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Misclassification Claims Threaten Gig Economy Business

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The gig economy — companies that hire workers for specific projects or "gigs" — is on the rise. Gig companies use technology to provide goods and services to consumers on demand. The companies hire workers who access and accept jobs through an internet-based platform.

A recent *Time* magazine survey estimated that more than 14 million people provide services in the gig economy. Companies, such as Uber and Lyft, base their success, at least in part, on the fact that they save significant expenses by classifying workers as independent contractors. This allows gig companies to avoid offering benefits, such as health insurance, retirement plans and paid time off. It also allows companies to avoid paying payroll taxes, unemployment insurance, workers' compensation insurance and other expenses usually required to be paid by employers. Increasingly, however, gig economy workers are fighting back by bringing lawsuits claiming that gig companies are misclassifying them as independent contractors and that they should be considered employees, with all the indicia of an employment relationship.

Independent Contractor Versus Employee

Independent contractor misclassification claims can arise in two ways: (1) a complaint by a private individual brought before a federal or state government agency or court, alleging that the individual should receive the rights and benefits of an employee; or (2) directly from a federal or state government agency that investigates a company's classification practices. Complaints brought by private individuals before a court are often filed as class or collective actions and brought on behalf of a group of individuals who are similarly situated.

Misclassification claims by private individuals have asserted various legal theories, based on the position that, if the individuals had been classified properly as employees, they would have received certain rights and benefits that employees receive, such as payment for overtime hours worked, fringe benefits, unemployment compensation and workers' compensation.

To determine whether independent contractors are classified properly, an agency or court uses a fact-intensive test. The particular test used depends on both the jurisdiction and the authority. However, all the tests have a general focus on the level of control the company has over the worker — the more control there is, the more likely that the relationship will be considered to be an employee/employer relationship. The various tests generally contain a number of factors that explore different aspects of control.

For example, the IRS test looks at three categories of control: (1) behavioral control (whether the company has a right to direct and control how work is done through avenues such as instructions and training); (2) financial control (whether the company has a right to direct or control the financial and business aspects of the work, such as who provides the tools to perform the work and how the worker is paid); and (3) the relationship of the parties (i.e., the length and permanency of the relationship and the terms and conditions of the relationship, such as whether the company provides the worker with any employee-type benefits).

By contrast, the U.S. Department of Labor uses an "economic realities" test that focuses on whether the worker is economically dependent on the employer. The DOL looks at the totality of the relationship between the parties by assessing numerous factors. One of the factors is whether the worker truly is in business for himself or herself. This is determined by assessing whether the worker supervises any of his or her own employees, has invested in tools or equipment to provide the services, and has an opportunity for profit and loss. Another factor is the permanency of the worker's relationship with the employer. Though not always the case, generally a more permanent relationship, especially when the amount of work provided is relatively high (i.e., the worker does not provide services to other clients), weighs in favor of employee status.

States generally have their own independent contractor tests, and the tests and their application vary widely between states. State tests are found in the state's wage payment laws, workers' compensation laws, unemployment compensation laws, and common law. Massachusetts is widely considered to have the most stringent test, and it is nearly impossible to establish an independent contractor relationship under Massachusetts state law. Workers are presumed to be employees, and an employer can treat an individual as an independent contractor only if it can show that work (1) is done without the direction and control of the employer; (2) is performed outside the usual course of the employer's business; and (3) is done by someone who has his or her own independent business or trade doing that kind of work.

Worker Classification and the Gig Economy

In recent years, many cases specific to the gig economy have been filed in New York and California. Both states have employee-friendly laws, making them appealing jurisdictions for claiming employee status. To determine whether an independent contractor is classified properly, both states focus on the level of control the company asserts over the worker. California uses the economic realities test (also referred to as a multifactor control test), which focuses on the company's right to control the worker both as to the work done and the manner in which it is performed, and also takes into account a number of additional factors. New York uses a similar test, determining whether the worker is free of supervision, direction and control in the performance of his or her duties by assessing a number of factors, such as whether the worker has his or her own established business, sets his or her own schedule, and offers his or her services to other businesses.

The gig economy cases in New York and California are either pending or were settled before the court could issue a determinative judgment as to the proper classification of the workers at issue. But the facts of the cases and the settlement details provide valuable insight into the potential risks and exposure for gig economy companies.

In September 2013, for example, a group of Lyft drivers brought a class action alleging they were improperly classified as independent contractors and seeking unpaid minimum wage and expense reimbursements. *See Cotter v. Lyft Inc.*, No. 13-cv-04065-VC (N.D. Cal.). Lyft argued that its business does not employ drivers, but rather maintains an online platform that makes it possible for riders and drivers to communicate with each other to arrange transportation. Lyft argued that the plaintiff-drivers control the services they provide because they determine when to access the Lyft platform, the length of time they spend on the platform and the geographic areas from which to accept ride requests. The plaintiffs also provided their own equipment — a smart phone and car — needed to perform the services, and are paid on a per-ride basis.

By contrast, the plaintiffs argued that Lyft controlled whether and when they were permitted to work, because Lyft could terminate the relationship at any time, and Lyft's practices penalized drivers for declining and cancelling rides. The plaintiffs also alleged that Lyft provided them with a number of materials that dictated how to perform the work, including a driver guide, rules of the road and FAQs.

The parties agreed early in the case to ask the court to decide the threshold issue of whether the drivers were classified properly as independent contractors, and they cross-moved for summary judgment. Noting that there were factors favoring each party's position, the court denied both motions, concluding that the issue should be decided by a jury. On one hand, the drivers acted like employees because Lyft had the right to control how they performed their jobs, including the power to terminate them if they did not meet Lyft's specifications about how to give rides, and Lyft drivers use no special skills to provide services. On the other hand, the drivers acted like independent contractors because they could control their own schedules. The court also observed that individuals who worked full-time and drove regularly were more likely to be employees.

The parties initially reached a settlement of $12.25 million for a class of approximately 100,000 members. The court denied preliminary approval, however, holding that plaintiffs counsel had "grossly underestimated" the value of the drivers' expense reimbursement claims. The parties submitted a new agreement to the court for $27 million, which the court approved in July 2016. The settlement also included nonmonetary terms such as: (1) a requirement that Lyft would no longer be able to deactivate (terminate) drivers for any reason, and instead would be able to deactivate drivers only for specific reasons, some of which would require notice and an opportunity to cure; (2) the implementation of a prearbitration negotiation process that provides drivers with the opportunity to resolve minor disputes with Lyft without having to invoke the arbitration process; and (3) a requirement that Lyft provide additional information about potential passengers to drivers before drivers accept or decline a ride. Importantly, however, Lyft was not required to reclassify the drivers as employees.

In March 2015, a group of Postmates contractors, who provide on-demand delivery services, filed a class and collective action alleging they were improperly classified as independent contractors and asserting various wage-related claims. *See Singer v. Postmates Inc.*, No. 4:15-cv-01284-JSW (N.D. Cal.). The parties reached a settlement of $8.75 million, which was approved in August 2017. The class included more than 200,000 Postmates couriers nationwide. The settlement also had nonmonetary elements, including a revision of the independent contractor agreement, implementation of a courier feedback system, and occupational accident insurance for bicycle couriers. Like the Lyft settlement, however, the Postmates settlement agreement did not require the company to reclassify the couriers as employees.

In November 2016, a class and collective action was brought against Uber in the Southern District of New York. *See Burgos v. Uber Technologies Inc.*, No. 1:16-cv-08512 (S.D.N.Y.). The plaintiffs, bicycle messengers who contracted with on-demand food delivery service UberEATS and on-demand goods delivery service UberRUSH, alleged that they were improperly classified as independent contractors and sought numerous types of damages, including minimum and overtime wages, spread-of-hours pay, gratuities and expense reimbursements.

The case was settled in July 2017 between Uber and the three named plaintiffs for $40,000. *Burgos* is a rare example of a case that was not settled classwide, and was settled for relatively little money. That said, there are a multitude of additional misclassification cases currently pending against Uber, including *Haider v. Uber Technologies Inc.*, No. 1:16-cv-04098, in the Southern District of New York. In *Haider*, a class and collective action, a group of Uber drivers seek unpaid minimum wage, overtime and expense reimbursements, among other claims. The plaintiffs allege that, despite being classified as independent contractors, they must follow strict company-imposed regulations that govern "how, when, where and who gets to work." For example, the plaintiffs allege that Uber directs and sets the terms of conditions of the drivers' work, including the setting of fares and fees, drivers' apparel, and what routes to take.

Very recently, a misclassification case against GrubHub, which provides on-demand food delivery services, went to trial in what is believed to be the first trial in an independent contractor classification case against a gig economy employer. *See Lawson v. GrubHub Inc.*, No. 3:15-cv-05128 (N.D. Cal.). Before trial, the court denied GrubHub's motion for summary judgment on the classification issue, stating that a defendant may obtain summary judgment only if all the facts and evidentiary inferences material to the employee/independent contractor determination are undisputed and a reasonable trier of fact could reach but one conclusion — that the drivers are independent contractors.

Drawing all inferences from the evidence in the plaintiff-driver's favor, the court found that GrubHub failed to satisfy its burden of proving that it did not have the right to exercise all necessary control over the details of the plaintiff's work. While the court noted that some factors weighed in favor of finding that the driver was an independent contractor — such as the fact that the driver supplied his own equipment, was not required to wear GrubHub clothing, and could perform delivery services for other companies — these factors were not dispositive of the lack of an employment relationship as a matter of law. Likewise, the court found that language in the agreement between the parties stating that the plaintiff was an independent contractor also was not dispositive. In denying the motion, the court acknowledged that a determination of whether the plaintiff was correctly classified as an independent contractor would be difficult to reach at the summary judgment stage.

The parties finished closing arguments in the bench trial on Oct. 30. A decision is expected in the coming months.

Conclusion

Many recent cases against gig economy companies alleging that workers are misclassified as independent contractors have settled without a ruling on the classification issue. A court or jury finding that Uber or Lyft drivers, for example, are not independent contractors would pose a significant threat to the business model of those companies. Although the settlements in *Cotter v. Lyft* and *Singer v. Postmates* have been large, they were presumably less than the potential damages the plaintiffs could have recovered in those cases and, perhaps more important to the companies, less than the cost of treating the drivers as employees.

Notably, the courts that have ruled on this issue have concluded to date that the decision whether workers are classified properly as independent contractors is a jury issue. The inability of companies to obtain summary judgment in these cases means defending misclassification claims is costly, and that companies may be subject to the vagaries of a jury.

As the gig economy grows and more companies seek to use independent contractors instead of employees, it is likely that the number of class action misclassification claims will rise. Gig economy companies should review their relationships with workers to assess whether they meet the relevant tests for independent contractor status under federal and state law, and modify those relationships as necessary. In particular, gig economy companies can reduce the risk of a misclassification claim by structuring the relationship so that it meets the relevant factors for establishing independent contractor status to the maximum extent possible. Examples of those factors include whether gig economy independent contractors (1) can control how they perform their jobs; (2) can determine their hours; (3) can perform work for other entities (even competitors); (4) can refuse assignments; (5) can decide their routes; and (6) may not be terminated at will. Gig economy companies that operate in multiple jurisdictions should check the laws in each jurisdiction to ensure that their independent contractor arrangements pass muster in each location where they do business.