THE WALL STREET JOURNAL.

AS THE GIG ECONOMY CHANGES WORK, SO SHOULD RULES

Workplace rules need to evolve for the sharing economy to grow while protecting workers

By Greg Ip
December 9, 2015

Ride-sharing companies like Uber Technologies have transformed not just the world of travel, but also the world of work. Uber now boasts 400,000 drivers, up from none four years ago.

Yet while Uber's disruption of the staid world of taxis has drawn widespread admiration, its work practices have been more controversial. Its drivers are independent contractors, not employees.

This is good for Uber: It has labor on demand, paid for only as long as it's needed. It's also good for many of its drivers. They can work as much as they want, when they want, to accommodate other jobs and family obligations.

But some worker advocates, and the Obama administration, worry such arrangements deprive workers of benefits and rights they would have as employees, from the right to form unions to vacation pay and health benefits. A group of Uber drivers suing to be treated as employees was recently granted class-action status in San Francisco.

The controversy highlights a little-appreciated gap in the U.S. economy: its labor laws and institutions haven't kept up with how the needs of businesses and workers have changed. In the U.S., you are either an employee, or you aren't. What the U.S. needs, a new study says, is a new category for gig-economy jobs that blends elements of both.

History shows that as technology transforms the economy, it also transforms work. Self-employed farmers and skilled craftsmen were the norm in the pre-industrial United States. But as technology such as power looms displaced craft skills, factories found themselves in need of permanent, specialized work forces. Those needs were met by new supplies of labor—young women leaving their farms, or poor Irish immigrants fleeing famine, for example.

Technology and management enabled companies to grow ever larger. As the economist Ronald Coase later demonstrated, the size of a company was determined by whether it was more efficient to acquire inputs (such as labor) on the open market or in-house. Big U.S. companies had to employ thousands of workers in countless occupations to achieve economies of scale and offer a range of products. To regulate the work place, the Fair Labor Standards Act was passed in 1938, establishing a maximum work week over which an employer had to pay overtime rates, and a minimum wage.

In recent decades, outsourcing and technology have enabled companies to move many tasks out from under their own roofs. Meanwhile, many workers want the flexibility of part-time work or telecommuting. Today, nearly a third of U.S. workers are in "contingent" arrangements such as temp firms, part-time jobs or day laborers.

Companies like Uber, ride-sharing rival Lyft and Grubhub act as intermediaries, matching a ready supply of labor to customer demand. This is Coase's insight in reverse. Since all the information Uber needs to connect its customers and drivers is in its app, it doesn't have to own cars or employ drivers. Whether a driver works one hour a week or 60 depends entirely on the driver's willingness to drive and the demand for rides.

In a new paper from the Hamilton Project, a liberal think-tank, Seth Harris, a Cornell University professor of industrial and labor relations, and Alan Krueger, a Princeton University economist, argue these characteristics differ from a typical employee because they supply only as many hours as they like. (Mr. Krueger has previously conducted research for Uber; Uber had no role in the latest study.)

Classifying them as employees would immediately raise several prickly questions. Should Uber drivers be compensated for the time they spend waiting for rides? Should such time go toward determining a minimum hourly wage? Would driving for Lyft violate an employee's duty of loyalty to Uber?

Messrs. Harris and Krueger propose a new "independent worker" designation for such employees. They need not be covered by the National Labor Relations Act, but could jointly negotiate work conditions through an exemption to antitrust laws.

The employer would have to deduct Social Security and Medicare contributions and withhold income tax. They would not be covered by federal overtime or minimum wage laws, or workers' compensation and unemployment insurance, none of which are well suited to how independent workers operate. They would, however, be protected by federal anti-discrimination laws, and could be pooled with other workers so that the employer could obtain health insurance more cheaply for them.

The object, Messrs. Harris and Krueger say, is to ensure that such companies thrive based on the strengths of their business model, not on "regulatory arbitrage," that is, their ability to pay less for employees than other firms do.

To be sure, the spread of contingent work arrangements is often a sign that governments have already burdened regular hires with onerous and costly regulations. This has left many European economies with labor markets polarized between secure, permanent jobs and precarious temporary ones. Extending basic rights to workers in the on-demand economy should not involve burdening all employers with costs that ultimately hurt economic growth.