According to an in-depth investigative report by USA Today, 97% of drivers' wage claims are successful, indicating rampant misclassification (Murphy 2017). According to advocates, in a limited number of cases, the wage claims have been successful in forcing companies to properly classify drivers as employees. Advocates point out, however, that these law-abiding companies then are undercut by companies that continue to rely on the illegal business model of misclassification (LAANE 2021).

As previously noted, states lose millions of dollars annually in tax revenue, and unemployment insurance and workers' compensation premiums from employers who are misclassifying workers. These losses are described in a comprehensive report by the National Employment Law Project (NELP 2020). Likewise, the California Department of Labor Standards Enforcement estimates that misclassification costs the state more than $7 billion annually.[5] The federal government, too, loses revenue. A 2009 report by the U.S. Government Accountability Office (GAO) found that the federal government lost $1.6 billion (in 1984 dollars) in tax revenue from employers misclassifying workers as independent contractors. This translates into $2.72 billion in 2006 inflation-adjusted dollars (GAO 2009).

The ABC test can deter misclassification

To address the problem of misclassification, more than 20 states have adopted what is known as the ABC test for determining whether an individual is an employee or an independent contractor for purposes of coverage of certain workplace laws. The ABC test got its name from the three, interlocking elements of the test—parts (A), (B), and (C). It establishes a presumption that an individual performing services for an employer is an employee, not an independent contractor, unless the employer can establish three factors (Mass. FLD 2021):

Table 3

States that have adopted the ABC test for unemployment insurance eligibility and/or wage and hour protections

State	ABC for unemployment insurance	ABC for wage/hour/other
Alaska	Yes	
California	Yes	Yes
Connecticut	Yes	Yes
Delaware	Yes	
District of Columbia	Yes for construction	Yes for construction
Hawaii	Yes	
Illinois	Yes	Yes for construction
Indiana	Yes	
Louisiana	Yes	
Maine	Yes	
Maryland	Yes	Yes for construction and landscaping
Massachusetts	Yes	Yes
Nebraska	Yes	Yes
Nevada	Yes	
New Hampshire	Yes	
New Jersey	Yes	Yes
New Mexico	Yes	
New York	Yes for construction	Yes for construction
Vermont	Yes	Yes
Washington	Yes	
West Virginia	Yes	

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- (A) The work is done without the direction and control of the employer.
- (B) The work is performed outside the usual course of the employer's business.
- (C) The work is done by someone who has their own, independent business or trade doing that kind of work.

By establishing a presumption of employee status and shifting the burden onto the employer to demonstrate the individual is truly an independent contractor in business on their own, the ABC test establishes a strong, protective, pro-employee test, which streamlines the process for workers to prove they are employees who have been misclassified as independent contractors.

As **Table 3** shows, many states have used the ABC test for purposes of their unemployment insurance programs for decades. Using a strong, protective test for this program both assures workers of important income when they are temporarily jobless, and ensures that employers are paying their fair share into the program by remitting unemployment insurance premium payments on behalf of all covered workers. As previously noted, the loss of revenue for social welfare programs like UI due to misclassification is a key reason why states have adopted the ABC test.

The Massachusetts story

Massachusetts, like other states, has been impacted by the misclassification problem, and the state has been a leader in addressing the issue. A major study from the Harvard Labor and Worklife Program in 2004 showed widespread misclassification, with significant impacts on workers, law-abiding employers, and state revenues. The study showed that from 2001–2003, 14% to 24% of all construction employers in Massachusetts misclassified construction workers as independent contractors, costing the state up to $152 million in lost income taxes, up to $35 million in lost unemployment insurance premiums, and up to $91 million in unpaid workers' compensation premiums (Carré and Wilson 2004).

The report provided added impetus for legislation establishing the ABC test for purposes of Massachusetts labor and employment laws, and Republican Gov. Mitt Romney signed the bill into law later that year. Experts in the state think adoption of the ABC test has improved legal compliance and reduced misclassification. The attorney general has brought dozens of enforcement actions against employers in construction, hospitality, cleaning and janitorial services, transportation and delivery, staffing and temporary agencies, and others, for misclassifying workers as independent contractors and failing to pay them all earned wages, including minimum wages, overtime, and earned sick time pay.[6] Recently, the attorney general brought a lawsuit against Uber and Lyft for misclassifying workers and denying them wages under the state's wage and hour law.

While acknowledging the importance of a strong legal test, advocates point out that the test, standing alone, is insufficient—strong enforcement is needed. As one state official put it, "Has having the ABC test helped? Of course it has helped. It establishes a presumption of employment and puts the burden on the employer to prove otherwise. But there are other ways to cheat, and unscrupulous employers continue to find new ways to cheat workers."[7]

The ABC test in play in California—and the sequel, Proposition 22

In April 2018, the California Supreme Court issued its decision in *Dynamex Operations West, Inc. v. Superior Court of Los Angeles, 4 Cal. 5th 903 (Calif. 2018).* Dynamex is a same-day courier and delivery service. Prior to 2004, the company treated its drivers as employees, but in 2004, the company converted all drivers into independent contractors. Two drivers brought a class-action lawsuit challenging their misclassification. In its decision in *Dynamex*, the California Supreme Court held that the ABC test was the appropriate test for evaluating employee status under California's Wage Orders, which contain portions of the state's wage and hour laws. The *Dynamex* ruling was hailed by worker advocates as a major step forward for workers.

State legislators, led by Assemblywoman Lorena Gonzalez, then introduced AB5, to codify the *Dynamex* decision into law. AB5 establishes that the ABC test is the operative test for determining coverage not only under California's Wage Order, but also under the California labor code, unemployment insurance, workers' compensation, and other labor laws, with certain limited exceptions.[8] According to subsequent reports and analyses, the legislation applies the ABC test to approximately 1 million janitors, maids and other cleaners, truck drivers, taxi drivers, retail workers, grounds maintenance workers, and child care workers, among others (LAO 2020; Thomason, Jacobs, and Jan 2019).

The legislation passed in September 2019, despite fierce lobbying against the bill by Uber, Lyft, and other platform companies. These same companies lobbied California Gov. Gavin Newsom to reject the legislation. Newsom ultimately signed AB5 into law (CA Gov. Ofc. 2019), but he authored an op-ed suggesting that a more flexible approach was needed (Newsom 2019). At the governor's urging, many meetings were held between the companies, the governor's representatives, unions, and others, but efforts at reaching a deal ultimately failed (Conger and Scheiber 2019; Eidelson 2021).

AB5 took effect on Jan. 1, 2020. Various industries continued to agitate and lobby for an exclusion from the law. Legislation providing additional exemptions from the ABC test for certain music industry professionals, performing artists, freelance writers and photographers, and individuals who provide underwriting inspections, premium audits, risk management or loss-control work for insurance or financial services industries passed and was signed in September 2020.[9] In the meantime, Uber and Lyft were sued by the California attorney general, the California labor commissioner and several city attorneys for misclassifying drivers as independent contractors. The lawsuits were successful in securing court rulings that drivers were employees under AB5, but that was undercut by the passage of Proposition 22, described below, such that only claims for unpaid wages predating the passage of Proposition 22 remain in litigation.

Even before AB5 was passed and signed, app-based platform companies, led by Uber and Lyft, announced that if they were not legislatively exempted from the law, the companies

would spearhead and fund a ballot initiative campaign to overturn AB5 as it applied to platform drivers (Calif. AG 2019). The ballot initiative that the rideshare companies sponsored, known as Proposition 22, the Protect App-Based Drivers and Services Act, was approved by voters in November 2020 after the platform companies spent more than $200 million on their campaign in support of the law (White 2020).

As a result of the passage of Proposition 22, more than 750,000 app-based drivers are now exempted from AB5 and deprived of employee status under California law (Jacobs and Reich 2020). Proposition 22 promises drivers an hourly income of at least 120% of the state minimum wage, plus a health care stipend, totaling a minimum of $15.60/hour. But according to researchers from the University of California, Berkeley, with deductions for taxes, expenses, and unpaid waiting time, the true guaranteed hourly wage for drivers could be as low as $5.64/hour.[10] In contrast, the hourly labor cost (including wages, taxes, health care, etc.) for a driver with employee status who is paid 120% of the California minimum wage would be approximately $30.93 (Jacobs and Reich, 2019; Reich 2020).

By winning an exemption from AB5, Uber and Lyft have avoided paying hundreds of millions of dollars into the California unemployment insurance system—a staggering $413 million from 2014–2019, and an estimated $115 million in 2018 alone (Jacobs and Reich 2020). Drivers are unable to draw regular unemployment benefits from the system. Because of the economic pain caused by the COVID-19 pandemic, Congress authorized unemployment benefits for independent contractors and loans to small businesses, including independent contractors. These programs are paid for by taxpayers, not employers. Tens of thousands of Uber and Lyft drivers have accessed these programs, meaning that the federal government—and taxpayers—financially supported the drivers through the pandemic, not Uber and Lyft. According to *The Washington Post*, tens of thousands of Uber and Lyft drivers received at least $80 million in government assistance during the coronavirus pandemic. More than 5,000 Uber and Lyft drivers received an average of $15,000 each in loans from the program (Siddiqui and Van Dam 2021).

Experience under *Dynamex* and AB5

The passage of AB5 strengthened protections for hundreds of thousands of California workers. An estimated 1 million workers whom employers have classified—or misclassified—as independent contractors are now covered by the ABC test, meaning their employers now will have the burden of meeting the strict criteria of the test to legally continue to exempt them from worker protection laws.[11] According to researchers at the University of California, Berkeley Center for Labor Research and Education, the most common occupations where the ABC test will apply include janitors, maids and other cleaners, truck drivers, taxi drivers, retail workers, grounds maintenance workers, and child care workers (Thomason, Jacobs, and Jan 2019).

Workers in California have not yet experienced the full benefits of AB5, for several reasons. First, the continued uncertainty around the passage, applicability, and permanence of AB5 led some companies to resist complying with the law. Some industries resisted reclassification and subsequently won legislative exemption for their industry. The

trucking industry brought—and recently lost—a lawsuit against the applicability of AB5 in that industry on grounds of federal preemption, and although the companies were unsuccessful, the litigation created uncertainty and delay in extending AB5 coverage to drivers.[12] The rideshare and delivery platform companies sought an exemption from the law, and when unsuccessful in winning it from the legislature, won it from the voters in November 2020. Some companies continue to disagree that their workers are employees, and are fighting efforts in the courts to require them to classify workers as employees under AB5.[13] And, less than two months after AB5 took effect, the COVID-19 pandemic struck, shutting down major parts of the California economy and shifting focus to other existential issues like unemployment benefits for unemployed workers, paid leave for workers who themselves or whose family members contracted the coronavirus, and health and safety protections for essential workers on the job. These factors, alone and in combination, have presented challenges to the implementation and enforcement of the law, and have muted AB5's impact. (They also have made it impossible to collect comprehensive data on the impact of the law.)

Importantly and disturbingly, the continuing efforts by platform companies and others to avoid the reach of AB5 have put enormous pressure on companies that continue to treat workers as employees. A vivid example involves delivery drivers for Safeway.

Grocery Delivery Drivers Lose Out to DoorDash

In November 2019, 150 drivers for Safeway.com in the San Francisco Bay area voted to form a union with the United Food and Commercial Workers International Union (UFCW). The drivers do home grocery deliveries, similar to DoorDash and Instacart. But unlike these platform companies, Safeway treats the drivers as employees. Bargaining began for a collective bargaining agreement, and a tentative agreement was reached in November 2020 that provided drivers with increased wages (up to $22/hour by the end of the contract's term), health benefits, paid time off, minimum hours, a health and safety committee to address hazards, and more. The agreement could have provided a model for other drivers at Safeway and other grocery chains. But then Proposition 22 passed, exempting platform-based delivery services from AB5 and the obligations of employee status. Because of the competitive threat presented by Instacart, DoorDash, and other app-based delivery services that treat their drivers as independent contractors, the month after reaching an agreement with the Safeway.com drivers, Safeway's parent company, Albertsons, signed a national deal with DoorDash to provide grocery delivery services at all but the unionized stores, and it began laying off its nonunion delivery drivers. Hundreds of Safeway.com drivers have lost their jobs (Dickerson 2021). Instead of the San Francisco unit sparking organizing drives among other Safeway delivery drivers, the San Francisco drivers stand alone, with two other Teamsters-represented units, as the only delivery drivers who are actual employees of Safeway.[14]

Instacart illustrates the downside to drivers being classified as independent contractors.

The number of people working on Instacart's platform jumped from 180,000 to 500,000 in eight weeks at the start of the COVID-19 pandemic, as more and more shoppers turned to home delivery to avoid in-person shopping.[15] Instacart drivers earn significantly less than drivers who are employees. Large companies like Albertsons and Kroger directly employ delivery drivers as employees with pay between $15 and $17/hour, depending on location, and pay is even greater where drivers are represented by a union. In contrast, one national survey of Instacart workers estimated median hourly gross earnings at $9.50 before deducting expenses (Benner et al. 2020). And, Instacart has shown itself to be hostile to workers joining together to improve their pay. In contrast to its delivery drivers, Instacart treats in-store shoppers as employees. Instacart in-store shoppers in Skokie, Illinois, voted to form a union in February 2020. Instacart responded by laying off the employees (Schiffer 2021).

As previously noted, some California employers have resisted complying with AB5, taking the position that their workers are independent contractors, notwithstanding the applicability of the ABC test. For example, Handy, a major app-based company that provides cleaning and handyman services, continues to maintain its workers are independent contractors, not employees. The district attorneys of San Francisco and Los Angeles have brought suit against Handy for misclassifying workers, seeking back wages and injunctive relief for thousands of workers. An estimated 17,000 Handy workers in California stand to benefit if the cities prevail in this litigation (LADA 2021; Iovino 2021).

Taking the show on the road: Platform companies look to expand Proposition 22's reach

After their success in passing Proposition 22, the rideshare and delivery companies pledged to pursue similar initiatives in other states and at the federal level (Feiner and Kolodny 2020). Uber officials said they hoped to "work with governments across the U.S. and the world to make this [the Proposition 22 approach] a reality" (Korosec 2020). As Uber CEO Dara Khosrowshahi said, "You'll see us more loudly advocate for new laws like Prop 22" (Eidelson 2020). The platform companies have lobbied the Biden administration and members of Congress for an alternative approach to employment protections for platform company workers, and are opposing the PRO Act, which would bring them under the fold of the National Labor Relations Act (Jaffe 2021). At the same time, states continue to sue Uber and Lyft for misclassification under state wage and hour and unemployment insurance laws, and at least three state courts have ruled that Uber has misclassified its drivers (Scheiber 2021).

The uncertainties created by the platform companies' aggressive campaign to be exempted from labor and employment laws has led some policymakers and advocates to explore ways of establishing some rights for drivers, such as collective bargaining rights, coverage under unemployment insurance, workers' compensation, and anti-discrimination laws, etc., without full employee status. A proposal for this "third category" of employment

(in between "employee" and "independent contractor") was floated in 2015 (Harris and Krueger 2015), and was roundly criticized by worker advocates, including EPI (Eisenbrey and Mishel 2016). Some unions have held discussions with state legislators, Uber, and Lyft about establishing a set of rights, including bargaining rights, premised on drivers remaining independent contractors for purposes of state law. Legislative proposals have been floated in Connecticut and New York, but they faced strong criticism from some drivers and worker advocates and, as of this report, have not proceeded (Eidelson and Penn 2021; Greenhouse 2021; Chen 2021).[16] However, Uber did reach a deal with a union in Great Britain to provide bargaining rights for drivers there (Eidelson, Milligan, and Levingston 2021).

The ABC test provides better protection for workers than other legal tests

The ABC test is stronger than other legal tests for determining whether an individual is an employee or independent contractor because it shifts the presumption to one of employee status, places the burden on the employer to prove independent contractor status, and strictly defines a narrow test for independent contractor status. In contrast, the Internal Revenue Service uses a 20-factor test that focuses on which entity controls how and when work is performed (IRS 2021b). The test is subject to manipulation and interpretation, and is further complicated by a "safe harbor" that excuses employers from misclassification if they are following industry practice (Erlich 2020).

The National Labor Relations Act (NLRA), establishing organizing and collective bargaining rights, and Title 7 of the Civil Rights Act, establishing anti-discrimination protections, utilize versions of the "common law" test, derived from court decisions over the years. The common law test, as articulated by the Restatement (Second) of Agency, uses 10 factors for evaluating whether an individual is an employee or independent contractor. It has been criticized for being overly subjective and open to manipulation (Garden 2019).

The broadest test, used under the federal Fair Labor Standards Act (FLSA) for purposes of determining minimum wage and overtime protections, is the six-factor "economic realities" test, which, as its name suggests, looks at the economic realities of the arrangement to determine whether an individual is in reality subject to the direction and control of the employer or in business for herself. The economic realities test derives from the FLSA's broad definition of employee, which states that an employee is any person whom an employer "suffers or permits" to work. The FLSA's test has been described as the broadest possible test ("A broader or more comprehensive coverage of employees within the stated categories would be difficult to frame," *U.S. v. Rosenwasser*, 323 U.S. 360 (1945)).

Elections have consequences:

Employee status under the Federal Fair Labor Standards Act and National Labor Relations Act

Workers who are deemed employees have minimum wage and overtime protections under the federal Fair Labor Standards Act, meaning they must be paid at least the minimum wage, and except for exempt workers, be paid 150% of their regular wage for hours worked in excess of 40 in a week. Workers who are classified as independent contractors have no such minimum wage or overtime protections, meaning they can be paid less than the federal minimum wage of $7.25/hour.

During the Obama administration, Wage and Hour Administrator David Weil issued an administrator's interpretation, explaining that under FLSA's language, most workers are employees and not independent contractors (DOL WHD 2015). Drawing from long-standing U.S. Supreme Court and federal circuit court decisions and settled agency interpretations, the guidance document explained how FLSA's economic realities test applies to independent contractor situations. Weil's interpretative guidance was lauded by workers' rights advocates as an important and helpful primer on employee status under the FLSA.

The U.S. Department of Labor in the Trump administration took a different tack. The Trump Department of Labor quickly withdrew Weil's interpretation (DOL 2017), and later issued an opinion letter stating that workers in a "virtual marketplace" were categorically independent contractors, not employees (DOL 2019). The Trump Labor Department then proposed and issued an interpretive regulation that took a very narrow view of employee coverage under the FLSA. According to an EPI analysis of the rule, an estimated 530,000 workers would be reclassified as independent contractors and lose employee status and protections as a result of the rule (Shierholz 2020). As seen in **Table 4,** EPI estimated that the Trump administration rule would cost workers $3.7 billion annually—at least $400 million in new annual paperwork costs, and $3.3 billion in lost compensation. EPI further estimated that social insurance funds would lose at least $750 million annually in the form of reduced employer contributions.

The new Biden administration moved quickly to restore workers' rights. It promptly withdrew the Trump administration's not-yet-effective interpretive regulation and opinion letter (Wiessner 2021). The Biden administration has proposed a $30.5 million increase in the Wage and Hour Division's 2022 budget, and has identified cracking down on misclassification as a priority, including supporting federal legislation to establish the ABC test for labor and employment laws (DOL WHD 2021).

Table 4

Annual impact of proposed Trump administration rule making it easier for employers to classify workers as independent contractors

Total annual cost to workers	At least $3.7 billion
Cost to workers of new ongoing paperwork	At least $400 million
Tax obligations on workers	At least $3.3 billion
Lost revenue for unemployment insurance and workers' compensation funds	At least $750 million

Economic Policy Institute

Employer status under the National Labor Relations Act

Questions over employee status and misclassification have also played out at the National Labor Relations Board (NLRB), the federal agency that enforces workers' collective bargaining rights. Workers who are classified as independent contractors are not covered by the NLRA, so have no federal right to organize and collectively bargain. As previously indicated, the legal test for employee status under the NLRA is the multifactor common law test.[17] The NLRB and reviewing courts look to the Restatement (Second) of Agency and its 10-factor common law test for determining whether an individual is an employee or an independent contractor (*FedEx Home Delivery v. NLRB* (D.C. Cir. 2017)). The NLRB majority appointed by President Obama issued several decisions finding truck drivers, canvassers, and other workers to be employees, not independent contractors.[18] The Obama-appointed NLRB General Counsel brought a number of complaints alleging that employers commit an unlawful unfair labor practice when they misclassify workers as independent contractors.

However, Trump appointees on the NLRB took a more restrictive view of the law. The Trump NLRB issued decisions finding workers to be independent contractors, saying they would evaluate the 10 common law factors through the prism of entrepreneurial opportunity, and taking a broad view of that term to deny workers coverage.[19] The Trump appointees also rejected the complaint brought by the Obama-appointed NLRB General Counsel, refusing to find misclassification to be a violation of the NLRA.[20] The Trump-appointed NLRB General Counsel issued a memorandum concluding that Uber drivers are independent contractors, not employees, and therefore outside of the NLRA's protections

(NLRB GC 2019).[21]

Because the NLRA does not include an independent right of workers to bring their own claims of employer unfair labor practices directly to the NLRB or a court, this conclusion by the Trump NLRB General Counsel deprived hundreds of thousands of Uber drivers and other similarly situated workers of their federally protected organizing and bargaining rights. A new NLRB General Counsel and new majority on the NLRB could reverse course and determine that app-based rideshare drivers are indeed employees covered under the NLRA.

Establishing the ABC test for collective bargaining rights—the PRO Act

In order to better define "employee" in a way that assures broader coverage and protection for workers, Rep. Bobby Scott (D-Va.) and Sen. Patty Murray (D-Wash.), the chairs of their respective labor committees, have introduced the Protecting the Right to Organize (PRO) Act (H.R. 842, S. 420), which, among many other provisions, adopts the ABC test for purposes of coverage under the NLRA.

The PRO Act passed the U.S. House of Representatives with bipartisan support in March 2021 and is pending in the U.S. Senate, where 47 senators have signed on as co-sponsors. Passage of the PRO Act is a top priority for the labor movement and its allies. Because of the significance and implications of establishing the ABC test for purposes of federal labor law on their operations, gig companies have lobbied heavily against the PRO Act (Cassel and Adams 2021).

Employee status is gaining attention internationally

Issues of employee status, the need to protect workers against misclassification as independent contractors, and the question of legal protections for platform-based workers continue to generate significant interest and attention in the European Union (EU) and at international labor bodies. EU countries have taken different approaches to the issue, with some adopting varying laws on the protections to be provided to workers. The International Labour Organization recently issued a comprehensive report on the topic, describing the variety of approaches and noting the importance of the employment relationship to worker protections, as addressed by ILO Recommendation 198 (De Stefano et al. 2021).

Recently, the Supreme Court in the United Kingdom ruled that Uber must treat its 70,000 drivers as workers—an intermediate category of employment—and pay them the minimum

wage. After initially resisting, Uber announced it would comply with the court's decision, and it later reached a deal to provide drivers with collective bargaining rights (Satariano 2021). Spain recently enacted a law requiring platform companies to classify drivers as employees (Parra and Brito 2021). International labor organizations have called for strengthened protections for workers engaged in nonstandard forms of work, including independent contractors and platform workers (ITUC 2019). The European Commission is examining whether to issue a directive that would redefine the scope of EU competition law to enable collective bargaining under some circumstances for the solo self-employed (European Commission 2020). Thus, in the EU and Britain, as in the United States, the issue continues to be a focus of attention by policymakers, advocates, and business.

Conclusion: A strong test and strong enforcement are vital

Employee status under U.S. labor and employment laws is essential to fundamental workplace rights, benefits, and protections. A strong, protective legal test for establishing employee status is critically important to combat employer misclassification of employees as independent contractors, and help ensure workers get the rights, benefits, and protections they are due, governments are not wrongly deprived of important revenue for social protections, and law-abiding employers are not undercut by employers engaging in fraud. Efforts to establish the ABC test as the prevailing test continue in the states and in Congress, as do efforts by platform companies to avoid the reach and obligations under these laws. In the meantime, in the absence of a uniform ABC test and strong enforcement, workers continue to be misclassified by their employers and deprived of important rights and protections. These are issues with real-life impact on working people and their standard of living that policymakers need to address.

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Endnotes

1. One expert points to two factors in particular that have led to the misclassification problem in construction: the adoption of the Section 530 safe harbor under the Internal Revenue Code, and the push from a general contractor model on construction projects to a construction manager model, with multiple, separate contractors. See Erlich 2020.

2. For examples of lost wages from misclassification, see Weil 2017, 2019.

3. A.B. 5, 2019–20 Assemb., Reg. Sess. (Cal. 2019).

4. Drivers have also participated in class-action lawsuits and have pursued charges at the National Labor Relations Board, among other actions. See LAANE 2021.

5. A.B. 5, 2019–20 Assemb., Reg. Sess. (Cal. 2019).

6. For a comprehensive database of enforcement actions taken by the attorney general against employers since 2015, see Mass. AG 2021.

7. Author interview with Cynthia Mark, chief, Public Protection & Advocacy Bureau, Office of the Attorney General, May 17, 2021.

8. A.B. 5, 2019–20 Assemb., Reg. Sess. (Cal. 2019).

9. A.B. 2257, 2019–20 Assemb., Reg. Sess. (Cal. 2019).

10. Uber and Lyft have lowered driver pay since the passage of Proposition 22. See Sainato 2021. A lawsuit brought by drivers and worker advocates seeking to overturn Proposition 22 is pending. See Mulvaney 2021.

11. According to the California Legislative Analyst's Office (LAO), AB5 applies to approximately 1 million Californians working as independent contractors. The LAO report explained that it could not estimate the number of contractors who would be converted to employees because that is dependent on various unknown factors, including whether businesses would change their model to continue hiring independent contractors. See LAO 2021.

12. *California Trucking Association v. Bonta* (9th Cir. 2021).

13. For example, Jan-Pro, a national janitorial and cleaning services company, has been sued for misclassifying workers as independent contractors, and continues to resist reclassifying its workers even after AB5's passage. See CleanLink 2019.

14. In a more hopeful example, delivery drivers for Imperfect Food—a food delivery app—recently voted to form a union with the United Food and Commercial Workers (UFCW). But the passage of Proposition 22 makes it difficult for other drivers to follow suit because of the incentives the measure creates for companies to treat drivers as independent contractors. See Harnett 2021. In another hopeful sign, there are indications that major grocery chains are looking to bring delivery services back in house so as not to lose the customer connection—and customer data—to a third party. See Benner et al. 2020.

15. Prior to the pandemic, 2% of grocery sales were online; estimates are that as much as 10% will be

done post-pandemic. See Benner et al. 2020.

16. Collective action by independent contractors also raises antitrust issues, as demonstrated by the court decision striking down Seattle's ordinance to provide collective bargaining rights for platform drivers (*Chamber of Commerce v. City of Seattle*, 890 F.3d 769 (9th Cir. 2018)). The draft New York legislation contained provisions seeking to address these issues by requiring the state to approve collectively bargained terms.

17. *National Labor Relations Board v. United Insurance Co. of America et al.*, 390 U.S. 254 (1968).

18. See, e.g., Fed Ex Home Delivery, 361 NLRB 610 (Sept. 30, 2014) (Fed Ex home delivery drivers are employees, not independent contractors); Sisters' Camelot, 363 NLRB No. 13 (Sept. 25, 2015) (canvassers are employees, not independent contractors); Minnesota Timberwolves Basketball, 365 NLRB No. 124 (Aug. 18, 2017).

19. SuperShuttle, 367 NLRB No. 75 (Jan. 25, 2019) (holding that SuperShuttle drivers are franchisees, not employees.

20. National Labor Relations Board, Velox Express, Inc. and Jeannie Edge, 368 NLRB No. 61 (Aug. 29, 2019).

21. For a critique of the Advice Memorandum, see Mishel and McNicholas 2019.

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