Construction Workers and the Gig Economy

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Last September, California Governor Gavin Newsom signed Assembly Bill 5, which imposes stringent criteria to determine whether a worker is an employee or an independent contractor. What may seem like an arcane definition of employment law generated enormous controversy. The California Chamber of Commerce, business associations, and gig economy employers strenuously opposed the bill. Uber, Lyft, DoorDash, and other similar companies argued that AB 5 posed a fundamental threat to their business model, one that relies on drivers to operate as independent contractors.

The outsized nature of the California economy and the pervasive influence of Silicon Valley drew national attention to the legislative battle. Prior to the attention focused on AB 5, the debate over the legitimacy and legality of independent contracting had been limited to employment professionals, union activists, academics, attorneys, and federal and state wage enforcement agencies. But the misclassification of employees as independent contractors is not a new issue, nor is it restricted to ride sharing and gig firms. Silicon Valley executives may justify the status in terms of work schedule flexibility and the opportunity to "be your own boss," but in reality, employers misclassify workers simply to save money and minimize accountability. A firm that designates its workforce as independent contractors evades responsibility for the payment of state and federal taxes as well as workers' compensation insurance premiums, resulting in up to 30 percent savings in labor costs. Workers lose basic rights including legal entitlements to minimum wage and overtime payments, paid sick leave, unemployment insurance in case of layoff, workers' compensation benefits in case of an on-the-job injury, anti-discrimination protections, and the right to form a union and collectively bargain. Misclassification is a business model that depends on tax, insurance, and payroll fraud. It is an assault on a century of hard-won workers' rights.

On December 30, Uber and Postmates filed suit to block the law, claiming that is was a "thinly veiled attempt" to harm gig economy businesses. In February, a federal judge denied the companies' request for a preliminary injunction to prevent enforcement but the underlying suit is still on the docket. The CEOs of Uber, Lyft, and DoorDash have threatened to spend hundreds of millions of dollars on a referendum campaign to undo AB 5. The litigation and threats garnered headlines, but the bill may have just as large an impact on more traditional industries, such as construction, trucking, hospitality, and janitorial services. In particular, non-union construction employers have misclassified their workers for decades in order to lower costs, largely motivated by the desire to avoid the high workers' compensation premiums that accompany work in a dangerous industry. They now have a well-established system in which workers function as employees in every respect but are classified as independent contractors. The practice has been one of the principal elements underlying the loss of union market share and the inexorable decline of wage and safety standards in the U.S. construction industry.

Misclassification was an integral part of the broader abandonment of the post–Second World War social contract, the fissuring of the economy, and the business community's strategy of shedding obligations for employees through the increasing use of outsourcing, subcontracting, and franchising. In many ways, misclassification was an easy stratagem to use in construction, an industry with large numbers of legitimate sole proprietors and independent contractors.

Construction workers in New York City in 2017 (Gordon Zheng/Wikimedia Commons)

Federal and state laws contain a variety of definitions of what constitutes an employee versus an independent contractor, but the simplest common-sense distinction is that if workers operate under the direction and control of another, they are employees. The solo plumbers who install or repair toilets or water heaters at a residence may well work on their own, scheduling appointments, ordering materials, performing the work, and collecting payments. But the thousands of drywall carpenters, wood framers, painters, roofers, and other trades workers who show up every day at multi-million-dollar project jobsites working under the direction of a foreman with company-provided power tools and materials are no more independent contractors than any conventional employee. Today, there are an estimated 300,000 construction workers in the United States who are improperly classified as independent contractors and another 1.2 million construction workers who are paid off the books in cash.

The legal sanction for misclassification can be traced back to 1978, when Congress granted a “safe harbor” in the tax code to employers that operated in industries where the use of independent contractors was a “long-standing recognized practice.” Decades later, in 2014, a high-level Internal Revenue Service officer argued that the safe-harbor provision served as a green light for construction contractors to transform the industry into what he termed the “Wild West.” In 1987, a Q&A fact sheet at the largest national construction employers’ convention posed the question: “What if I decide just to give up and have no one in my business other than independent contractors and leased employees?” The very existence of the question provided its own answer. The wide acceptance of misclassification created a cottage industry of lawyers, accountants, and consultants that advised contractors how to increase profits by moving their workforce off payrolls. In 2001, the American Bar Association’s Construction Lawyers Guide included a five-page boilerplate independent contractor agreement for construction employers to use with their workers.

Two important changes happened to the role of misclassification in the economy around the turn of the twenty-first century. The first was driven again by developments in construction. The growing participation of immigrant workers—in particular, undocumented workers—in construction eliminated much of the need for legally sophisticated independent contractor agreements with individual trades workers. Between 1990 and 2000, Pew reported that the proportion of Hispanic male workers in construction increased four times as fast as the increase of white male workers. By 2006, nearly one-third of recently arrived foreign-born Hispanic workers were in construction. By 2014, undocumented immigrants made up 15 percent of the total national construction workforce, actually outnumbering immigrant workers with valid working papers. These vulnerable workers received low wages and feared reprisals in the face of all-too-common instances of wage theft. High-priced lawyers and accountants were replaced by labor brokers who trafficked workers from Mexico and Central America to construction sites in the United States. A system of extensive paperwork and the issuance of 1099 tax forms at the end of each year was replaced by payments in cash with little or no reporting or recording of the transactions.

The growth of the gig economy also shifted the perception of the use of independent contractors. Instead of independent contracting being simply a cost-saving (and potentially illegal) method of employment that eradicated workers' rights, the classification was increasingly promoted as a desirable alternative to the dreary rat-race of employee wage slavery. As the founder of Pasona, one of the world's largest temporary staffing agencies, said in 2007: "Be a regular worker—and be exploited for the rest of your life." As an alternative, he proposed the life of an independent contractor, which supposedly offered the allure of independence, individualism, flexibility, and entrepreneurialism. The ideological spin attempted to transform independent contracting from an obligation-evading scam into a transcendent model for twenty-first-century employment. As the managing director of a nonprofit school charged with teaching low-income workers how to develop skills for the new sharing economy told the *San Francisco Chronicle* in 2017: "Everyone can be their own CEO."

But the bloom appears to be off the rose for many gig companies. Uber and Lyft's much ballyhooed IPOs landed on Wall Street with a remarkable thud. More important, gig workers are increasingly challenging working conditions and company policies. Among the many creative job actions of 2019, Uber and Lyft drivers staged a twenty-four-hour strike in May and in February of this year launched a global network of app-based drivers. Also in February, U.S. District Judge William Alsup of the North District of California ordered DoorDash to engage in individual arbitration with over 5,000 couriers who claimed they were misclassified as independent contractors. Ironically, DoorDash had proposed a class-wide lawsuit in order to avoid the $10 million in arbitration filing fees after initially insisting on arbitration as an alternative to class-action litigation. "This hypocrisy will not be blessed, at least by this order," wrote Judge Alsup.

Since the inception of the ridesharing firms, executives had told their drivers that the highly prized flexible scheduling aspect of their work was contingent upon the status of independent contracting. For the most part, drivers hesitated to challenge this misleading legal claim as long as "the money was decent," according to Los Angeles–based Rideshare Drivers United organizer Ivan Pardo. "But once pay began dropping to subminimum wage levels in 2017 and 2018," continued Pardo, "drivers began to re-evaluate their relationship with the employers. And as conditions deteriorated further in 2019 and AB 5 entered the scene, drivers in California began to see reclassification and a union contract as the best path to secure better pay and fair treatment."

AB 5 codified a 2018 California Supreme Court ruling that established the "ABC test" as the determinant of employment status. The ABC test presumes a worker is an employee unless three clear and simple criteria (the contractor is free from control and direction by the hiring company, performs work that falls outside the usual course of its operations, and is "customarily engaged" in similar independent work) are met. It is the cleanest and strongest of the numerous definitions in state and federal law and had been adopted in Massachusetts in 2004. In the past, much of the regulatory emphasis had been on construction misclassification because the violations were so obvious, egregious, and extensive. In fact, the ABC test is already in place for construction in New York and New Jersey. New York, New Jersey, and Illinois are also considering expanding the test to gig economy employers as a result of AB 5.

At the federal level, the U.S. Department of Labor (DOL) had also become more actively engaged in the discussion of misclassification after the 2014 appointment of labor market policy expert David Weil as the DOL's Administrator of the Wage and Hour Division. In 2015, Weil issued a lengthy Administrator's Interpretation (AI) that concluded, based on the Fair Labor Standards Act definitions, that "most workers are employees." Weil negotiated a series of memoranda of understanding with state enforcement agencies to coordinate federal and state actions against employers that misclassified. Now based at Brandeis University, Weil weighed in on the AB 5 discussion in a July 2019 *Los Angeles Times* op-ed, arguing that rideshare drivers were in fact employees who happened to work under "a management system based on software rather than human beings."

Unsurprisingly, as with numerous other Obama-era policies, the Trump administration has reversed course on this and deleted the AI from the DOL website. In April 2019, the general counsel of the National Labor Relations Board (NLRB) determined that Uber drivers are independent contractors. Two weeks later the DOL concluded that the workforce of an unidentified firm that operated in the "on-demand" or "sharing" economy should be considered independent contractors. Again, as with so many developments in the Trump era, a significant number of states have taken the opposite stance and actually ramped up enforcement activities regarding payroll fraud and wage theft. The same month that the NLRB and the DOL released their opinions, Michigan, Montana, and Wisconsin announced the creation of taskforces to combat employee misclassification. In response to the federal rulings, New Jersey labor commissioner Rob Asaro-Angelo suggested that the DOL "opinion letter has zero effect on how the New Jersey Department of Labor enforces state laws."

A number of state agencies have recently filed valuable civil and criminal cases against violations in the trades sector, alongside examples of private class-action suits and litigation. In the last several months alone, the District of Columbia's attorney general's office settled with a major electrical contractor for $2.75 million for the misclassification of 535 workers, the New York City district attorney's office indicted a construction labor broker for defrauding $1 million in workers' compensation premium payments, a Minnesota construction contractor pleaded guilty to labor trafficking undocumented workers, and the New Jersey Department of Labor fined Uber $649 million for misclassification. On the other hand, industry lobbyists have successfully pushed through gig company "carve-out" bills in seven red states that allow independent contracting for transportation network companies and similar gig firms by exempting that sector from state employment laws.

The size of the gig economy should not be exaggerated. A recent study by the U.S. Bureau of Labor Statistics reported that only 1 percent of the nation's workforce performs "electronically mediated work." Construction, to take just one example, is a much larger industry and has been plagued by misclassification for far longer. But construction is perceived as an archaic industry, resistant to change and largely untouched by the wonders of technology. In this view, ridesharing and other forms of platform work represent the future, both in terms of algorithmic sophistication and the organization of labor.

The vast majority of American workers are still on payrolls and operate under the terms and conditions of the standard employment model. Yet the modern workplace has become more precarious, both in terms of declining job security and the disappearance of traditional benefit plans. The postwar notion of a paternalistic employer obligation to a workforce has largely evaporated. Much of the current debate on the future of work revolves around robotics, artificial intelligence, and the other shiny transformative toys that technology can produce. There is far less discussion about the future of worker protections.

Certainly, the overheated reaction of employers to the passage of AB 5 is a recognition that their favored business model may be at risk. David Nelson, the public policy director of the California Asian Pacific Chamber of Commerce, direly predicted that "forcing ride-share and delivery drivers to become employees would significantly limit the availability and affordability of these services to exist." The impending lawsuits and the proposed ballot initiative to reverse AB 5 will determine the viability of the new law. The stakes are high. In the words of a pro-AB 5 spokesman, "we're going to spend what it takes to win."

The adoption of the ABC test in a number of states represents an alternative path to the individualistic vision of workers left to fend for themselves. The test is not a silver bullet, and its value should not be overstated, but it does help preserve basic worker protections. Even the strongest examples of legislation, however, are only meaningful if there is a parallel commitment to aggressive regulatory enforcement of the laws at both the federal and state levels.

AB 5 took effect in California on January 1. Despite a significant number of occupational carve-outs in the bill, the state's Legislative Analyst's Office estimates that roughly a million workers may need to meet the ABC test to continue as independent contractors. Governor Gavin Newsom's budget allocates $21.68 million to enforce AB 5, but it is still too early to determine how the law will be interpreted and implemented. In any case, there is no chance of coordinated federal enforcement under the current administration. Officials in a number of states are also reluctant to be overly aggressive, for fear of appearing to quash innovation and alienate an influential and high-profile sector of the economy.

Enacting and enforcing strong employment laws is a precondition for elevating worker standards. Uber and Lyft drivers cannot form unions unless they are considered employees, and the likelihood of a return to a high-wage unionized construction industry in every part of the country is slim without a sustained attack on all forms of payroll fraud. Treating workers as employees establishes a floor for basic protections. The broader challenge will be to use that floor as a springboard to organize the growing number of precarious occupations.

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