

# Independent Contractors and the Gig Economy

## Objective Standards Can Preserve Benefits, Protect Individuals

### Summary

The hiring of independent contractors is a popular and lawful tool companies utilize as a part of their overall business model. For businesses, it is a cost-effective way in which to address specialized needs. For entrepreneurs, it is a way in which to maximize profits and grow their own business. Businesses have utilized independent contractors for years and have always struggled with the subjective and conflicting standards at the federal and state levels with regard to who qualifies as an employee versus an independent contractor. With the creation of the gig economy, which relies significantly upon the use of independent contractors, the proper classification of individuals as independent contractors has intensified, as well as the availability of benefits that are traditionally provided to employees.

### The Gig Economy

The “gig economy” refers to a business model that utilizes independent contractors to fulfill temporary positions, jobs, or short-term projects. Through the use of technology and software applications on smartphones, businesses can quickly connect a consumer with an independent contractor who is available to perform the task or assignment. For example, companies such as Uber and Lyft provide the platform through which a consumer can connect with an available driver for a ride.

Although the size of the gig economy is hard to define given the lack of any comprehensive data collection, several publications have provided estimates of the size and growth of this sector.

- An article published on January 5, 2017 by *Fast Company* titled “How the Gig Economy Will Change in 2017” estimated that there are up to 55 million people working in the gig economy.
- In October 2016, McKinsey Global Institute (MGI) published a study titled “Independent Work: Choice, Necessity, and the Gig Economy” that estimated there are 54 million to 68 million workers who are independent earners or workers, which the study defines as individuals who have a high degree of autonomy in determining their workload; are paid by task, assignment, or sale of an asset/lease of property; and have a short-term relationship between the worker and the customer. MGI determined that 20%–30% of the working population in the United States is independent workers. MGI estimates that approximately 70% are engaged in the gig economy by choice, while 30% participated out of necessity. The MGI study also found that approximately 44% of the independent workers relied upon the earnings in the gig economy as their primary income, while 56% of the independent workers used the gig economy for supplemental income.
- A separate study by JPMorgan Chase & Co., “Paychecks, Paydays, and the Online Platform Economy,” published in February 2016, distinguished between “labor platform” workers, meaning those who utilize an online intermediary to connect customers with freelance or contingent workers who perform an assignment, and “capital platforms,” which utilize an online intermediary to connect customers with individuals who rent assets or sell goods. The study found that only 25% of workers on the labor platform relied upon income earned in the gig economy as a primary source of income (75% of the worker’s total income); and “the vast majority—82 percent of labor platform participants and 96 percent of capital platform participants—relied on platform earnings for less than 25 percent of their income.”

### Benefits/Disadvantages of the Gig Economy

One of the primary attractions to the gig economy is the flexibility for individuals to set their own schedule. In the MGI study, the independent workers who chose to work as freelance agents rated their level of satisfaction as higher than employees who worked in traditional jobs. The study stated that the independent workers are “more engaged in their work, and they relish the chance to be their own boss and have more control over their hours.” With regard to independent workers who work in the gig economy out of necessity, MGI also cited flexibility as the main benefit to the work they received.

The January 2017 article in *Fast Company* also indicated that a majority of workers with regular jobs are choosing to work in the gig economy as a way to make additional money.

Conversely, the primary disadvantage for individuals working in the gig economy is the lack of income security. Independent contractors are not employees and therefore are not covered by labor standards such as minimum wage, overtime, or unemployment insurance. They also are not entitled to employer benefits such as health insurance, paid time off, or 401(k)s.

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In a July 12, 2015 *New York Times* article, “Growth in the ‘Gig Economy’ Fuels Work Force Anxieties,” Noam Scheiber states that “many live with the uncertainty of not knowing how long they will go between assignments, during which time they earn no income from the company.” The MGI study also stated that individuals who work in the gig economy out of necessity are less satisfied with their income level and security than those in traditional jobs.

### Classifying Individuals as Employees vs. Independent Contractors

Ensuring the proper classification of an individual as an employee versus an independent contractor has always been a daunting task for any business/employer, especially in California, given the subjective and inconsistent analysis that is used to determine whether an individual qualifies as an employee versus an independent contractor. This analysis is no different with individuals working in the gig economy.

In November 2014, the gig economy became a focus of the independent contractor debate when drivers for Uber Technologies, Inc. (Uber) filed a class action in the Northern District Court of California, claiming that they were misclassified as independent contractors. While the parties reached a tentative settlement of the case in 2017, the court rejected the settlement. The case is now stayed pending an appeal on the enforcement of the arbitration provisions in Uber’s driver agreements. A similar lawsuit was filed against Lyft. Parties to that lawsuit settled in March 2017.

Other companies in the gig economy have faced similar independent contractor/employee challenges. One of the most recent and closely watched is a lawsuit filed in California against GrubHub. Instead of settling, the parties went to a bench trial starting in September 2017 and finished closing arguments at the end of October 2017. At publication time, the judge had not issued his decision on whether a former GrubHub delivery driver should have been classified as an independent contractor or an employee.

Requiring hosting platforms in the gig economy to reclassify all workers as employees instead of independent contractors could have a significant financial impact on the companies and their viability. On September 10, 2017, *techcrunch.com* posted a blog titled “What you missed at the GrubHub trial about 1099 independent contractors.” In it, Megan Rose Dickey stated “[i]n 2015, a Recode analysis estimated it would cost Uber \$209 million to reclassify 45,000 drivers in California. As companies like Uber, Lyft and Postmates are still trying to reach profitability, the costs of reclassifying their workers could have a negative impact on their respective bottom lines.” On September 2, 2017, *techcrunch.com* also posted another blog titled “GrubHub trial could have major implications for the gig economy,” which stated “[i]t’s worth noting that companies like Shyp, Luxe and Sprig, which all made a big deal about switching its workers from 1099 contractors to W2 employees, have either ceased operations in major markets or shut down entirely.”

### Recent California Activity

In 2016, Assemblymember Lorena Gonzalez Fletcher (D-San Diego) introduced AB 1727, which sought to allow all independent contractors to collectively bargain with a “hosting platform,” defined as “a facility for connecting people or entities seeking to hire people for work with people seeking to perform that work, using any medium of facilitation, including, but not limited to, a dispatch service, an Internet Web site, or other Internet-based site,” on issues related to work assignments, compensation, and terms of service. The bill ultimately failed in the Assembly Judiciary Committee.

In 2017, Gonzalez Fletcher introduced AB 1099, which sought to require a ride-sharing platform that allowed the payment of a transaction with a debit or credit card to also allow a consumer to provide a driver with a gratuity on a debit or credit card as well. In spring 2017, Uber announced a new policy allowing drivers to receive gratuities through debit or credit cards, thereby eliminating the need for AB 1099.

### CalChamber Position

The challenge employers face with regard to properly classifying individuals as employees versus independent contractors has been an issue in California for years. The growth of the gig economy has simply mainstreamed the challenge.

Given the significant benefits and financial opportunities the gig economy has provided and continues to provide to numerous individuals, simply shutting down the business models that operate in this economy by deeming all individuals to be employees or allowing such individuals to collectively bargain should not be the answer. Rather, California should look at a balanced approach to addressing the concerns of individuals working in the gig economy, as well as preserving the benefits that the gig economy provides. All employers in California, including those in the gig economy, would benefit from objective standards that provide better guidance of who qualifies as an employee versus an independent contractor.

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January 2018

## UPDATE

### **Court Rules in Favor of Grubhub**

On February 8, 2018 in the case of *Raef Lawson v. Grubhub, Inc.*, the U.S. Court for the Northern District of California held that the former Grubhub delivery driver was properly classified as an independent contractor.

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