



Washington Is Out of Touch with the 21st Century Workforce

Jared Meyer
Fellow, Economics21
Manhattan Institute for Policy Research

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Introduction

Chairman Walberg, Ranking Member Wilson, and other Members of House Education and the Workforce Committee, thank you for the opportunity to give testimony on how new administrative interpretations of the Fair Labor Standards Act of 1938 fail to reflect the realities of today's workforce.

I am a fellow at Economics21 at the Manhattan Institute for Policy Research and am the coauthor, with Diana Furchtgott-Roth, of *Disinherited: How Washington Is Betraying America's Young*.¹ I am also the author of *Uber Positive: Why Americans Love the Sharing Economy*.² Since this summer, I have traveled across the country and heard millennials talk about the economic challenges they are facing and their plans for the future.

The American economy is changing, and millennials' attitudes about work and their careers are changing with it. The rapid rise of the so-called "sharing economy" embodies many young Americans' new economic ideal – one driven by technology, convenience, and flexibility. However, government policy, particularly in regards to labor regulation, ignores the realities of a 21st century economy and continues to hold back millennials' economic opportunities.

Millennials want to be entrepreneurs, and they desire employment that is flexible, mobile, and individualized. The Department of Labor's attempts to stifle the rise of promising new business models through regulation is no way to help millennials achieve their vision of the American Dream.

What Is the Sharing Economy?

Entire industries are being transformed, consumers have more power than ever before, and people are finding new ways to earn a living – even in today's slow economic recovery. All of these improvements stem from the rise of the so-called sharing economy. However, groundbreaking business models are in danger of being suppressed because of overzealous labor regulation that codifies outdated views of the workforce.

While much has been written about novel sharing-economy business models and the opportunities that they create, the idea behind the sharing economy is nothing new.

¹ Diana Furchtgott-Roth and Jared Meyer, *Disinherited: How Washington Is Betraying America's Young*, Encounter Books, May 2015.

² Jared Meyer, *Uber-Positive: Why Americans Love the Sharing Economy*, Encounter Book, April 2016.

What sets these innovative companies apart from those of the past is their ability to use the Internet and smart phones to easily connect those who want something with those who have something to offer. The Internet offers easy access to an online platform that facilitates transactions between buyers and providers of goods or services. These transactions are the basis of the sharing economy.

Peer-to-peer online interaction, made available only recently by technological advances, is behind everything from eBay and Airbnb, to Zipcar and EatWith, to TaskRabbit and Uber. There have always been people who want to buy a hard-to-find product, find a place to stay, eat a home-cooked meal, get assistance on a task, or find a way to get around. The problem was finding someone who was willing to offer the desired goods or services at a reasonable price. Imagine going from door to door, asking home owners if they had an extra room to rent and for how much. Now, travelers simply have to log on to Airbnb, and, with a few clicks of a mouse, they can find a room that fits their needs and budgets.

Companies such as Uber and Airbnb offer the technical platform and support to allow transactions between buyers and sellers or service providers to easily take place. For this reason, these types of companies are often referred to as “intermediaries.”³ Those who partner with intermediaries are classified as independent contractors, not employees.

Before intermediaries existed, the difficulty of matching buyers with sellers led to the rise of many types of industries, such as those of the taxi and travel agency, that built their business models around the lack of consumer empowerment. Now, with the sharing economy’s rapid expansion, these industries are facing increased competition.

These benefits of reduced transaction costs for workers do not end with those who partner with intermediaries. They also extend to entrepreneurial skilled professionals, such as photographers, personal trainers, academic tutors, lawyers, and accountants, who are now able to find customers and promote their businesses at much lower cost.⁴

The flexibility that independent contractor status offers workers is vital to the sharing economy’s success. While some workers use these platforms full time, the vast majority use them for part-time work or supplemental income. About 8 in 10 Lyft drivers choose to drive 15 hours a week or less, and half of Uber drivers use the platform for less than

³ Seth Harris and Alan Krueger, *A proposal for modernizing labor laws for 21st century work: The “independent worker”*, The Hamilton Project, December 2015.

⁴ Jon Lieber and Lucas Puente, *Beyond the Gig Economy: How New Technologies Are Reshaping the Future of Work*, Thumbtack, March 2016.

10 hours a week.⁵ Independent contractor status allows the decision of when or for how long to work to be controlled by workers, not companies.

Control over one's hours is a valuable option for many Americans that needs to be maintained. An independent survey of 3,100 Lyft drivers found that 82 percent of the drivers agreed or strongly agreed with the statement, "I like being an independent contractor." Since flexibility is one of the main benefits of the sharing economy model, it is not surprising that 99 percent of Lyft drivers agreed that with the statement that "I like to choose when I work."⁶

Though surveys can encourage respondents to answer in a particular fashion and should not be taken as authoritative, the overwhelming number of favorable responses points to the conclusion that Lyft drivers value their independent contractor status.

Uber drivers share the same sentiment. When 600 Uber drivers were asked the question, "If both were available to you, at this point in your life, would you rather have a steady 9-to-5 job with some benefits and a set salary or a job where you choose your own schedule and be your own boss?" 73 percent said that they prefer flexibility over the traditional employment model.⁷

An analysis of its customers' bank accounts by JPMorgan Chase & Co. shows that one out of every 100 Americans earned income through a sharing economy platform in September 2015.⁸ This is up from one in every 1,000 in October 2012. Over the three-year study, over 4 percent of Americans earned income through the sharing economy.

While the sharing economy still accounts for a small percentage of overall U.S. employment, the individualized work arrangements that it embraces make up a much larger, and growing, percent of the labor force.⁹ For the 70 percent of Americans ages 18 to 24 who experience an average change of over 30 percent in their monthly incomes, the opportunity to smooth out earnings to meet rent, pay down student loans, or fund a new business venture is a benefit of the sharing economy that must be protected.¹⁰

⁵ Jonathan Hall and Alan Krueger, *An Analysis of the Labor Market for Uber's Driver-Partners in the United States*, January 22, 2015.

⁶ Keker & Van Nest LLP, *Declaration of Simona A. Agnolucci in Support of Lyft, Inc.'s Brief Regarding Preliminary Approval of Class Action Settlement*, March 17, 2016.

⁷ Jonathan V. Hall and Alan B. Krueger, *An Analysis of the Labor Market for Uber's Driver-Partners in the United States*, Uber, January 22, 2015.

⁸ *Paychecks, Paydays, and the Online Platform Economy*, JPMorgan Chase & Co., February 2016.

⁹ Will Rinehart and Ben Gitis, *Independent Contractors and the Emerging Gig Economy*, American Action Forum, July 29, 2015.

¹⁰ *Paychecks, Paydays, and the Online Platform Economy*, JPMorgan Chase & Co., February 2016.

For example, working with Uber supplies the only source of income for 20 percent of Uber drivers.¹¹ But Uber earnings provide supplemental, non-significant income for 48 percent of drivers.

Furthermore, half of Lyft's drivers work another job while partnering with the company, and three out of ten work another full-time job.¹² Similarly, two-thirds of Uber drivers hold another full- or part-time job.¹³

Policymakers often fail to realize that a 21st century economy cannot flourish while it is under the thumb of labor laws and regulations that are inapplicable to today's workforce. Economies grow through a dynamic process that necessitates change and disruption. Forcing new business models to comply with labor laws and regulations that limit entrepreneurship is no way to promote a dynamic market.

Millennials' Yet-Unrealized Entrepreneurial Dreams

The sharing economy's rise obscures a troubling economic trend. Once dynamic, the American economy is now growing slowly. The Brookings Institution reports that business startup rates are much lower now than they were in the second half of the 20th century.¹⁴ Business dynamism, determined by firm entry, firm exit, and job reallocation rates, has also declined. This fall in entrepreneurship is leading to the aging of American businesses. In 1992, 23 percent of firms had existed for 16 years or more. By 2011, this percentage had increased to 34 percent.¹⁵

New business formation is vital for economic growth. Young Americans desperately need more employment opportunities, as 20- to 24-year-olds still face an unemployment rate of over 8 percent.¹⁶ For teenagers, the unemployment rate is 16 percent.

A decline in entrepreneurship is troubling for the economy for a variety of reasons — especially when starting a business is seen as a major part of the American dream for many millennials.

¹¹ *Uber Driver Roadmap 2.0*, Benenson Strategy Group, November 14, 2015.

¹² Kecker & Van Nest LLP, *Declaration of Simona A. Agnolucci in Support of Lyft, Inc.'s Brief Regarding Preliminary Approval of Class Action Settlement*, March 17, 2016.

¹³ *Uber Driver Roadmap 2.0*, Benenson Strategy Group, November 14, 2015.

¹⁴ Ian Hathaway and Robert E. Litan, *Declining Business Dynamism in the United States: A Look at States and Metros*, Brookings Institution, May 2014.

¹⁵ Ian Hathaway and Robert E. Litan, *The Other Aging of America: The Increasing Dominance of Older Firms*, Brookings Institution, July 31, 2014.

¹⁶ *The Employment Situation*, Bureau of Labor Statistics, March 4, 2016.

Millennials have been called the most entrepreneurial generation. While this may be true based on their desires to start businesses and their near-universal respect for entrepreneurs such as Steve Jobs, few young Americans have followed through on their entrepreneurial dreams. Millennials' failure to start businesses follows the troubling trend of declining entrepreneurship and dynamism in the U.S. economy.

A Bentley University survey of millennials found that 66 percent of respondents want to start their own business.¹⁷ Echoing these findings, Deloitte found that about 70 percent of millennials envision working independently at some point in their careers.¹⁸

Yet, as of 2013, only 3.6 percent of private businesses were at least partially owned by someone under the age of 30. This is the lowest proportion since the Federal Reserve began collecting data nearly a quarter-century ago.¹⁹

The U.S. Department of Labor's effort to make it more difficult for independent contractors to work is an example of regulation that fails to comprehend the realities of today's economy by limiting entrepreneurial work.

The distinction between contractors and full-time employees can have important implications for millennials. The American Dream may have once been finding employment at a large company, working there for a few decades, and then retiring with a defined-benefit pension, but now millennials' American Dream looks much different than their parents' and grandparents'. New opportunities to change or advance one's career are prioritized, and individualized, flexible work arrangements are the model of the future.

DOL's Fight Against Independent Contractors

The Labor Department recently issued an administrator's interpretation, effective immediately, to clarify the definition of an independent contractor. It states that "most workers are employees," not independent contractors.²⁰ Because it was termed "guidance," it did not have to go before the public for comment, even though it has the potential to upend the sharing economy.

¹⁷ *The Millennial Mind Goes to Work*, Bentley University, November 11, 2014.

¹⁸ *The Deloitte Millennial Survey*, Deloitte, January 2014.

¹⁹ Ruth Simon and Caelainn Barr, *Endangered Species: Young U.S. Entrepreneurs*, *The Wall Street Journal*, January 2, 2015.

²⁰ David Weil, *Administrator's Interpretation No. 2015-1*, Department of Labor, July 15, 2015.

The popularity of the sharing economy has propelled the distinction between independent contractors and employees into the forefront of policy. This is an important debate that the public needs to take part in through the legislative process. Congress cannot continue to let unelected bureaucrats determine the future of America's labor market outside of public view.

Currently, workers are either categorized as employees or independent contractors. Employees are given many protections and benefits under the Fair Labor Standards Act that are not available to contractors. In exchange, employers set the conditions of workers' terms of employment. On the other hand, the independent contractor model provides workers with more control and flexibility.

The Labor Department's new interpretation formally accepts the six-part "economic realities" test for determining whether workers are employees or independent contractors.²¹ At the same time, it downplays one of the six criteria, a lack of control over workers' hours, as a determinant of employment status.

Shifting from independent contractors to employees is costly. The Labor Department's Employment Cost Index shows that providing benefits adds around 30 percent to the cost of employing a worker.²² This estimate is not an overstatement. When MyClean (the Uber of housecleaning) moved from independent contractors to full-time employees, its labor costs increased 40 percent, according to its CEO.²³ A similar company, Homejoy, shut down this year due to labor classification disputes.²⁴

Something similar could happen to Uber, as one California driver who brought a case against the company was legally classified as an Uber employee.²⁵ If this ruling against Uber's current business model in *Berwick v. Uber Technologies, Inc.* is extended to the rest of the company and the emerging sharing economy as a whole, many other startups and workers will suffer.

²¹ *Fact Sheet 13: Am I an Employee?: Employment Relationship Under the Fair Labor Standards Act (FLSA)*, Department of Labor, May 2014.

²² *Employment Cost Index*, Bureau of Labor Statistics, October 2015.

²³ Kate Rogers, *What the Uber, Lyft lawsuits mean for the US Economy*, CNBC, March 16, 2015.

²⁴ *Homejoy says goodbye, and thank you*, Homejoy, July 17, 2015.

²⁵ *Barbara Berwick v. Uber Technologies, Inc.*, California Labor Commission, June 16, 2015.

Uber also faces a class action lawsuit *O'Connor v. Uber Technologies Inc.* over its employment classification practices.²⁶ Lyft just settled its pending employment classification class action lawsuit *Cotter v. Lyft Inc.* for \$12.25 million.²⁷

The settlement allows Lyft to continue classifying its drivers as independent contractors – a designation that is crucial to the sharing economy's success. But even though the settlement does not carry any legal precedent, it will lead to additional lawsuits and uncertainty for other sharing-economy companies. This will raise the costs of these services, costs that will be passed on to consumers.

The Labor Department has muddled the once-clear distinction between employees and independent contractors. This move creates uncertainty and costly legal battles for businesses and workers. Moving these workers into an employer-employee relationship from their current – but threatened – independent contractor status would substantially hinder the growth of sharing economy, not to mention the work opportunities and consumer benefits that it provides.

Unlike employees, independent contractors are not entitled to minimum wage, overtime pay, unemployment insurance, or workers' compensation. But extending these employment protections to independent contractors makes no sense.

Since intermediaries do not control workers' hours, and determining how much someone is actually working solely for the intermediary is difficult (if not impossible), minimum wage and overtime pay requirements are inapplicable to the companies' workers. Additionally, one of the benefits of the sharing economy is that supply can easily fluctuate to meet ever-changing demand.

Because of the option of flexibility, independent contractor work for intermediaries is often transient, or done in addition to other work. This is why there is little reason to compel employers to fund unemployment insurance benefits. Intermediaries' workers also usually complete jobs off-site and use their own materials. For these reasons, workers' compensation systems should remain optional – not mandatory – for intermediaries.

When debating the future of worker classification, lawmakers should also resist calls to amend federal antitrust laws to allow independent contractors to collectively bargain.

²⁶ Edward Chen, *O'Connor v. Uber Technologies, Inc. et al.*, C13-3826 EMC, U.S. District Court, Northern District of California, December 22, 2015.

²⁷ *Class Action Settlement Agreement and Release Case No. 3:13-cv-04065-VC*, January 27, 2016.

Collective bargaining is currently reserved for employees, who are able to unionize if a majority of an identified group of employees wants to be represented by a union.

Successful collective bargaining efforts would likely take away many benefits of the flexible, entrepreneurial work arrangements that independent contractors enjoy. Independent contractors are allowed to unionize, but under federal labor law they cannot collectively bargain (though the Seattle City Council recently voted to extend collective bargaining to ridesharing and taxi drivers).²⁸

This makes sense because independent contractors work for themselves. The reason antitrust law would have to be amended is that collective bargaining by independent businesses violates federal prohibitions against price fixing.

Additionally, why should independent contractors who do not want union representation be forced to follow and fund collectively-bargained labor agreements that they do not support? Of course independent contractors should be allowed to join a union, as they are now, but it makes little sense to force them to adhere to collectively-bargained agreements when they often work with more than one company and/or have another full-time job.

These workers have diverse priorities and work arrangements, even when they work with the same intermediary. Those who use Uber for supplemental income and part-time work have vastly different concerns than those who use the service for a full-time job. If collective bargaining is allowed, which group's interests will the union represent? Majority rule could take away one of the cornerstones of the sharing economy – the diverse benefits that flexible work opportunities provide.

Many independent contractors who partner with intermediaries would prefer to have access to some portable benefits. Portable pensions already exist in the form of Individual Retirement Accounts and Simplified Employee Pension Plans. Portable health insurance, although expensive, exists through the Affordable Care Act. Social Security provides disability insurance.

Even with the existing options, the option to offer other portable benefits without being determined to be an employer is something that many sharing economy firms are interested in.²⁹ This ability would help firms attract and keep the best talent. Intermediaries could benefit from pooling their independent contractors to secure better

²⁸ Nick Wingfield and Mike Isaac, *Seattle Will Allow Uber and Lyft Drivers to Form Unions*, New York Times, December 14, 2015.

²⁹ *Common Ground for Independent Workers*, Medium, November 10, 2015.

rates for benefits such as auto, health, and disability insurance and savings and retirement programs. Unfortunately, intermediaries that offer such benefits are in danger of being classified as employers. A legal carve-out should be created to allow intermediaries to offer these benefits and still retain their non-employer status.

Regulatory overreach is not confined to the Department of Labor Wage and Hour Division's recent administrator's interpretation that downplays companies' lack of control over workers' hours and tasks as a factor in deciding employment cases. The National Labor Relations Board has, through a series of decisions, also made it more difficult to work as an independent contractor.³⁰

The Labor Department's Wage and Hour Division and the National Labor Relations Board are trying to change the previously-clear distinction between employees and independent contractors. This, combined with the changing nature of work, leaves judges with the impossible task of dealing with these two agencies' guidelines as lawsuits work their way through the courts. The uncertainty the status quo creates harms many companies and their workers, both inside and outside the sharing economy.

The worker classification question needs to be sorted out by federal legislators, not courts or unaccountable executive agencies. The alternative is the crippling of the sharing economy by executive agencies set on incorrectly classifying the vast majority of new economy workers as employees.

Conclusion

Millennials desire to work for themselves, but government labor regulation hinders the realization of their entrepreneurial dreams. This obstructionism is clear in the Department of Labor's treatment of independent contractors. In order to promote an entrepreneurial workforce, Congress needs to use its powers to rein in the Labor Department.

³⁰ Chairman Pearce, Member Hirozawa, and Member McFerran, *Sisters' Camelot and Christopher Allison and IWW Sisters' Camelot Canvassers Union*, National Labor Relations Board, September 25, 2015; Chairman Pearce, Member Hirozawa, Member Johnson, and Member Schiffer, *FedEx Home Delivery, an Operating Division of FedEx Ground Package Systems, Inc. and International Brotherhood of Teamsters, Local Union No. 671*, National Labor Relations Board, September 30, 2015.