Welcome to the Gig Economy: The New Normal?

by Elizabeth M. Ebanks

The "gig economy," in which temporary positions are common and organizations contract with independent workers for short-term engagements, has opened up vast opportunities for workers and consumers, but has also led to a surge in employment issues. For example, the US Department of Labor (DOL) recently announced new guidelines meant to crack down on alleged worker misclassification and to ensure that workers who are jointly employed by two entities are properly paid overtime. Many of the highest profile on-demand companies, including Uber, Lyft, Instacart, Postmates, Washio, Caviar, Homejoy, and Handy, are facing class action lawsuits alleging misclassification of their workers as independent contractors rather than employees. Recent rulings in federal court generated headlines as two different federal judges ruled that the misclassification claims by drivers for Uber and Lyft could proceed to trial.

Nonetheless, in this competitive marketplace, employers frequently turn to both independent contractors and staffing companies to supply temporary and other variations of contingent workers — ranging from clerical staff to production workers to highly-skilled professionals — to fill a variety of positions. Such arrangements carry legal risks for employers, but at the forefront are independent contractor misclassification and joint employer liability.

Independent Contractors: Misclassification Matters

Misclassification occurs when a business treats its workers as independent contractors

only to have a government agency, or workers themselves, claim that they were functioning as employees, entitled to all the benefits and protections afforded by an employer-employee relationship. Risks associated with misclassification include liability for unpaid benefits, overtime wages, taxes, unemployment insurance, and exposure to intensive audits by the DOL.

The DOL's Wage and Hour Division (WHD) is pursuing a major initiative to strictly enforce misclassification. In addition to dedicating millions of dollars to enforcement, the DOL has also enhanced coordination with the Internal Revenue Service and state agencies to consolidate efforts to protect workers from misclassification. Consider the following:

- In 2014, the DOL awarded $10.2 million in competitive grant money to nineteen states to target misclassification.[1]
- The DOL's 2015 budget allocated $14 million to independent contractor misclassification enforcement.[2] This was a continuation of a five-year misclassification initiative announced in 2010.
- The DOL's 2017 budget includes $10 million for bolstering state efforts to detect and remedy misclassification[3]
- At least thirty-one states have entered into a Memorandum of Understanding (MOU) with the DOL, including Virginia.[4]
- The DOL has doubled its number of investigators and has hired 2,000 new investigators since 2008.
- The DOL is conducting audits of certain targeted industries in which it believes misclassification is most prevalent.[5]

The DOL's enforcement in this area is succeeding by all accounts. In 2014, it recovered over $240 million from employers on behalf of employees. In 2015, it collected approximately $246.8 million in back wages for 240,340 workers. The success of the DOL's initiative highlights both the importance of classifying workers appropriately and a widespread failure to do so.

Misclassification Standard(s): When to Apply What?

The tests used to determine independent contractor status vary depending on jurisdiction and which statute applies. Nonetheless, most tests used to determine independent contractor status focus, in whole or in part, on the same general factors, including: who controls the manner, method, and means of performance; whether opportunities for profit or loss exist; who provides the equipment and pays expenses; the length of the relationship; whether the services provided are an integral part of the business; and the degree of skill required.[6] Other factors often considered in this analysis include whether benefits are provided, the intent of the parties, and whether the individual is paid on a 1099 or W-2 basis, is free to hire helpers or employees, is able to work elsewhere or have another business, and can or does operate as a separate legal entity.

In the Fourth Circuit, the tests commonly used in determining a worker's status are:

- The common law or "right-to-control" test;[7]
- The economic realities test;[8] and
- The hybrid test (which involves a combination of the above).[9]

The right-to-control test considers a multitude of common-law factors,[10] and still applies in National Labor Relations Act and Employment Retirement Income Security Act cases. Recently, however, courts have departed from or refashioned the right-to-control test in favor of more flexible standards for cases involving remedial social legislation such as the Fair Labor Standards Act (FLSA). In Virginia, courts hearing FLSA cases employ the economic realities test, while cases brought under Title VII of the Civil Rights Act (Title VII) and the Age Discrimination in Employment Act are decided based on hybrid tests.

In the context of the FLSA, misclassification determinations are important because the act does not protect workers who are independent contractors. The overtime and minimum wage requirements of the FLSA apply only to "employees."[11] Problematically, the statutory

Tips for Employers Engaging Independent Contractors

Employers who use independent contractors should consider taking the following steps:

- Conduct a thorough, enterprise-wide risk analysis of your independent contractor population.
- Design and implement a comprehensive compliance program.
- Establish an internal team to implement and monitor the compliance program.
- Carefully draft independent contractor agreements.
- Ensure proper education and training on the front lines.
- Utilize separate policies and procedures for independent contractors.
- Review and refine your benefit plans.
- Perform periodic internal audits.
- Create an internal avenue for independent contractors to raise classification concerns.

definitions of employer, employee, and "to employ" are circular and offer little guidance. An "employee" is statutorily defined as "any individual employed by an employer."[12] An "employer" includes "any person acting directly or indirectly in the interest of an employer in relation to an employee." A "person" includes corporate entities.[13] And, "to employ" means "to suffer or permit to work."[14]

Based on the statute's expansive definition of the term "employ," courts have rejected the application of the common law agency test in FLSA cases.[15] To determine whether an individual is an employee under the FLSA, courts examine whether the individual is "economically dependent on the business to which he renders service . . . or is, as a matter of economic fact, in business for himself."[16]

While no single factor is determinative and the entirety of the relationship must be examined, the Fourth Circuit considers the following six factors when applying the economic realities test:

- The degree of control exercised by the alleged employer over the manner in which the work is to be performed;
- The alleged employee's opportunity for profit or loss and investment in the business;
- The degree of skill and independent initiative required to perform the work;
- The permanence or duration of the working relationship;
- The extent to which the work is an integral part of the alleged employer's business; and
- The extent of the relative investments of the employer and worker.[17]

As with all FLSA issues, the labels given to the relationship by the parties are given little weight by the courts.

On July 15, 2015, DOL Administrator David Weil issued Administrator's Interpretation No. 2015-1 (AI 2015-1), which provides guidance about the factors that should be considered in determining whether an independent contractor or employment relationship exists.[18] Notably, the memorandum states DOL's position that *most workers* qualify as employees under the expansive definition of employment under the FLSA.

The DOL emphasized that the focus of the test is whether the worker is really in business for him or herself, or whether he or she is economically dependent on the employer. If the individual is economically dependent on the purported employer, then an employment relationship exists. If the person is not economically dependent, but instead is in business for him or herself, then he or she is an independent contractor.

Functionally, AI 2015-1 offers little new material to the economic realities test itself, but the administrator's commentary tips his hand by describing misclassification as resulting in an "uneven playing field for employers" and as a "means to cut costs and avoid compliance with labor laws."[19]

Joint Employment: Who's the Boss?

Making matters more complicated, an individual may simultaneously have more than one employer. This can have grave consequences, as multiple employers may be individually and jointly liable for the same claims. Joint employment issues commonly arise when businesses use staffing companies to fill temporary or contingent positions. Although language in the parties' staffing agreement may be helpful in determining which entity is the worker's employer, it is not dispositive.

A primary legal issue associated with the use of temporary employees is determining which entity — the staffing company, the worksite client, or both — is the temporary worker's "employer." There is a high risk in many arrangements that the temporary worker will be deemed to be "jointly employed" by both the staffing company and the worksite client. A finding of joint employment raises two primary risks for the worksite client: they may be liable if the temporary employee asserts an employment-related claim, and the client may be liable to others for the acts of the temporary employee, for example, accusations of sexual harassment by another employee.

Recent decisions in the Fourth Circuit affirmed the applicability of the joint employer doctrine in FLSA claims[20] and expressly adopted it in the Title VII context.[21] In July 2015, the Fourth Circuit articulated a nine-factor hybrid test for determining Title VII joint employer status. No one factor is dispositive, but the court noted that "control remains the principal guidepost," identifying the first three factors as most important:

- Authority to hire and fire the individual;
- Day-to-day supervision of the individual, including employee discipline;
- Whether the putative employer furnishes the equipment used and the place of work;

- Possession of and responsibility over the individual's employment records, including payroll, insurance, and taxes;
- The length of time during which the individual has worked for the putative employer;
- Whether the putative employer provides the individual with formal or informal training;
- Whether the individual's duties are akin to a regular employee's duties;
- Whether the individual is assigned solely to the putative employer; and
- Whether the individual and putative employer intended to enter into an employment relationship.[22]

The FLSA joint employment test is distinct from Title VII because the FLSA defines "employ" in broader terms, namely "to suffer or permit to work."[23] Thus, courts in the Fourth Circuit determine FLSA joint-employer status by examining the economic realities of the employment relationship.[24] Generally, under the FLSA a joint-employment relationship exists in the following situations:

- Where there is an arrangement between the employers to share the employee's services, as, for example, to interchange employees; or
- Where one employer is acting directly or indirectly in the interest of the other employer (or employers) in relation to the employee; or
- Where the employers are not completely disassociated with respect to the employment of a particular employee and may be deemed to share control of the employee, directly or indirectly, by reason of the fact that one employer controls, is controlled by, or is under common control with the other employer.[25]

The issue of which individual or entity may be held accountable for FLSA violations as a joint employer has also received increased attention by the DOL. Continuing its quest to regulate changes in the traditional employee-employer relationship, on January 20, 2016, the WHD released Administrator's Interpretation No. 2016-1 (AI 2016-1) on joint employment.[26] Just as with AI 2015-1 on the misclassification of independent contractors, AI 2016-1 demonstrates the aggressive enforcement of joint employment status in DOL investigations.

AI 2016-1 states that the concept of joint employment should be broadly defined, so that it is more expansive than the common law concepts of employment and joint employment. As with misclassification, the primary focus of joint employment under the FLSA is the broader economic realities of the working relationship rather than the amount of control that an employer exercises over an employee under the common law concept.

AI 2016-1 also recognizes two types of joint employment: horizontal and vertical.

Horizontal joint employment exists in situations in which "the employee has employment relationships with two or more employers and the employers are sufficiently associated or related with respect to the employee such that they jointly employ the employee."[27] AI 2016-1 cites restaurants and home health care providers that share economic ties or have common management as examples of horizontal joint employers. In determining whether a horizontal joint employment relationship exists, the analysis focuses on the relationship between two (or more) employers to each other.

Vertical joint employment exists in situations in which the employee has an employment relationship with one employer, referred to as an "intermediary employer," and the economic realities show that he or she is economically dependent on, and thus employed by, another entity involved in the work. The employer that contracts with the intermediary employer to receive the benefit of the employee's labor would be considered the joint employer. Examples of intermediary employers are staffing agencies, subcontractors, and labor providers.

Tips for Employers Engaging Temporary Employees

- Engage only reputable, fully-licensed staffing firms.
- Require a comprehensive agreement stating that the firm, not the client, is the employer of the temporary employee.
- Vet staffing agency's financial documents.
- Obtain referrals from other clients.
- Pay special attention to indemnification provisions.
- Consider whether the staffing firm requires each temporary employee to sign an agreement acknowledging that he/she is employed by the staffing firm and not the client.
- To the extent possible, cede control of the manner and performance of the employee's work to the staffing firm. For example, one term that may be feasible is that the temporary employee will contact the staffing firm, not the client, if he or she will be absent, late, or needs time off.
- Ensure the staffing company supplies each temporary employee with the name of a staffing company supervisor and contact information to be called in the event the temporary employee has any work-related concerns, including issues of discrimination or harassment.
- Contact the staffing firm, not the temporary employee directly, if the client has concerns about the temporary employee's performance.

Conclusion

Despite the shifting nature of the independent contractor and joint employment landscape, there is little doubt that such relationships are under fire. The current enforcement system punishes passivity and missteps with severity. As such, now is the time to closely scrutinize the employment law minefield of the gig economy. Only with a proactive approach can liability be averted.

This paper has been written by the author to inform practicing attorneys and in-house counsel of important information in these areas of law. The information contained in this paper is not intended as specific legal advice.

Endnotes:

1 News Release, *$10.M Awarded to Fund Worker Misclassification Detection, Enforcement Activities in 19 State Unemployment Insurance Programs,* United States Department of Labor (Sept. 15, 2014), http://www.dol.gov/newsroom/releases/eta/eta20141708.

2 FY 2015 Department of Labor Budget in Brief, http://www.dol.gov/dol/budget/2015/pdf/fy2015bib.pdf.

3 FY 2017 Department of Labor Budget in Brief, http://www.dol.gov/sites/default/files/documents/general/budget/FY2017BIB_0.pdf.

4 *See* Wage and Hour Division, Misclassification of Employees as Independent Contractors, United States Department of Labor, http://www.dol.gov/whd/workers/misclassification (last visited July 8, 2016).

5 These industries include the construction industry, home health care, janitorial services, nursing, staffing companies, trucking companies, restaurants, motels, cable installation companies, oil and gas, landscaping, car services, supermarkets, internet services, and security.

6 *See, e.g., McFeeley v. Jackson St. Entm't, LLC,* __ F.3d __, 2016 WL 3191896 (4th Cir. 2016), Schultz v. Capital Intern. Sec., Inc., 466 F.3d 298 (4th Cir. 2006).

7 *See N.L.R.B. v. Gary Enterprises, Inc.,* 958 F.2d 368 (4th Cir. 1992).

8 *See Schultz*, 466 F.3d at 307.

9 *See Butler v. Drive Auto. Indus. of Am., Inc.,* 793 F.3d 404, 414 (4th Cir. 2015).

10 *See Nationwide Insurance Co. v. Darden*, 503 U.S. 318, 323-24 (1992) (summarizing common law factors).

11 29 U.S.C. §§ 206, 207(a)(1).

12 29 U.S.C. § 203(e)(1).

13 29 U.S.C. § 203(d).

14 29 U.S.C. § 203(g).

15 *See Schultz,* 466 F.3d at 304 (citing *Nationwide Mut. Ins. Co.,* 503 U.S. at 326) ("These definitions broaden 'the meaning of 'employee' to cover some [workers] who might not qualify as such under a strict application of traditional agency [or contract] law principles.'").

16 *Dole v. Snell,* 875 F.2d 802, 804 (10th Cir. 1989); *see also McFeeley,* 2016 WL 3191896, at *5 ("[T]he more [the worker] is personally invested in the capital and labor of the enterprise, the less the worker is 'economically dependent on the business' and the more he is 'in business for himself' and hence an independent contractor.").

17 *See, e.g., Schultz* 466 F.3d at 304-05.

18 Wage and Hour Division, *Administrator's Interpretation No. 2015-1,* United States Department of Labor (July 15, 2015), https://www.dol.gov/whd/workers/misclassification/ai-2015_1.htm.

19 *Id.*

20 *See Schultz, 466 F.3d at 305-06.*

21 *Butler, 793 F.3d at 409.*

22 *Id. at 414.*

23 29 U.S.C. § 203(g). *See also West v. J.O. Stevenson, Inc.,* 2016 WL 740431, at *8 (E.D.N.C. Feb. 24, 2016) (comparing application of the joint employment doctrine in civil rights and labor relations claims).

24 *See Schultz,* 466 F.3d at 306 (applying the economic realities test for FLSA joint employer analysis).

25 29 C.F.R. § 791.2(b).

26 Wage and Hour Division, *Administrator's Interpretation No. 2016-1,* United States Department of Labor (January 20, 2016), http://www.dol.gov/whd/flsa/Joint_Employment_AI.pdf.

27 *Id.*

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