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**Pennsylvania Democratic Caucus Policy Committee**

**Testimony of Brian Chen, Senior Staff Attorney, National Employment Law Project, on Policy Solutions to Independent Contractor Misclassification**

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My name is Brian Chen, and I'm a senior staff attorney at the National Employment Law Project, a national nonprofit that has advocated for good policies and good jobs for workers for over 50 years. NELP is a national legal, research, and policy organization with fifty years of experience advocating for policies that create good jobs, expand access to work, and strengthen protections and support for workers in low-wage industries and for unemployed workers. For decades, we have focused on the ways in which various work structures—subcontracting, temp and staffing, calling workers "franchisees" or "independent contractors"—affect income and wealth inequality, the segregation of workers by race and gender into poor quality jobs, and the ability of workers to come together to negotiate with business over wages and working conditions.

When companies misclassify their workers, they unlawfully evade accountability to workers who rightly should be considered employees. This undermines the rights of workers in nearly every industry in Pennsylvania—construction, janitorial services, home care, and the app-based or "gig economy." These practices also cost the state millions in unpaid payroll and workers' compensation premiums, and promote unfair competition by companies that don't play by the rules.

**The single best way to stand against this willful evasion of labor laws is to adopt an "ABC test" to determine when a company must be accountable to its employees, as Pennsylvania already has used in the construction industry and in its unemployment insurance law.[1]**

For more than a century, labor and employment laws have required employers to comply with baseline labor standards—like the right to collectively bargain, minimum wage and overtime, health and safety, and anti-discrimination protections—for their employees but not for independent contractors.

To evade complying with these laws, bad actor employers illegally label their workers "independent contractors." In doing so, law-breaking employers

[1] Pennsylvania's UI law uses a modified version of the "ABC test." 43 PS § 753(l)(B).

unlawfully lower their operating costs and fail to pay the taxes and other payroll costs required for businesses, pocketing as much as 30 percent of payroll costs.[2] When employees are misclassified as independent contractors, they are robbed of basic labor standards, including wage and hour protections, health and safety standards, workers compensation, and unemployment insurance. Big companies are trying to carve their workers out of these benefits, making it easier for them to rake in massive profits – all at the expense of local communities, small businesses, and publicly funded programs.

Employers claim—wrongly—that giving workers "flexibility" somehow requires those same workers to forego vital labor rights and protections. In reality, employee status and flexibility are fully compatible. Laws do not force workers into choosing between having basic workplace protections and having flexibility. Companies do.

**To pass risk from themselves onto their workers, employers intentionally and regularly label workers as "independent contractors."** This dereliction of employer responsibility is a widespread, pernicious problem across the United States. The U.S. Department of Labor has found that as many as 30 percent of firms incorrectly label their employees as independent contractors,[3] and studies commissioned by state governments often cite estimates that are even higher.[4] These studies suggest that millions of workers nationally may be misclassified.[5]

Misclassification has been especially prevalent in construction, retail, janitorial, home care, trucking, delivery services, transportation, and other low-wage industries where people of color have historically worked. As a group, workers of color—Black, Latino, Asian/Pacific Islander, and Native American—are overrepresented in misclassification-prone construction, trucking, delivery, home care, agricultural, personal care, ride-hail, and janitorial and building service sectors by over 36 percent; they comprise just over a third of workers overall, but between 55 and 86 percent of workers in home care, agricultural, personal care, and janitorial sectors.[6] In digital labor platform work, Black and Latino workers are overrepresented by 45 percent—more than in traditional misclassification-prone sectors.[7] Because independent contractor misclassification often comes with a wage and benefit penalty, as noted above, the practice perpetuates growing racial income and wealth inequality and health disparities in the U.S. Rooting out independent contractor misclassification and guaranteeing proper and broad coverage of employment protections is a critical racial justice matter.

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[2] National Employment Law Project, *Independent Contractor Misclassification Imposes Huge Costs on Workers and Federal and State Treasuries*, October 2020, available at http://www.nelp.org/publication/independent-contractor-misclassification-imposes-huge-costs-on-workers-and-federal-and-state-treasuries-update-2020/.

[3] Lalith de Silva, et al., *Independent Contractors: Prevalence and Implications for Unemployment Insurance Programs,* i-iv, *prepared for* U.S. Planmatics, Inc. (Feb. 2000), available at http://wdr.doleta.gov/owsdrr/00-5/00-5.pdf.

[4] NELP, *supra* note 2.

[5] National Employment Law Project, *Independent Contractor vs. Employee: Why independent contractor misclassification matters and what we can do to stop it*, May 2016, available at http://www.nelp.org/publication/independent-contractor-vs-employee/.

[6] NELP analysis of 2020 Current Population Survey Annual Social and Economic Supplement microdata.

[7] Bureau of Labor Statistics, U.S. Department of Labor, "Electronically mediated work: new questions in the Contingent Worker Supplement," Monthly Labor Review, Sept. 2018, https://www.bls.gov/opub/mlr/2018/article/electronically-mediated-work-new-questions-in-thecontingent-worker-supplement.htm.

Where there is no clear line of employer-employee accountability, work conditions are more likely to deteriorate: pay declines, wage theft increases, and workplace injuries rise. Occupations with high rates of misclassification are among the jobs with the highest numbers of workplace violations.[8] Further, anecdotal studies of working conditions for workers misclassified as independent contractors by their employers show elevated rates of wage theft and workplace injury.[9] Real-life examples of these problem abound, in industries as varied as trucking and delivery, construction, and home care.[10] The app-based transportation and food delivery sectors similarly show endemic poor working conditions, with chronic low and inconsistent pay, long hours, significant risk of severe physical injury, and substantial out-of-pocket expenses.[11]

**When employers skip out on paying their fair share, the public must make up the difference.** Federal, state, and local governments suffer hefty losses of revenue due to independent contractor misclassification, in the form of unpaid and uncollectible income taxes, payroll taxes, and unemployment insurance and workers' compensation premiums.[12] A 2009 report by the Government Accountability Office estimates independent contractor misclassification cost federal revenues $2.72 billion in 2006.[13] According to a 2009 report by the Treasury Inspector General for Tax Administration, misclassification contributed to a $54 billion underreporting of employment tax, and losses of $15 billion in unpaid FICA taxes and UI taxes.[14] A 2017 review of the findings from the twenty state studies of independent contractor misclassification demonstrates the staggering scope of these abuses.[15] Within the so-called "gig economy," app-based companies have abandoned their obligations to state funds. In California, if Uber and Lyft paid UI taxes on account of their drivers as employees, the two companies

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[8] *See* National Employment Law Project, *Holding the Wage Floor,* October 1, 2005, available at http://www.nelp.org/content/uploads/2015/03/Holding-the-Wage-Floor2.pdf.

[9] NELP, *supra* note 2.

[10] *See*, *e.g.*, National Employment Law Project, *The Big Rig: Poverty, Pollution, and the Misclassification of Truck Drivers at America's Ports*, available at http://www.nelp.org/content/uploads/2015/03/PovertyPollutionandMisclassification.pdf; McClatchy DC, "Misclassified: Contract to Cheat," 2014, available at http://media.mcclatchydc.com/static/features/Contract-to-cheat/ (detailing the effects of misclassification within the construction industry); National Employment Law Project, "Independent contractor classification in home care," available at http://www.nelp.org/content/uploads/Home-Care-Misclassification-Fact-Sheet.pdf (detailing the effects of misclassification within the home care industry).

[11] *See generally* Chris Benner, *On-Demand and On-the-Edge: Ride-Hailing and Delivery Workers in San Francisco*, University of California Santa Cruz Institute for Social Transformation (May 2020), https://transform.ucsc.edu/wp-content/uploads/2020/05/OnDemand-n-OntheEdge_MAY2020.pdf; Maria Figueroa, et al., *Essential but Unprotected: App-based Food Couriers in New York City*, Cornell University Industrial and Labor Relations School & Workers' Justice Project (Sept. 14, 2021), https://img1.wsimg.com/blobby/go/6c0bc951-f473-4720-be3e-797bd8c26b8e/09142021CHARTSLos%20Deliveristas%20Unidos-v02.pdf.

[12] U.S. Dep't of Labor, Wage and Hour Division, "Misclassification of Employees as Independent Contractors," available at https://www.dol.gov/whd/workers/Misclassification/.

[13] U.S. Government Accountability Office, *Employee Misclassification: Improved Coordination, Outreach, and Targeting Could Better Ensure Detection and Prevention* (August 2009), available at http://www.gao.gov/new.items/d09717.pdf.

[14] Treasury Inspector General for Tax Administration, *While Actions Have Been Taken to Address Worker Misclassification, Agency-Wide Employment Tax Program and Better Data Are Needed*, February 4, 2009, available at http://www.treas.gov/tigta/auditreports/2009reports/200930035fr.pdf.

[15] *See* NELP, *supra* note 2.

would have owed the state $413 million between 2014 and 2019.[16] In 2019, the New Jersey Department of Labor assessed Uber $523 million in past-due unemployment and disability insurance taxes.[17]

**Companies' willful refusal to be accountable to their employees undercuts the business of law-abiding employers.** Employers that correctly classify workers as W-2 employees often are unable to compete with lower-bidding companies that reap the benefits of artificially low labor costs. Misclassification, as the Treasury Inspector General found, "plac[es] honest employers and businesses at a competitive disadvantage."[18] This is especially a problem in delivery services, construction, janitorial, home care, and other labor-intensive low-wage sectors, where employers can gain competitive advantage by driving down payroll costs.

Misclassification, especially when pervasive in an industry, skews markets and can drive responsible employers out of business. Law-abiding employers also suffer from inflated unemployment insurance and workers' compensation costs, as "free riding" employers that misclassify employees as independent contractors pass off costs to employers that play by the rules. A 2010 study estimated that misclassifying employers shifts $831.4 million in unemployment insurance taxes and $2.54 billion in workers' compensation premiums to law-abiding businesses annually.[19]

**The gold standard policy to address businesses' willful lack of accountability to their employees is to establish an "ABC test" that clearly and simply defines employee status.**

Currently, employers are able to take advantage of the "common law" test for employee status, which is a convoluted and poorly defined standard for who receives employment protections. For workers, the current test means that asserting your rights as an employee means time-consuming, extended litigation. For law-breaking companies, it means that they can classify their workers knowing that most workers won't understand to contest their classification, or have the time and resources necessary to do so. Workers and employers would be better served by having a direct, straightforward approach that lets everyone know their rights and responsibilities upfront.

The ABC test rightfully creates a presumption that a person performing work for a company is an employee. The company can overcome the presumption by showing that their workers (A) are free from control; (B) work outside the usual course of business of the company; and (C) are

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[16] Ken Jacobs & Michael Reich, *What would Uber and Lyft owe to the State Unemployment Insurance Fund?*, Univ. of Calif. Berkeley Labor Center (May 7, 2020), available at https://laborcenter.berkeley.edu/what-would-uber-and-lyft-owe-to-the-state-unemployment-insurance-fund/.

[17] Chris Opfer, *Uber Hit With $650 Million Employment Tax Bill in New Jersey*, Bloomberg Law (Nov. 14, 2019), available at https://news.bloomberglaw.com/daily-labor-report/uber-hit-with-650-million-employment-tax-bill-in-new-jersey.

[18] Treasury Inspector General for Tax Administration, *Additional Actions Are Needed to Make the Worker Misclassification Initiative with the Department of Labor a Success*, February 20, 2018, available at https://www.treasury.gov/tigta/iereports/2018reports/2018IER002fr.pdf.

[19] NELP, *supra* note 2, *citing* Douglas McCarron, "Worker Misclassification in the Construction Industry," BNA Construction Labor Report (April 7, 2011), available at https://web.carpenters.org/Libraries/PDFs_Misc/Construction_Labor_Report_--_McCarron_on_Misclassification_4-7-2011_sm.sflb.ashx.

in business for themselves. Under an ABC test, companies may no longer engage in the too-common practice of forcing an individual to act as an "independent" business even as the company maintains the right to set rates, direct work, and impose discipline.

Because this test is clear and easy to enforce, it will give people who are currently wrongly categorized as contractors the chance to become employees. This will mean fewer workers shut out of basic workplace protections, and more employers paying into Pennsylvania's social insurance programs.

**ABC is a clear, commonly-used test for "employee" status.** Four states currently use an unmodified ABC test to determine employment relationships for wage and hour laws: California, Massachusetts, New Jersey, and Vermont.[20] At least eight states have passed laws that combat misclassification in the construction industry through adoption of versions of the ABC test: Delaware, Illinois, Maine, Maryland, Minnesota, Nebraska, New York, and Pennsylvania.[21] Additionally, more than half of the country's state unemployment insurance laws use the ABC test.[22] Pennsylvania has had a version of the ABC test in its unemployment insurance law for decades.[23]

As advocates for and substantive experts on the labor and employment rights of low-wage workers, NELP believes that an ABC test is the best approach to restore the rights of the many misclassified workers in Pennsylvania.

Sincerely,

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National Employment Law Project

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[20] Cal. Labor Code 2750.3; M.G.L.A 149 § 148B; *Hargrove v. Sleepy's LLC*, 220 N.J. 289 (N.J. Jan. 14, 2015); 21 V.S.A. § 341(1).

[21] Del. Code § 3501 (2009); Ill. Compiled. Stat. § 185:10 (2008); 39-A Me. Stat. § 1043 (2011); Md. Code, Labor and Employment § 3-903 (2009); Minn. Stat. § 181.723 (2009); Neb. Rev. Stat. § 48-2903 (2010); N.Y. Labor Law § 861-c (2010); 43 Pa. Stat. § 933.3 (2011).

[22] There are 26 states that use some form of the ABC test to determine employment status for unemployment insurance eligibility: Alaska, Arkansas, Colorado, Connecticut, Delaware, Georgia, Hawaii, Iowa, Idaho, Illinois, Indiana, Louisiana, Massachusetts, Maryland, Maine, Nebraska, New Hampshire, New Jersey, New Mexico, Nevada, Ohio, Oklahoma, Pennsylvania, Vermont, Washington, and West Virginia. AK Stat. 23.20.525(8); A.C.A § 11-10-210; C.R.S.A. § 8-70-115(b); C.G.S.A § 31-222(a)(1)(B); 19 Del.C. § 3302(10)(K); Ga. Code Ann. § 34-8-35(f); HRS § 383-6; IA Code § 96.19(18(a)(2); I.C. § 72-1316; 820 I.L.C.S. 405/212; IC 22-4-8-1; LSA-RS § 23:1472(12)(E); M.G.L.A. 151A § 2; MD Code, Labor and Employment § 3-903(c)(1)(ii); 26 M.R.S.A. § 1043(11)(E); Neb.Rev.St. § 48.604(5); N.J.S.A § 43:21-19(6); N.M.S.A. § 51-1-42(F)(5); NRS 612.085; RC § 4141.01; 40 Ok.Stat.Ann § 201(14); 43 PS § 753(l)(B); 21 V.S.A. § 1301(6)(B); RCW 50.04.145; W. Va. Code § 21A.1A.16(7).

[23] *See* https://www.uc.pa.gov/employers-uc-services-uc-tax/covered/Pages/Employee-or-Independent-Contractor.aspx.