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# The Square Peg Between two Round Holes: Why California's Traditional Right to Control Test is not Relevant for On-Demand Workers

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## I. Introduction

“What’s in a name? that which we call a rose// By any other name would smell as sweet.” The idea that a name is artificial and meaningless seems enchanting with respect to Romeo and Juliet’s star-crossed romance. However, a name actually has particular force in today’s complicated and evolving workforce, where courts face the difficult challenge of differentiating employees from independent contractors. While an employer may label a worker as one thing, it is the job of the courts to look past the label and ensure a worker is properly classified. The classification of a worker as an employee or independent contractor has significance for both the worker and the employer. An employee receives, among other things, statutorily required income and benefits. That means an employer can avoid substantial costs by labeling a worker as an independent contractor. Currently, there is no standardized test that provides guidance to courts for distinguishing employees from independent contractors. Rather different agencies and jurisdictions use different tests. Courts are faced with the challenge of applying the different factors of varying tests to aspects of a business’s policies and procedures that will definitively classify a worker as an independent contractor or an employer.

Today, we have emerging new business models in which classification of workers is critical to the success of the company’s business model, yet poses a challenge because of its non-traditional nature. California, an employee-friendly state, is considering the classification issue of two rising on-demand companies, Uber and Lyft. In March, two district court judges in the Northern District of California denied summary judgment to both companies, leaving the question of whether drivers were employees or independent contractors to a jury.<sup>1</sup> Both courts applied the California right to

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<sup>1</sup> Cotter v. Lyft, 60 F. Supp. 3d at 1069; O’Connor v. Uber Techs., 82 F. Supp. 3d at 1135.

control test for determining if a worker is an employee or independent contractor, which was developed in *S.G. Borello & Sons, Inc. v. Dep't of Industrial Relations*.<sup>2</sup>

The Ninth Circuit is no stranger to shaking up the independent contractor business model. In 2014, it ruled in *Alexander v. FedEx*<sup>3</sup> that FedEx drivers were employees, despite the fact that FedEx labeled them as independent contractors. *Alexander* applied California's right to control test, and found that the underlying employment relationship between FedEx and its drivers was clear and unambiguous.<sup>4</sup> However, the recent Uber and Lyft cases do not provide such an obvious answer to the classification question. Up to this point, the *Borello* factors have been applied to an economic model vastly different from the quickly evolving on-demand economy.<sup>5</sup> That means that, using the same test that determined FedEx drivers were employees, Uber and Lyft drivers may also be considered employees. As an alternative, this Article considers the possibility that Uber and Lyft drivers fall into a new category of employment, one that has not been considered among the traditional work relationships. First, the Article lays out the different tests various branches of government use to classify workers as employees or independent contractors. Next, the Article will narrow the scope towards the Ninth Circuit, and outline the history of the employment misclassification test formed in *Borello* and applied in *Alexander*. Then, the Article will turn towards the employee misclassification cases in California involving Uber and Lyft. It will contrast the on-demand business models analyzed in these cases with FedEx's business model. Finally, the Article will propose a new classification of workers that will make room for emerging on-demand business models –the square peg between two round holes.

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<sup>2</sup> 769 P.2d 399, 404 (Cal. 1989).

<sup>3</sup> 765 F.3d 981 (9th Cir. 2014).

<sup>4</sup> *Id.* at 990.

<sup>5</sup> *Cotter*, 60 F. Supp. 3d at 1081.

## II. The History and Development of Employee Misclassification

### A. CLASSIFYING WORKER STATUS

#### a. Why Do Employers Misclassify?

Under a traditional understanding of employment, employees were “individuals hired on a permanent or full-time basis or part-time basis with an understanding of continuous employment”<sup>6</sup> and independent contractors were “individuals who lack a contract for long term employment and whose minimum hours may vary at random.”<sup>7</sup> However, this traditional understanding has been complicated because different government agencies and states use different factors and balancing tests to determine if a worker is an independent contractor or an employee.<sup>8</sup> The complications of the tests cause some employers to misclassify their workers out of genuine error. However, many employers intentionally misclassify because of the financial benefits they gain from labeling workers as independent contractors.<sup>9</sup> If an employer classifies a worker as an employee, federal and state laws require employers to pay that employee at least minimum wage and overtime; refrain from discrimination on the basis of race, sex, and other personal characteristics; maintain safe and healthy workplaces; contribute toward payroll taxes that go towards the employee’s unemployment insurance; provide Social Security, Disability Insurance and Medicare; provide workers’ compensation insurance; and, in many employers cases, provide healthcare.<sup>10</sup> The laws that afford protections to a worker classified as an employee places an expensive burden on the

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<sup>6</sup> Karen R. Harned, Georgina M. Kryda & Elizabeth A. Milito, *Creating A Workable Legal Standard For Defining An Independent Contractor*, 4, 10 J. BUS. ENTREPRENEURSHIP & L. 93, 95 (2010).

<sup>7</sup> *Id.*

<sup>8</sup> *Id.* at 99.

<sup>9</sup> Ruth Burdick, *Principles of Agency Permit the NLRB to Consider Additional Factors of Entrepreneurial Independence and the Relative Dependence of Employees When Determining Independent Contractor Status Under Section 2(3)*, 15 HOFSTRA LAB. & EMP. L.J. 75, 76 (1997).

<sup>10</sup> Seth D. Harris and Alan B. Krueger, *A Proposal for Modernizing Labor Laws for Twenty-First-Century Work: “The Independent Worker”*, in THE HAMILTON PROJECT (2015).

employer. By changing this business model and classifying workers as independent contractors, employers can avoid the expenses associated with employee status.

Another benefit employers receive from misclassifying workers as independent contractors is escaping vicarious liability. Under that theory, an employer is liable, as well as the employee, for the negligent acts of its employee, as long as the acts were committed in the course and scope of the employment.<sup>11</sup> If an employer retains a worker as an independent contractor, however, the employer cannot be held responsible.

#### b. Common Law Test

The common law agency test is used to determine whether an individual is classified as an employee or an independent contractor for purpose of defining when an employer was vicariously liable for the tortious acts of its agents.<sup>12</sup> Under the Restatement (Second) of Agency, these factors include:

- (1) the extent of control which, by the agreement, the master may exercise over the details of the work;
- (2) whether or not the one employed is engaged in a distinct occupation or business;
- (3) the kind of occupation, with reference to whether in the locality, the work is usually done under the direction of the employer or by a specialist without supervision;
- (4) the skill required in the particular occupation;
- (5) whether the employer or the workman supplies the instrumentalities, tools, and the place of work for the person doing the work;
- (6) the length of time for which the person is employed;
- (7) the method of payment, whether by the time or by the job;
- (8) whether or not the work is a part of the regular business of the employer;
- (9) whether or not the parties believe they are creating the relation of master and servant; and
- (10) whether the principal is or is not in business.<sup>13</sup>

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<sup>11</sup> Burlington Indus. v. Ellerth, 524 U.S. 742,756 (1998).

<sup>12</sup> Griffin Toronjo Pivateau, *Rethinking the Worker Classification Test: Employees, Entrepreneurship, and Empowerment*, 34 N. ILL. U. L. REV. 67, 76 (2013).

<sup>13</sup> RESTATEMENT (SECOND) OF AGENCY § 220 (2)(a)-(j) (1958). See also *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318, 323-24.

These factors are weighed and balanced against each other. It is not necessary that each factor is met, and the main focus of the test is whether an employer retains the right to control the manner and means by which the product is accomplished.<sup>14</sup>

c. The ABC Test

The “ABC” test is used by many states to determine employer’s obligation for payment of unemployment taxes.<sup>15</sup> To be considered an independent contractor, a worker must meet three requirements: (a) the worker is free from control or direction in the performance of the work; (b) the work is done outside the usual course of the company’s business and is done off the premises of the business; and (c) the worker is customarily engaged in an independent trade, occupation, profession, or business.<sup>16</sup> This test is broad and results in classification for most workers as employees.<sup>17</sup> It creates a presumption of employment, which makes it harder for employers to escape financial and legal obligations by intentionally misclassifying.<sup>18</sup>

However, any given individual may be classified as an employee and an independent contractor at the same time under different common law and statutory regimes. Therefore, workers who are classified as employees under a state ABC test may be considered independent contractors for purposes of vicarious liability or under federal statutes. The test’s expansiveness may cause confusion for both employers and workers who would traditionally be classified as independent contractors.<sup>19</sup>

d. The IRS Test

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<sup>14</sup> *Cnty. for Creative Non- Violence v. Reid*, 490 U.S. 730, 751-52 (1989).

<sup>15</sup> Karen R. Harned, *Creating A Workable Legal Standard For Defining An Independent Contractor*, 4. J. BUS. ENTREPRENEURSHIP & L. 93, 102 (2010).

<sup>16</sup> *Id.*

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

The Internal Revenue Service created a twenty-factor test to determine whether a worker is an employee or independent contractor for purposes of withholding taxes.<sup>20</sup> An employer is responsible for withholding income taxes, withholding and paying Social Security and Medicare taxes, and paying unemployment taxes on wages to employees. Employers do not pay taxes for independent contractors, which is another incentive to classify workers as such.<sup>21</sup> The IRS grouped the twenty-factors that determine the degree of control and independence an employer holds over a worker into three categories: (1) Behavioral:<sup>22</sup> Does the company control or have the right to control what the worker does and how the worker does his or her job?; (2) Financial:<sup>23</sup> Are

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<sup>20</sup> *Independent Contractor (Self-Employed) or Employee?*, Internal Revenue Service, <http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Independent-Contractor-Self-Employed-or-Employee> (last updated Aug. 5, 2015).

<sup>21</sup> *Id.*

<sup>22</sup> (1) Instructions: If the employer directs where, when, or how work is done, the worker is likely an employee. This is similar to the right-of-control common law test; (2) Training: If the employer provides training so that the worker performs in a particular manner and with a particular result, the worker is likely an employee. This is especially true if the training is provided at regular intervals; (3) Order or sequence: If the employer requires the worker to perform his tasks in a particular order or sequence, or retains the right to establish a particular order or sequence, the worker is likely an employee; (4) Assistance: If the employer hires, supervises, and pays assistants to aid the worker, the worker is likely an employee; (5) Furnishing of tools and materials: If the employer provides the supplies, materials, equipment, and other tools necessary to perform the work, the worker is an employee dependent on his employer; (6) Oral or written reports: If the employer requires the worker to submit reports at regular intervals, the worker is likely an employee; (7) Payment: If the employer pays the worker by salary or by hour, week, or month, the worker is likely an employee. If the worker is paid when he or she bills for services performed, or is paid on commission, the worker is likely an independent contractor; (8) Doing work on employer's premises: If the employer requires the worker to perform his/her services on the premises, where the employer can have control over the worker, the worker is likely an employee; (9) Set hours of work: If the employer requires the worker to perform a set number of work hours, sets the worker's schedule, or retains approval rights over the worker's schedule, the worker is likely an employee. If the employer does not approve the worker's schedule, the worker is likely an independent contractor.; (10) Full time required: If the employer requires the worker to work on a full-time basis, the worker is likely an employee.; (11) Working for more than one firm at a time: If the employer does not allow the worker to perform work for another firm so long as it is performing work for the employer's firm, the worker is likely an employee. However, a worker can be an employee of multiple firms at the same time. (12) Making services available to the public: If the employer does not allow the worker to perform his work for the public as a free service, the worker is likely an employee.

<sup>23</sup> (13) Significant monetary investment: If the worker must make a significant monetary investment in order to perform his services, he is independent of the employer and is not an employee. There is no set dollar limit that qualifies as a "significant investment"; it is determined on a case-by-case basis.; (14) Payment of business and/or traveling expenses: If the worker must expend money for business or business-related travel, and the employer pays these expenses, the worker is likely an employee. In this case, the employer generally has the ability to control the extent of the employee's business or travel expenses.; (15) Realization of profit or loss: If the worker does not have the opportunity to profit (or loss) from his work, he is an employee. The employer is in the capacity of receiving the money directly from the client and has the opportunity for profit or loss.

the business aspects of the worker's job controlled by the payer?; and (3) Type of Relationship:<sup>24</sup> Are there written contracts or employee type benefits? Will the relationship continue and is the work performed a key aspect of the business?<sup>25</sup> The IRS asserts that no single factor is dispositive of classification, and that businesses must weigh all the factors in relation to the relationship.

e. Economic Realities Test

Courts use the economic reality test to determine coverage and compliance with the minimum wage and overtime requirements of the Fair Labor Standards Act.<sup>26</sup> The economic reality test, like the common law right to control test, takes into account the degree of control an employer has over his or her employee, but it also considers the degree to which the workers are economically dependent on the business.<sup>27</sup> Under the economic reality test, courts look at six factors: "(1) the degree of control exerted by the alleged employer over the worker; (2) the worker's opportunity for profit or loss; (3) the worker's investment in the business; (4) the permanence of the working relationship; (5) the degree of skill required to perform the work; and (6) the extent to which the work is an integral part of the alleged employer's business."<sup>28</sup> The court must look at the totality of the circumstances rather than one single factor.<sup>29</sup>

B. A NEW ERA OF OF EMPLOYEE MISCLASSIFICATION CASES

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<sup>24</sup> (16) Services rendered personally: If the worker must perform the work personally, and cannot delegate the tasks, he/she is an employee; (17) Integration: If the employer uses the worker as part of the course of normal business operations, the worker is likely an employee. In this case, the success of the business may be directly related to the success of the individual employee; (18) Continuing relationship: If the employer and the worker have a longstanding, continuing relationship, the worker is likely an employee. This includes work that is done at recurring intervals or services performed by a worker who is "on call."; (19) Right to discharge: If the employer may fire or dismiss the worker, the worker is likely an employee.; (20) Right to terminate: If the worker can terminate the work relationship and not be liable for completion of a particular job or service, the worker is likely an employee. If the worker remains liable for a job or service, he or she is an independent contractor.<sup>24</sup>

<sup>25</sup> Pivateau, at 85-88.

<sup>26</sup> See *Tony & Susan Alamo Found. v. Sec'y of Labor*, 471 U.S. 290 (1985).

<sup>27</sup> See *Baker v. Flint Eng'g & Constr. Co.*, 137 F.3d 1436, 1440 (10<sup>th</sup> Cir. 1998).

<sup>28</sup> *Id.*

<sup>29</sup> See *Id.*

a. Shift to an “On Demand Economy”

A few years ago no one knew about Uber<sup>30</sup> or Lyft<sup>31</sup> and few could imagine technology that would allow individuals to ride in a stranger’s personal vehicle. Now, these platforms have become well-recognized businesses connecting people with fast and cheap transportation. Uber and Lyft’s business models revolve around smart-phone apps that connect drivers offering rides to passengers who seek them.<sup>32</sup> The passengers pay a mileage-based fee through credit cards that the companies keep on file.<sup>33</sup> Uber and Lyft take a percentage of the fee and give the rest to the drivers.<sup>34</sup> These type of business models have given rise to the “on demand economy,” which is “the economic activity created by technology companies that fulfill consumer demand via the immediate provisioning of goods and services.”<sup>35</sup> The theory behind this business model is that access to goods and skills is more important than ownership of them.<sup>36</sup> An entire economy is being formed around the exchange of goods and services between individuals instead of directly from business to consumer.<sup>37</sup> “This new class of on-demand companies relies on a large freelance

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<sup>30</sup> “Uber Technologies, Inc. provides a smartphone application that connects drivers with people who need a ride. The company’s application enables users to arrange and schedule transportation and/or logistics services with third party providers. Uber Technologies services customer in North, Central, and South Americas, as well as Europe, the Middle East, Africa and the Asia Pacific. . . . [T]he company was founded in 2009 and based in San Francisco, California.” *Company Overview of Uber Technologies, Inc.*, BLOOMBERG BUSINESS (October 24, 2015, 12:12 PM), <http://www.bloomberg.com/research/stocks/private/snapshot.asp?privcapId=144524848>.

<sup>31</sup> “Lyft Inc. helps commuters to share rides with friends, classmates, and coworkers going the same way. It helps organizations to establish private and social networks for ridesharing. The company focuses on college, university, and corporate communities. . . . [T]he company was founded in 2007 and is based in San Francisco, California. Lyft Inc. operates as a subsidiary of Enterprise Holdings, Inc.” *Company Overview of Lyft Inc.*, BLOOMBERG BUSINESS (October 24, 2015 12:43 PM) <http://www.bloomberg.com/research/stocks/private/snapshot.asp?privcapId=58995029>.

<sup>32</sup> Brishen Rogers, *The Social Costs of Uber*, 82 U CHI L REV DIALOGUE 86 (2015).

<sup>33</sup> *Id.*

<sup>34</sup> *Id.*

<sup>35</sup> Mike Jaconi, *The ‘On-Demand Economy’ Is Revolutionizing Consumer Behavior-Here’s How*, Jul. 13, 2014 Business Insider.

<sup>36</sup> Danielle Sacks, *The Sharing Economy*, Fast Company (Apr. 18 2011), <http://www.fastcompany.com/1747551/sharing-economy>.

<sup>37</sup> Irving Wladawsky-Berger, *The Continuing Evolution of the On-Demand Economy*, THE CIO REPORT (July 24, 2015 12:25 PM), <http://blogs.wsj.com/cio/2015/07/24/the-continuing-evolution-of-the-on-demand-economy/>.

workforce instead of on a classic company workforce.”<sup>38</sup> Companies in the on-demand economy hire workers to perform the services the companies offer and the individuals receive. The on-demand economy is breaking down the traditional employment structure in favor of jobs that more are flexible and temporary.

Uber and Lyft are ride-share companies that have broken ground in the on-demand economy through their widely used smartphone apps that connect passengers to drivers for hire.<sup>39</sup> All hiring and payment goes through the app, rather than the driver.<sup>40</sup> The passengers input their location and destination, and the app informs the customer when the driver has arrived.<sup>41</sup> The app shows customers the route the driver takes, the estimated time of arrival, and the identity of the driver.<sup>42</sup> After the transaction is completed, the passenger rates the driver.<sup>43</sup> Central to Uber and Lyft’s business model is the classification of drivers as independent contractors, and itself as a technological platform to connect those drivers with passengers.

b. A New Dilemma

Recently, two separate decisions in California district courts on wage and hour suits brought by drivers for Uber and Lyft have shaken the independent contractor business model the ride-sharing companies rely on. Two judges denied summary judgment to Uber<sup>44</sup> and Lyft<sup>45</sup> to declare the drivers independent contractors, and instead established a rebuttable presumption that

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<sup>38</sup> *Id.*

<sup>39</sup> Thomas Robinson, *Could Employee Classification Issues Uberwhelm the Uber Business Model?*, THE WORKCOMP WRITER (Feb. 3, 2015), <http://www.workcompwriter.com/could-employee-classification-issues-uberwhelm-the-uber-business-model/>.

<sup>40</sup> *Id.*

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

<sup>43</sup> *Id.*

<sup>44</sup> *See O’Connor* 82 F. Supp. 3d 1133.

<sup>45</sup> *See Cotter* 60 F. Supp. 3d 1067.

the drivers were employees because they performed services for the company's benefit.<sup>46</sup> Both judges found that material facts remain disputed, and in light of this, the on-demand car services will need to make their case to juries as to why their drivers should not be classified as employees instead of independent contractors under the California Labor Code.<sup>47</sup>

In both cases, the courts relied on the right to control test adopted in the California Supreme Court case *S.G. Borello & Sons, Inc. v. Department of Industrial Relations*.<sup>48</sup> In addition, both courts relied on a Ninth Circuit wage and hour case, *Alexander v. FedEx Ground Package Sys.*, in which FedEx drivers alleged that FedEx had misclassified its drivers as independent contractors, thus entitling the drivers to unpaid wages and expenses.<sup>49</sup> The court found that the California FedEx drivers were misclassified as independent contractors under the California right to control test.<sup>50</sup> The *Alexander* decision seems to be a catalyst for lawsuits against emerging on-demand companies, such as Uber and Lyft, which similarly rely on independent contractors for the success of their business. However, Uber and Lyft's relationship with its drivers is far more complicated and inconclusive than FedEx's.

### c. California's Employee Friendly Laws

California law provides employees with many benefits and protections, while independent contractors are afforded almost none:<sup>51</sup>

Employees are generally entitled to, among other things, minimum wage and overtime pay, meal and rest breaks, reimbursement for work-related expenses, workers' compensation, and employer contributions to unemployment insurance. Employers are also required

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<sup>46</sup> See *O'Connor* 82 F. Supp. 3d 1133; see also *Cotter*, 60 F. Supp. 3d 1067.

<sup>47</sup> *Id.*

<sup>48</sup> 769 P.2d 399, 404 (Cal. 1989).

<sup>49</sup> 765 F.3d 981 (9th Cir. 2014).

<sup>50</sup> *Id.*

<sup>51</sup> *Cotter* 60 F. Supp. 3d at 1074.

under California Unemployment Insurance Code to withhold and remit to the state their employees' state income tax payments.<sup>52</sup>

California provides employees with these protections to ensure that employers do not take advantage of employees due to the inequality in bargaining power.<sup>53</sup> In essence, these laws balance the scales and provide employees with more contractual leverage. The California legislature does not provide the same protections to independent contractors because their independent status presumably affords them more bargaining power against companies.<sup>54</sup> Independent contractors can “take their services and equipment elsewhere when faced with unfair or arbitrary treatment, or unfavorable working conditions.”<sup>55</sup> Further, they often are working for more than one company at a time, and therefore are not “dependent on a single employer in the same all-or-nothing fashion as traditional employees who tend to work on a full-time basis for an indefinite term.”<sup>56</sup> Past decisions in California have demonstrated that the statutory provisions aimed at employees should be liberally construed in favor of protecting the employees and implementing the legislature's intent.<sup>57</sup>

d. *Borello* Decision

In *Borello*, the California Supreme Court examined whether agricultural laborers engaged to harvest cucumbers under a written “sharefarmer” agreement were independent contractors exempt from workers' compensation coverage under the California Labor Code.<sup>58</sup> The deputy labor commissioner issued a stop order against a grower, S.G. Borello & Sons, for failure to secure

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<sup>52</sup> *Id.*

<sup>53</sup> *Id.*

<sup>54</sup> *Id.*

<sup>55</sup> *Id.* (internal quotations omitted).

<sup>56</sup> *Id.*

<sup>57</sup> *Id.* at 1075.

<sup>58</sup> *Borello*, 769 P.2d at 400.

worker's compensation coverage for laborers.<sup>59</sup> The grower argued that the workers were seasonal agricultural laborers that harvested cucumbers worked under a sharefarmer agreement, meaning they were tenant farmers who received a share of the profits.<sup>60</sup> Therefore, the grower argued, the farmers were only seasonal, temporary workers, and should be considered independent contractors.<sup>61</sup>

Following the common law vicarious liability tradition, the court held that, “[t]he principal test of an employment relationship is whether the person to whom service is rendered has the right to control the manner and means of accomplishing the result desired.”<sup>62</sup> The court noted that the factor of control is often inapplicable to a variety of employment relationships when applied in isolation.<sup>63</sup> Therefore, the court concluded that, although the right to control work details is the most important consideration, there are other “secondary” factors to consider.<sup>64</sup> The court identified the right to discharge at will, without cause, as strong evidence in support of an employment relationship.<sup>65</sup> Further, the court identified additional factors: (1) whether the one performing the services is engaged in a distinct occupation or business; (2) the kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of the principal or by a specialist without supervision; (3) The skill required in the particular occupation; (4) Whether the principal or the worker supplies the instrumentalities, tools, and the place of work for the person doing the work; (5) The length of time for which the services are to be performed; (6) The method of payment, whether by the time or by the job; (7) Whether or not the work is a

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<sup>59</sup> *Id.* at 401.

<sup>60</sup> *Id.* at 402.

<sup>61</sup> *Id.*

<sup>62</sup> *Id.* at 404.

<sup>63</sup> *Id.*

<sup>64</sup> *Id.*

<sup>65</sup> It should be noted that this factor is unique to California's right to control test.

part of the regular business of the principal; and (8) Whether or not the parties believe they are creating the relationship of the employer-employee.<sup>66</sup> The court viewed these factors not as separate tests, but as interrelated.<sup>67</sup>

Ultimately, the court held that the share-farmers were employees and were entitled to compensation coverage.<sup>68</sup> The grower argued that the share-farmers managed their own labor, shared in the profit or loss, performed a job that requires specific skill and judgment, and signed an agreement in which they expressly agreed that the parties' relationship was principal-independent contractor.<sup>69</sup> However, the court found that the grower exercised "pervasive control over the operation as a whole."<sup>70</sup> The grower owned and cultivated the land for his own account, made the decision to grow cucumbers, supplied the materials and transportation, and controlled worker's documentation for production and payment.<sup>71</sup> The court held that, "[a] business entity may not avoid its statutory obligations by carving up its production process into minute steps, then asserting that it lacks control over the exact means by which one such step is performed by the responsible workers."<sup>72</sup> Under the test the court had adopted, the grower maintained all necessary control over the process.<sup>73</sup>

e. *Alexander* Decision

The Ninth Circuit reversed a ruling by Multidistrict Litigation Court, which granted summary judgment in favor of FedEx in a class action alleging that FedEx drivers in California

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<sup>66</sup> *Id.*

<sup>67</sup> *Id.*

<sup>68</sup> *Id.* at 410.

<sup>69</sup> *Id.* at 407-10.

<sup>70</sup> *Id.* at 408.

<sup>71</sup> *Id.*

<sup>72</sup> *Id.* (internal quotations omitted).

<sup>73</sup> *Id.* at 401.

were employees rather than independent contractors.<sup>74</sup> Instead, the Ninth Circuit held that the amount of control FedEx exhibited over its drivers weighed in favor of finding an employment relationship.<sup>75</sup> The court applied the right to control test adopted in *Borello*.<sup>76</sup> The Ninth Circuit found that “FedEx’s policies and procedures unambiguously allow FedEx to exercise a great deal of control over the manner in which its drivers do their jobs.”<sup>77</sup> FedEx maintained control through its detailed appearance requirements for the drivers and their vehicles.<sup>78</sup> FedEx also controlled the time its drivers can work by adjusting workloads so that they forced to work nine and a half to eleven hours a day.<sup>79</sup> The court found that FedEx also controlled how and when drivers delivered packages.<sup>80</sup> It rejected FedEx’s argument that there were details of the driver’s work it did not control, and that it controls results of the work alone.<sup>81</sup> The court noted that absolute control is not necessary for workers to be considered employees under the right to control test.<sup>82</sup>

The court found that the secondary factors of the right to control test did not sufficiently favor FedEx to permit it to classify its drivers as independent contractors.<sup>83</sup> The right to terminate at will is strong evidence of employee status.<sup>84</sup> FedEx’s operating agreement contained an arbitration clause, which slightly weighed in Fed-Ex’s favor.<sup>85</sup> The provision of tools and equipment also slightly favored FedEx.<sup>86</sup> However, the court found that, even though plaintiffs

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<sup>74</sup> *Alexander* 765 F.3d at 983.

<sup>75</sup> *Id.* at 997.

<sup>76</sup> 769 P.2d 399, 404 (Cal. 1989).

<sup>77</sup> *Alexander* 765 F.3d at 990.

<sup>78</sup> *Id.*

<sup>79</sup> *Id.*

<sup>80</sup> *Id.*

<sup>81</sup> *Id.*

<sup>82</sup> *Id.*

<sup>83</sup> *Id.* at 994.

<sup>84</sup> *Id.*

<sup>85</sup> *Id.*

<sup>86</sup> *Id.* at 995.

provided their own trucks and were not required to get equipment from FedEx, the majority of them did so.<sup>87</sup> The final factor that favored FedEx was the parties' agreement that they were creating an independent contractor relationship.<sup>88</sup> The operating agreement identifies the relationship as an independent contractor; however the court found that this was not dispositive or controlling if, as a matter of law, a different type of employment relationship exists.<sup>89</sup> "What matters is what the contract, in actual effect, allows or requires."<sup>90</sup> After examining FedEx's policies and procedures, the court concluded that the drivers were employees, rather than independent contractors.<sup>91</sup>

In this holding, the Ninth Circuit expressly rejected the "entrepreneurial test" that had been adapted by the District of Columbia Circuit for classifying employment status.<sup>92</sup> Under the entrepreneurial test, the emphasis is shifted away from control, and the primary factor is whether the worker has significant opportunity for gain or loss.<sup>93</sup> FedEx relied on the D.C. Circuit decision to argue that the drivers had the opportunity under the Operating Agreement to delegate to other drivers, take on additional routes, or sell routes to third parties.<sup>94</sup> However, the court held that these entrepreneurial opportunities FedEx provides drivers are limited because, for example, FedEx may refuse to let a driver take on additional routes or sell his route.<sup>95</sup> The court held that, regardless, the entrepreneurial test had no application to the case: "There is no indication that

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<sup>87</sup> *Id.*

<sup>88</sup> *Id.* at 996.

<sup>89</sup> *Id.*

<sup>90</sup> *Id.* at 989.

<sup>91</sup> *Id.* at 997.

<sup>92</sup> *Id.* at 993-94.

<sup>93</sup> *FedEx Home Delivery v. Nat'l Labor Relations Bd.*, 563 F.3d 492, 497 (D.C. Cir. 2009).

<sup>94</sup> *Alexander* 765 F.3d at 994.

<sup>95</sup> *Id.*

California has replaced its longstanding right-to-control test with the new entrepreneurial-opportunities test developed by the D.C. Circuit.”<sup>96</sup>

### III. New Business Model, Same Old Test

The California right to control test, when applied to the facts in *Alexander*, led the court to the conclusion that the workers were employees. Though FedEx contracted with the drivers as independent contractors, most aspects of FedEx’s relationship with its drivers looked like a traditional employer/ employee relationship. However, worker relationships in emerging business models, such as Uber and Lyft, do not so neatly fit into the traditional independent contractor-employee dichotomy. The *Borello* test has consistently been applied to result in either independent contractor or employee status. In *Cotter* and *O’Connor*, both judges recognize a new, unclassified relationship between worker and company.

#### A. WHAT IS CONTROL: DISPARITIES BETWEEN *ALEXANDER* AND EMERGING ON-DEMAND CASES

The court in *Cotter* examined whether Lyft drivers should be considered employees or independent contractors under California law.<sup>97</sup> The court denied cross-motions for summary judgment, and found that the issue presented a mixed question of law and fact that should be resolved by a jury.<sup>98</sup> The court in *O’Connor* reviewed a similar matter involving the classification of Uber drivers.<sup>99</sup> The court denied defendant’s motion for summary judgment, leaving a jury to resolve the matter.<sup>100</sup> In *Alexander*, even though FedEx cloaked its drivers as independent contractors, the Ninth Circuit found that FedEx drivers were employees as a matter of law because

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<sup>96</sup> *Id.* at 993.

<sup>97</sup> *Cotter*, 60 F. Supp. 3d at 1069.

<sup>98</sup> *Id.*

<sup>99</sup> *O’Connor*, 82 F. Supp. 3d at 1135.

<sup>100</sup> *Id.*

“the arrow pointed so strongly in the direction of one status or another that no reasonable juror could have pointed the arrow in an opposite direction after applying California’s multi-factor test.”<sup>101</sup> The courts in both ride-share cases acknowledged that the *Borello* right to control test does not produce such a conclusive result when applied to Uber and Lyft drivers. The court in *O’Connor* noted that “numerous factors point in opposing directions.”<sup>102</sup> The court in *Cotter* recognized that “[a]t first glance, Lyft drivers don’t seem much like employees. . . . But Lyft drivers don’t seem much like independent contractors either.”<sup>103</sup>

In *Cotter*, the parties disagreed about the amount of control Lyft exercises over its drivers. The court acknowledged that Lyft maintains a good deal of control over how drivers proceed after they accept ride requests.<sup>104</sup> Lyft provides a driver with instructions on what not to do on the job.<sup>105</sup> Also, Lyft reserves the right to penalize or terminate drivers who violate company policy.<sup>106</sup> Lyft maintains quality control over its drivers through a rating system, and any driver who falls below a certain threshold is subject to termination.<sup>107</sup> However, the court also recognized that the Lyft driver “enjoys great flexibility in when and how often to work—far more flexibility than the typical employee.”<sup>108</sup> The court noted that there were no undisputed facts that provided overwhelming evidence of an employment relationship, as in *Alexander*.<sup>109</sup> The court further pointed out, “the experience of the Lyft driver is much different from the experience of the FedEx

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<sup>101</sup> *Cotter*, 60 F. Supp. 3d. at 1075.

<sup>102</sup> *O’Connor*, 82. F. Supp. 3d at 1153.

<sup>103</sup> *Cotter*, 60 F. Supp. 3d. at 1069 (alteration in original).

<sup>104</sup> *Id.* at 1078.

<sup>105</sup> *Id.*

<sup>106</sup> *Id.* at 1079.

<sup>107</sup> *Id.* at 1071.

<sup>108</sup> *Id.* at 1081.

<sup>109</sup> *Id.*

driver, underscoring why the plaintiffs have not established here that summary judgment should be granted in their favor.”<sup>110</sup>

In *O’Connor*, the court recognized that many factors of control were disputed and ambiguous in Uber’s relationship with its drivers.<sup>111</sup> First, the court pointed out that whether a driver can be terminated at will was in dispute.<sup>112</sup> Plaintiffs claimed that Uber might fire drivers at any time for any reason, which would be strong evidence of an employment relationship.<sup>113</sup> However, Uber pointed out that before it terminates drivers it must give notice or there must be a material breach.<sup>114</sup> Uber uses a customer rating system as a form of quality control, similar to Lyft.<sup>115</sup> The court pointed to evidence that, if a driver’s star rating falls below the minimum star rating, Uber terminates the driver.<sup>116</sup> The court noted that the customer rating system is a form of control used by Uber to “constantly monitor certain aspects of a driver’s behavior,” and that a jury could find it weighs in favor of finding an employment relationship.<sup>117</sup> The court noted that the fact that Uber has no control over its drivers’ hours and when they report for work significantly weighs in favor of independent contractor status.<sup>118</sup> However, the court pointed out that the more relevant inquiry is how much control Uber exerts when drivers actually do report for work.<sup>119</sup> The court in *O’Connor* noted that there were many factors of the *Borello* test that pointed in different

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<sup>110</sup> *Id.*

<sup>111</sup> *O’Connor*, 82. F. Supp. 3d at 1153.

<sup>112</sup> *Id.* at 1149.

<sup>113</sup> *Id.*

<sup>114</sup> *Id.*

<sup>115</sup> *Id.* at 1151.

<sup>116</sup> *Id.*

<sup>117</sup> *Id.*

<sup>118</sup> *Id.* at 1152.

<sup>119</sup> *Id.*

directions, including those involving Uber’s level of control over the manner and means of performance.<sup>120</sup>

## B. WHY TRADITIONAL CLASSIFICATIONS UNDER *BORELLO* DO NOT WORK FOR UBER AND LYFT

The courts in *O’Connor* and *Cotter* were faced with the task of applying traditional common law principles encompassed in the *Borello* right to control test, to technological platforms that operate from a smartphone. The independent contractor model of the emerging on-demand companies becomes the “Wild West” of classification: “The test the California courts have developed over the 20<sup>th</sup> Century for classifying workers isn’t very helpful in addressing this 21<sup>st</sup> Century problem. Some factors point in one direction, some point in the other, and some are ambiguous.”<sup>121</sup> It is true that the factors of the *Borello* test can sometimes produce different outcomes when applied to many old economy jobs, depending on how a court interprets the facts of the case or weighs a specific factor. However, the business models of Uber and Lyft do not look anything like old economy jobs. From an economic and societal perspective, the technology Uber and Lyft provide creates exciting and new opportunities for workers. It seems critical to tread through the legal uncertainty and define the employment relationship between Uber/Lyft and driver.

The core test of an employment relationship under the *Borello* test is “whether the person to whom service is rendered has the right to control the manner and means of accomplishing the result desired.”<sup>122</sup> The court in *O’Connor* recognized, the *Borello* test “evolved under an economic

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<sup>120</sup> *Id.* at 1153.

<sup>121</sup> *Cotter*, 60 F. Supp. 3d. at 1081.

<sup>122</sup> *Borello*, 48 Cal. 3d at 350.

model very different from the new sharing economy.”<sup>123</sup> Companies employed workers to provide services for the companies’ own benefit. There was a traditional and more direct connection between worker and business. Whether an individual was an independent contractor or employee depended on how much control that business had over that worker. However, the Uber and Lyft business models diverge from the traditional forms of employment and present challenges to the application of the *Borello* test.

The relationships Uber and Lyft maintain with its drivers do not neatly result in classification under the *Borello* test. Like an independent contractor, drivers are given freedom to work for different employers; they are not economically dependent on the ride-share services for their main source of income. The drivers have flexibility in their work hours and where they work. The drivers use their own cars for each ride. Drivers also control acceptance of rides, and therefore are in control of their own opportunity for profit or loss. Contrastingly, like traditional employees, the drivers are integral to the companies’ businesses. Uber and Lyft maintain control over pricing of rides and payment. They maintain control through rating systems. However, the form of control the courts in both cases focused heavily on, the rating system, differs from that of the traditional business model of a company like FedEx because it does not seek to control every aspect of the worker’s performance. Rather, it is a form of quality control based on customer feedback. Uber and Lyft seek to continue or discontinue the engagement based on whether customers are satisfied. The on-demand companies rely on customer feedback to ensure quality performance. Under this system, the individuals receiving the service-those being transported- have the ability to rate and provide feedback. Once Uber or Lyft receive this feedback, the company responds accordingly to maintain quality control over its business.

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<sup>123</sup> *O’Connor*, 82. F. Supp. 3d at 1153.

Uber and Lyft provide workers flexibility and freedom in some important aspects of the work relationship yet maintain control in others. This relationship falls into a gray area of employment classification.

### C. CREATING A NEW CLASSIFICATION: A HYBRID EMPLOYEE AND INDEPENDENT CONTRACTOR

The court in *Cotter* correctly stated that “the jury in this case will be handed a square peg and asked to choose between two round holes.”<sup>124</sup> Nearly all workers in the United States fall into one of two categories: employee or independent contractor. However, these categories seem outdated and ill fit with the technological age of on-demand businesses run through apps. In these businesses, where workers seem to cross the border of independent contractor and employee, a third category seems necessary. For example, courts and labor and employment statutes in Canada and Germany recognize an intermediate class, the “dependent contractor.”<sup>125</sup> This relationship forms when a contractor has formed an exclusive relationship (80% is the equivalent of exclusive for Canada) over a period of time with one client, and the client therefore becomes economically dependent on the relationship.<sup>126</sup> While this new worker status that has developed demonstrates the workability of new categories of work relationships, it does not precisely illustrate the flexible relationships of the on-demand economy, where employees make a living working for different companies and sometimes even at the same time.<sup>127</sup>

Seth Harris, a professor at Cornell University, and Alan Krueger a professor at Princeton University, have proposed legal reform that could provide a possible solution to the ambiguous

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<sup>124</sup> *Cotter*, 60 F. Supp 3d at 1081.

<sup>125</sup> Benjamin Sachs, *A New Category of Worker for the On-Demand Economy?*, ON LABOR (June 22, 2015) <http://onlabor.org/2015/06/22/a-new-category-of-worker-for-the-on-demand-economy/>.

<sup>126</sup> *E.g.*, Harris and Krueger, *supra* note 7, at 7.

<sup>127</sup> *Id.*

classification of Uber and Lyft drivers.<sup>128</sup> Harris and Krueger propose a new classification of workers, the independent worker, who “occupy a middle ground between traditional employees and independent contractors.”<sup>129</sup> In an effort to define this new class, Harris and Krueger suggest ideas of what protections and benefits these new workers would be provided. First, Harris and Krueger argue that independent workers should be given the freedom to organize and collectively bargain.<sup>130</sup> They contend that these workers should have the ability to bargain over the equivalent of wages, hours, and the terms and conditions of their contractual relationships.<sup>131</sup> Harris and Krueger point out that the main challenge to independent workers organizing is the federal anti-trust law.<sup>132</sup> They suggest an independent workers exemption to anti-trust laws, which would allow the workers to have a voice and some ability to influence their relationship.<sup>133</sup>

Harris and Krueger also advance that independent workers should be included within the protections of federal anti-discrimination statutes.<sup>134</sup> Providing independent workers with protections against discrimination could encourage better policy enforcement by Uber and Lyft against racial and sexual discrimination.<sup>135</sup> Uber would have to administer a new policy that not only takes into account the rating system of customers, who may discriminate against drivers cause driver terminations, but possibly also co-worker perception.

Harris and Krueger also suggest allowing intermediary companies, such as Uber and Lyft, to opt-in to workers’ compensation without transforming the relationship to employment.<sup>136</sup>

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<sup>128</sup> *Id.* at 5.

<sup>129</sup> *Id.*

<sup>130</sup> *Id.* at 15.

<sup>131</sup> *Id.*

<sup>132</sup> *Id.* at 16.

<sup>133</sup> *Id.*

<sup>134</sup> *Id.* at 17.

<sup>135</sup> *Id.*

<sup>136</sup> *Id.* at 19.

However, Uber and Lyft might be better off including workers' compensation into their business model. Drivers would have a reasonably predictable compensation for work related injuries, and Uber and Lyft could avoid costly lawsuits.<sup>137</sup>

These changes suggested by Harris and Krueger would help to protect every Uber and Lyft drivers; however other protections they address may be better aimed at drivers who work for the company in a more full-time capacity. For example, Harris and Krueger assert that independent workers should not be eligible for wage and hour protections, such as minimum wage, because it is too hard to measure to hours of a flexible, independent worker compared to a traditional employee.<sup>138</sup> While it is true that Uber and Lyft drivers work flexible, somewhat unpredictable hours, every hour they work is clocked in and out through the app. A better solution might be for Uber to pay minimum wage to drivers who work over thirty hours per week. Uber pays drivers on a weekly basis and uses the app to create a payment summary that shows the breakdown of all rides. It would be easy to calculate hours and pay drivers minimum wage just by requiring drivers to hit a thirty hour or more limit, and then referring to the app to see when that driver worked.

Another option might be to allow customers to tip Uber and Lyft drivers.<sup>139</sup> The U.S. Department of Labor does not require employers to pay minimum wage to a worker if the amount

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<sup>137</sup> It should be noted that Lyft and Uber already provides drivers with car insurance that varies depending on whether the driver is using the vehicle for personal use, using the app, or driving a passenger. Under Lyft, "the primary liability insurance is designed to act as the primary coverage during the period from the time you accept a ride request until the time the ride has ended in the app. The policy has a \$1,000,000 per accident limit. Note: If you already carry commercial insurance (or personal coverage providing specific coverage for ridesharing), Lyft's policy will continue to be excess to your insurance coverage." *Insurance Policy*, LYFT, <https://help.lyft.com/hc/en-us/articles/213584308-Insurance-Policy>. While drivers are on a trip, Uber covers, "\$1 million of liability coverage per incident. Uber holds a commercial insurance policy with \$1 million of coverage per incident. Drivers' liability to third parties is covered from the moment a driver accepts a trip to its conclusion. This policy is expressly primary to any personal auto coverage (However it will not take precedence over any commercial auto insurance for the vehicle). We have provided a \$1 million liability policy since commencing ridesharing in early 2013." *Insurance for uberX With Ridesharing*, UBER, <https://newsroom.uber.com/insurance-for-uberx-with-ridesharing/>.

<sup>138</sup> *Id.* at 20.

<sup>139</sup> There has been dispute about the social value of tipping. Some restaurant owners are moving to eliminate tipping and raise prices instead, arguing that laws against splitting tips with back of the house employees prevent employers from equally compensating. However, others have noted that tipping is a form of quality control, noting customer

paid plus tips received equals at least the federal minimum wage.<sup>140</sup> Currently, Uber's website discourages riders from tipping drivers.<sup>141</sup> Lyft's website provides instructions of how to tip a driver, but the reputation surrounding these platforms is that once the ride is over, the fare automatically charged is the final cost.<sup>142</sup> If both Uber and Lyft promoted tipping drivers, this may change how riders view the experience. Then, Uber and Lyft could avoid paying full minimum wage to drivers who make it in tips and only make up the difference in those who do not.

Similarly, health insurance could be distributed to drivers who reach the thirty-hour requirement. However, this presents a problem with maintaining neutrality of independent workers between the employer/ independent contractor classifications. Under the Affordable Care Act, employers must provide health insurance to employees who work thirty hours or more.<sup>143</sup> Instead, Harris and Krueger propose that intermediary companies pay a contribution equal to five percent out of independent workers' earnings to go towards health insurance tax subsidies.<sup>144</sup>

A new classification for the on-demand workforce could clear up ambiguities for courts that have previously attempted to pigeon hole these workers into the employee/independent contractor category. However, it is a lengthy conversation and one that would take years before it is implemented. The courts cannot create this new category of workers on their own, and therefore it will be left to the legislatures to provide a workable solution. In the meantime, the ongoing

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satisfaction and encouraging improvement in job performance and employee cooperation. See Samuel Estreicher & Jonathan Remy Nash, *The Case for Tipping and Unrestricted Tip-Pooling*, (NYU School of Law, Public Law Research Paper No. 16-05; NYU Law and Economics Research Paper No. 16-07.), available at <http://ssrn.com/abstract=2725699>.

<sup>140</sup> *What is the minimum wage for workers who receive tips?*, UNITED STATES DEPARTMENT OF LABOR, <http://webapps.dol.gov/elaws/faq/esa/flsa/002.htm>.

<sup>141</sup> *Do I need to tip my driver?*, HELP.UBER.COM, <https://help.uber.com/h/1be144ab-609a-43c5-82b5-b9c7de5ec073> (last visited Jan 25, 2016).

<sup>142</sup> *How to Tip Your Driver*, HELP.LYFT.COM, <https://help.lyft.com/hc/en-us/articles/213583978-How-to-Tip-Your-Driver> (last visited Jan. 25, 2016).

<sup>143</sup> *E.g.*, Harris and Krueger, *supra* note 7, at 20.

<sup>144</sup> *Id.*

lawsuits within the Ninth Circuit probably will not force Uber and Lyft to change their business model. Uber and Lyft are entirely constructed around its flexible drivers and independent contractor model. The cases, as of now, are limited to California drivers. These drivers are up against almost \$50 billion companies, so any damages they win will matter little in the general scheme of things. However, if the lawsuits spread, legislatures, Uber and Lyft will need to consider a new solution.

Uber and Lyft could potentially change their business model to make the drivers employees. However, if the drivers were to become employees they would not benefit from the flexibility that attracts many of them to the ride-share companies in the first place.<sup>145</sup> As it stands, Uber and Lyft drivers have control over when and how often they work. They are free to work other full-time jobs and still drive for Uber whenever the opportunity arises.<sup>146</sup> As employees, the employer would control their schedules.<sup>147</sup> The freedom to drive whenever and how frequently it is convenient for the driver would be lost.<sup>148</sup> Drivers who treat the job as a full-time job would benefit from this, but the many other drivers who do not would suffer.<sup>149</sup> Uber would likely compensate for rising labor costs by taking a larger cut in fares and decreasing its workforce.<sup>150</sup> As we address possible solutions to the on-demand dichotomy and ways to better protect worker interests, we must keep in mind that many workers are interested in preserving the flexibility and freedom that first attracted them to Uber and Lyft.

#### IV. Conclusion

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<sup>145</sup> Benjamin Means and Joseph A. Seiner, *Navigating The Uber Economy*, 49 U.C. DAVIS L. REV. (forthcoming 2016).

<sup>146</sup> *Id.*

<sup>147</sup> *Id.*

<sup>148</sup> *Id.*

<sup>149</sup> James Surowiecki, *Gigs With Benefits*, THE NEW YORKER, July 2015, <http://www.newyorker.com/magazine/2015/07/06/gigs-with-benefits>.

<sup>150</sup> *Id.*

The recent Uber and Lyft cases provide insight into the outdated employment classification test in California in light of the changing economy. However, on a broader scale it raises issues about what benefits and protections workers are entitled to when they are not an employee or independent contractor, but something in between. Ultimately, creating a new category of workers could strengthen the on-demand workforce and clear ambiguity among courts that have wrestled with these employment relationships.