INDEPENDENT WORK

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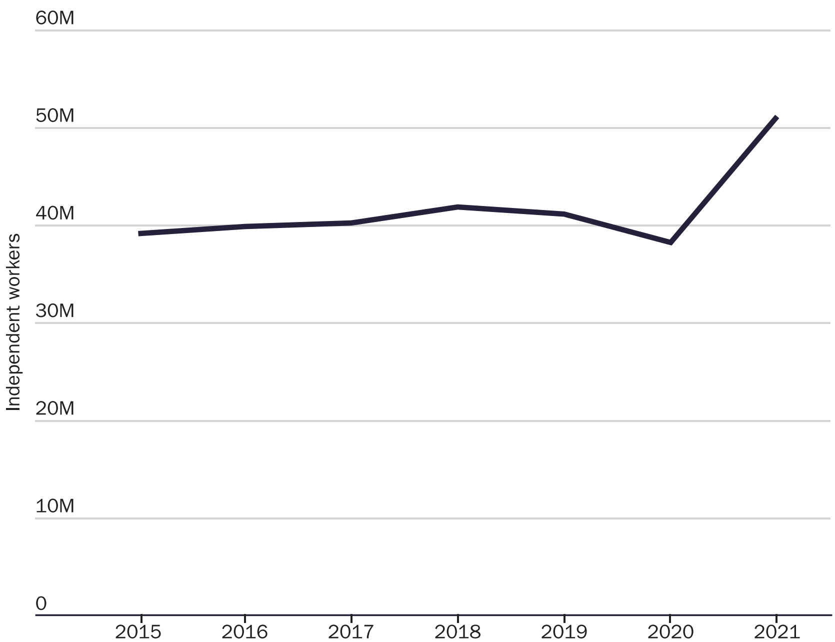
THE ISSUE: GOVERNMENT POLICIES DISCOURAGE OR EVEN PROHIBIT INDEPENDENT WORK, WHICH IS INCREASINGLY PREVALENT AND OFTEN PREFERRED BY AMERICAN WORKERS OVER TRADITIONAL ARRANGEMENTS

Almost all political discussions about the American worker address traditional employees, who work for a single employer providing regular compensation in exchange for controlling how, where, and when the employees' work will be completed. Yet the U.S. freelancing platform Upwork estimated that at some point in 2021, about 36 percent of the American workforce engaged in independent work—in which individuals take on short-term, specific assignments from multiple clients, relatively free from the clients' control or direction.[1] These numbers swelled during the pandemic: the more than 50 million independent American workers in 2021 represented a 25 percent increase from 2019 (see Figure 1).[2]

FIGURE 1 The United States gained almost 13 million independent workers in 2021



Source: "11th Annual State of Independence: The Great Realization," MBO Partners, December 2021.
Note: Includes those who engage in full-time, part-time, and occasional independent work.

While independent work often conjures images of supposedly "exploited" Uber drivers and DoorDash deliverers, the reality is far different. The IRS reports, for example, that only about 8.6 percent of all independent workers are employed in gig work (i.e., online platforms that enable on-demand services for the consumer and a flexible work arrangement for the provider), and the most common occupations for independent workers are in marketing, communications, and computer programming.[3] Freelance or contract work, moreover, is undertaken in almost every industry.

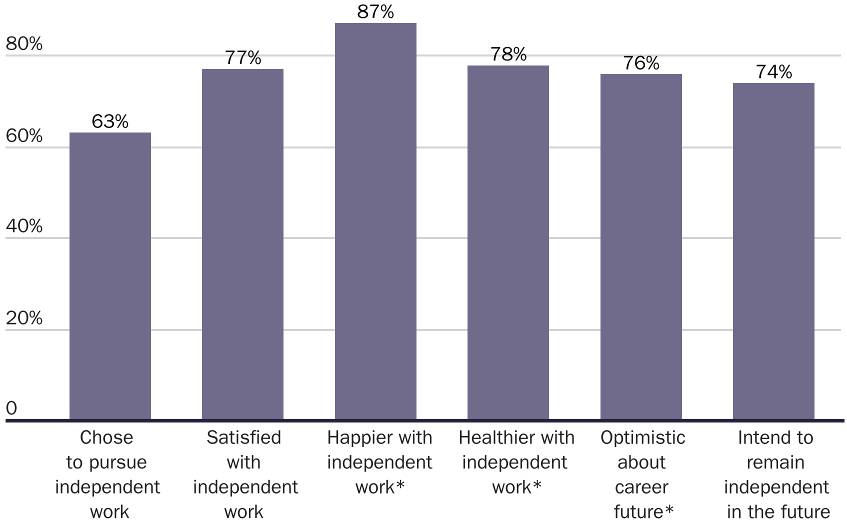
Much of this work is also high-paying: the *Wall Street Journal* reported in 2022 that many skilled freelancers make six-figure incomes, while Ravenelle and Kowalski (2022) found that these workers can command a $1,000 per day "minimum wage" on various global freelance platforms.[4] Yet policies seeking to discipline or even eliminate gig work usually affect these jobs too.

Furthermore, most Americans enter independent work arrangements because they prefer them to the more structured and controlled form of traditional employment, not because they have no other choice. A 2021 Upwork survey, for example, found that over 70 percent of both full-time and part-time independent workers see increased flexibility as the major reason for engaging in independent work.[5] A separate 2021 survey from MBO Partners showed that nearly 90 percent of respondents were happier in independent work than in traditional jobs and that roughly three-quarters of independent workers are satisfied with their work, intend to remain in independent work, and are optimistic about their career future (see Figure 2). By contrast, just 11 percent of these independent workers wanted to find full-time traditional employment.[6]

This preference extends to oft-maligned gig work. According to a 2021 Pew Research Center survey, for example, almost 80 percent of gig platform workers rated their experiences positively, with almost half citing schedule flexibility as a major reason for doing the work. Only 28 percent of respondents said they performed gig work because there were few other job opportunities available where they live.[7] And an examination by Chen et al. (2019) of more than a million U.S. Uber drivers over an eight-month period found that drivers valued the flexibility the arrangement provided—in both the timing and amount of work—at $150 per week (or 40 percent of expected earnings). Chen et al. also found that drivers would need a 50 percent raise to work for a less flexible taxicab company.[8]

Beyond the simple preference among many Americans for independent work are its significant economic benefits, which include boosting entrepreneurship, dynamism, and growth. Barrios et al. (2022) showed, for example, that the entrance of new gig economy platforms in different cities increased both new business registrations and new business loans in those places by roughly 5 percent, with the effect most pronounced in economically depressed areas.[9] Independent work also proved to be critical during the pandemic when, due to government restrictions or structural economic shifts, certain traditional employment options

FIGURE 2 Most independent workers viewed their work positively in 2021



Source: "11th Annual State of Independence: The Great Realization," MBO Partners, December 2021.

Note: Questions were asked of full-time, part-time, and occasional independent workers.

* Denotes a question asked of full-time independent workers only.

disappeared. Much of the substantial uptick in new business formations in 2020–2021, in fact, can be attributed to increasing numbers of independent workers, both individuals selling goods on e-commerce platforms and traditional freelance workers in service sectors.[10] And as noted in the Introduction, this increase has not been limited to white-collar professionals: for example, the number of new independent truck drivers increased from 43,953 in 2018 to more than 109,000 in 2021, with an estimated 70 percent of these being single-driver operations.[11]

Finally, independent work has been a boon for consumers—both businesses and individuals—beyond simply the benefits arising from new competition (more and more innovative choices, lower prices, etc.). Research shows, for example, that ridesharing services such as Uber and Lyft have reduced drunk driving and drinking-related car crashes as more people choose to take a rideshare home rather than risk driving under the influence.[12] Meanwhile, food delivery services such as DoorDash and Uber Eats greatly assisted restaurants in weathering lockdowns imposed during the COVID-19 pandemic, as customers turned to food delivery when dine-in services were not allowed.[13] And recently, new gig platforms such as Bite Ninja have helped restaurants navigate shortages of drive-thru workers.[14] Beyond gig work, a 2021 Mercatus Center survey found that 57 percent of tech startup executives report that independent workers are an essential part of the function of their businesses.[15]

Despite these trends, many current and proposed laws restrict or even prohibit independent work, and politicians routinely demonize it. In 2019, for example, California enacted Assembly Bill 5 (AB 5), which expands the definition of "employee" to encompass many independent workers. Under the law, an independent worker must be free from the control of the entity for which the work is performed; perform work that is different from the hiring entity's usual business; and already work in the same trade, occupation, or business as the work being performed for the hiring entity (known as the "ABC test"). If these conditions are not met, the government considers a worker to be an employee.[16] A similar proposal that passed the U.S. House of Representatives in 2021—the Protecting the Right to Organize Act—would employ this test nationally to determine the status of independent workers.[17]

Although AB 5 garners most of the media attention, California is hardly the first state to utilize the ABC test. Massachusetts has employed it since 2005, but gig workers like Uber and Lyft drivers have thus far been treated as independent workers. Such an exemption may not hold: the state attorney general has challenged the rule, arguing that gig workers should be treated as employees under the commonwealth's statute, and the lawsuit is pending in a Massachusetts court as of August 2022.[18] In addition to California and Massachusetts, four states—Connecticut, Nebraska, New Jersey, and Vermont—restricted independent work in a similar fashion as of April 2021, while nearly 20 others utilized the ABC test to determine unemployment insurance eligibility.[19] Also, AB 5–style legislation has been proposed in Virginia, Washington State, and New York.[20]

These laws have serious consequences for workers and companies—not merely those in the gig economy. Forcibly reclassifying independent workers as traditional employees would subject their work to various labor regulations, often to the workers' detriment. For example, the Affordable Care Act requires that all companies with at least 50 full-time employees (defined as working at least 30 hours per week) provide health insurance to these workers and their families or face steep penalties.[21] According to a 2021 Trump White House Council of Economic Advisors report, studies have shown that this employer mandate can impose significant costs, particularly when it comes to smaller firms. The cost of providing government-mandated health coverage, including the higher administrative costs that smaller firms face, suppresses employees' wages and discourages small firms from adding jobs so as to avoid the mandate entirely.[22] As noted in the Private-Sector Labor Regulation and Employee Benefits chapters, moreover, other regulations dictating employee hours, schedules, and content eliminate the freedom and flexibility that independent workers desire, while accompanying wage and non-health benefit requirements would make them even more costly to hire for employers, potentially resulting in less work or pricing the workers out of the market.[23]

Given these and other legal requirements, a 2019 Barclays study estimated that classifying a rideshare driver as an employee would cost Uber an additional $3,625 per driver (approximately $3.6 billion overall using Uber's data on its number of U.S. drivers), and in 2020 Uber estimated reclassification would force the company to terminate more than 900,000 drivers nationally.[24] And following the passage of AB 5, Vox terminated 200 freelance writers in California for similar reasons.[25] As discussed in the Private-Sector Labor Regulation and Employee Benefits chapters, moreover, expanding labor regulations to cover independent workers also would likely diminish labor market fluidity and dynamism, which has been found to boost workers' lifetime earnings and productivity.

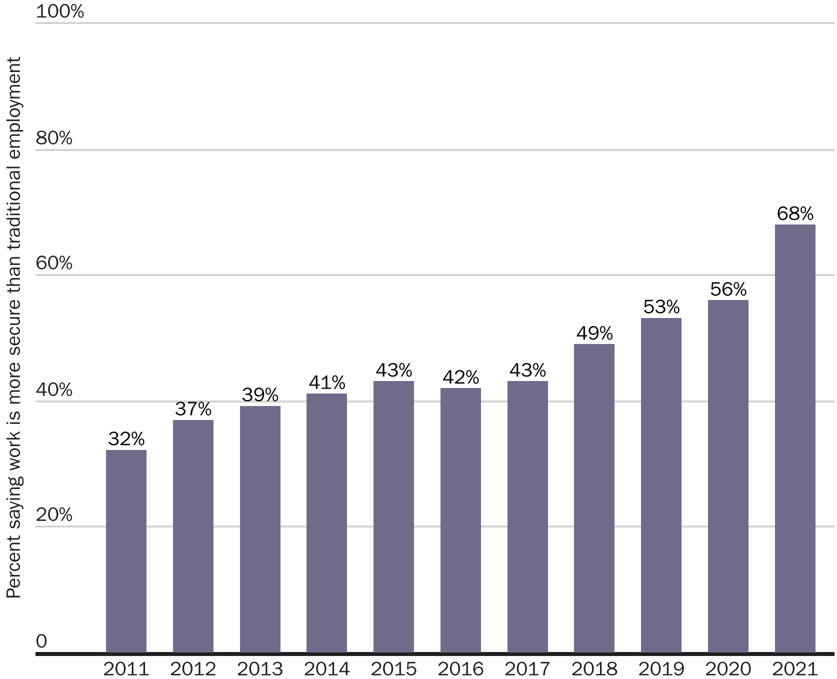
The additional costs associated with bills such as AB 5 would disproportionately harm smaller companies and startups that often rely on independent workers or lack the resources to offshore or automate certain core functions—thus benefiting large corporations and fueling the very market concentration that many AB 5 supporters claim to oppose.[26] These laws also would likely eliminate many common and widely accepted forms of independent work. For example, a freelance writer who contracts to write articles for online magazines would be considered an employee because the work is in line with the publications' usual business. A freelance fashion photographer would also be an employee because requirements to work at certain times (e.g., during a runway show) mean that the worker is not free from the hiring entity's control.

To assuage some of these concerns, and as a result of public outcry from independent workers themselves, California significantly reduced the scope of AB 5 to exempt more than 110 occupations, including photographers and writers, and ballot initiative Proposition 22 exempted gig economy workers.[27] However, many other common professions, such as the popular owner-operator model in domestic freight trucking, remain imperiled.[28] In fact, when court rulings applied AB 5 to commercial trucking in July 2022, potentially eliminating 70,000 independent truck owner-operators in California, hundreds of truckers protested their reclassification as employees and temporarily blockaded the Port of Oakland, one of the busiest shipping hubs in the country.[29]

These realities undermine proponents' most common justifications for new restrictions on independent work and reveal serious misunderstandings about it. First, they ignore that majorities of independent workers are satisfied with their incomes and work arrangements. For example, 58 percent of full-time independent workers reported they made more money than if they had been engaged in traditional employment, and 68 percent consider their work more secure than traditional employment (see Figure 3).[30] In Massachusetts, 83 percent of rideshare drivers want to remain independent workers, despite efforts to reclassify them as employees.[31]

Second, new restrictions on independent work would eliminate a critical lifeline for workers facing unemployment or other sudden declines in income. For example, a study of over 45,000 individuals from the United States, United Kingdom, and Italy found that respondents were more likely to migrate from

FIGURE 3 Independent workers increasingly say their work is more secure than traditional employment



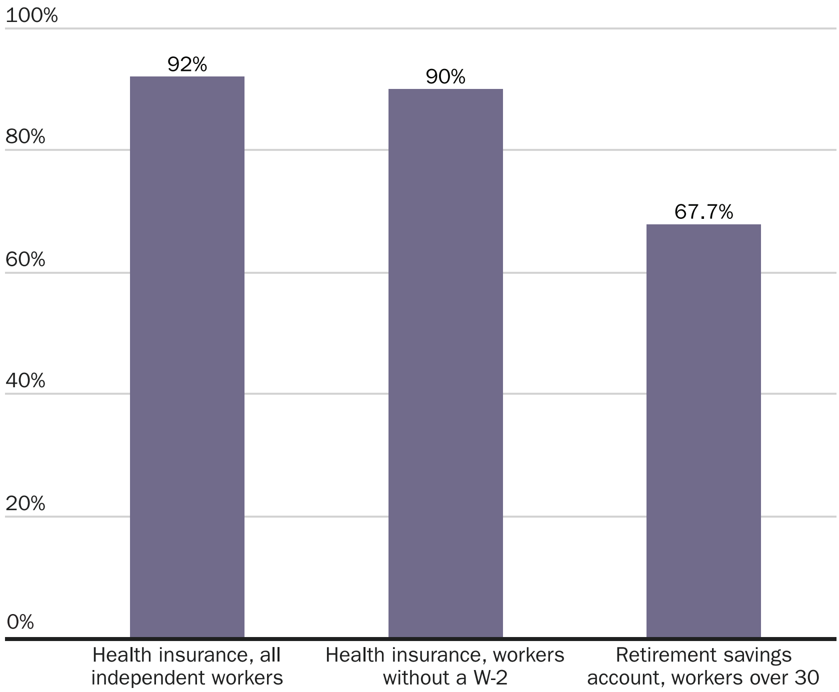
Sources: "11th Annual State of Independence: The Great Realization," MBO Partners, December 2021; "The State of Independence in America 2020: A Decade of Independence: Trends that Matter," MBO Partners, December 2020; and "The State of Independence in America: 2019: The Changing Nature of the American Workforce," MBO Partners, June 2019.
Note: Responses are from full-time independent workers only.

unemployment to independent work, rather than from traditional employment to independent work.[32] The gig economy plays a similar role: Huang et al. (2020) found that a 1 percent increase in unemployment in a particular U.S. county led to a 21.8 percent increase in gig economy employment among county residents.[33] Eliminating this option via regulation could therefore harm many American workers who are trying to get back on their feet following an unexpected disruption in employment or a broader economic downturn.

Third, proponents of independent work regulations ignore that health, retirement, and other benefits are available to independent workers outside their workplaces. Health insurance, for example, may be obtained through a spouse, private markets, or government programs (although this can be improved, as discussed in the following section). Several retirement account options, such as a SIMPLE IRA or a 401(k), are also available to many independent workers. In fact, over 90 percent of independent workers have health insurance, and roughly two-thirds have a retirement savings account—figures similar to those of the general American workforce (see Figure 4).[34]

Fourth, concerns about independent workers' hours, wages, and benefits ignore that many independent workers do not work full-time in the field at issue and instead use the arrangement as a "side hustle" to pay for school or to pursue their passions. In fact, a survey by Brannon and Wolf (2021) of independent workers in Michigan, Ohio, and Pennsylvania found that more than 80 percent of respondents used part-time independent work to supplement a main source of income.[35] A 2021 report by MBO Partners found that roughly two-thirds of independent workers are either part-time or occasional independent workers.[36] And according to the Bernhardt et al. (2022) review of California taxpayers, independent work accounts for only 10.6 percent of earnings for the median worker with both traditional and independent work income.[37] Restrictions on independent work could deny these individuals an important source of extra income or the ability to follow their dreams in music, art, and other fields.

FIGURE 4 Most independent workers had a health insurance and retirement account in 2019



Source: Ike Brannon and Samuel Wolf, "An Empirical Snapshot of the Gig Economy," *Regulation* 44, no. 4 (Fall 2021): 4–8.
Note: Survey of 1,082 part-time and full-time independent workers in Michigan, Ohio, and Pennsylvania.

Beyond outright restrictions on independent work, federal tax laws can otherwise discourage it. For example, independent workers often overpay taxes or face monetary penalties because federal law requires most self-employed individuals to submit estimated quarterly tax payments or face penalties, even if they are owed a refund. More than one-third of independent workers were unaware of the need to file quarterly tax estimates in 2018 and thus faced hundreds of dollars in IRS penalties.[38] Many independent workers are also confounded by, or unaware of, various deductions to lower their tax burden. An independent worker must undertake almost twice as many steps to file taxes as a comparable traditional worker, and a recent survey found that only half of independent workers were aware of the tax deductions for which they may be eligible.[39] These rules can not only impose financial hardship on current independent workers but also make independent work less attractive to others considering it.

Starting in 2022, taxes became even more complicated and cumbersome for many independent workers and the online platforms that they utilize. In particular, federal tax reporting and filing (through form 1099-K) is now required for online sales of goods and services through a third-party payment service after a seller receives just $600 in gross annual payments (including fees, taxes, and even canceled orders), up from the previous $20,000 or 200 transactions minimum.[40] Seven states (California, Maryland, Massachusetts, Mississippi, Missouri, Vermont, and Virginia) and the District of Columbia have the same $600 reporting requirement for state taxes, while several other states have similar requirements with different, but still low, thresholds.[41] Freelancers, consultants, and gig platform workers will likely receive a different form, 1099-NEC, that has a similar reporting requirement.

Thus, for example, a working mom who uses Etsy and similar websites to sell artwork in her spare time will now receive a 1099-K tax form from each site at which she received more than $600 during a calendar year, even though she could hardly be considered employed in the gig economy and had numerous expenses (materials, marketing, etc.) that would—if she were aware and keeping track of them—reduce her final tax liability. Individuals simply reselling their own property would also receive these forms, even if they sold at a loss (and thus owe no taxes).[42] Given how many Americans use third-party sales sites to supplement their incomes, this change will likely increase tax reporting and compliance burdens for millions of people, discouraging them from engaging in independent work.

THE POLICY SOLUTIONS: AVOID OR REPEAL NEW LAWS RESTRICTING INDEPENDENT WORK AND EASE TAX BURDENS ON INDEPENDENT WORKERS

Policymakers should allow independent workers to remain independent rather than forcing millions of Americans into unwanted employee arrangements. Unfortunately, many jurisdictions are following California and doing the opposite, despite independent work's unique benefits and many Americans' desire to pursue it. To preserve workers' flexibility and independence, all such laws should be repealed—not merely riddled with new exceptions—and new proposals should be rejected.

Policymakers should also look to ease tax burdens on independent workers. First, to simplify tax compliance, Congress should enact a standard business deduction (SBD) that independent workers could use instead of reporting individual business expenses (such as an Uber driver's car maintenance)—a process that can be particularly cumbersome for many types of independent work. The standard business deduction would operate like the standard deduction for income and would be a percentage of an independent worker's income. Proponents of such a reform, such as University of North Carolina at Chapel Hill law professor Kathleen DeLaney Thomas and the Tax Foundation, suggest that the deduction should be 60 percent of income, while the remaining 40 percent would be taxable, a level that is comparable to average profit levels. Much like employee income taxes, independent workers could choose to continue to itemize business expenses instead of using the SBD.[43]

Second, Congress should allow companies to voluntarily withhold taxes from independent workers' wages, as is already the case for traditional employees. Companies could estimate an independent worker's income from their platform using the 1099 tax forms and, utilizing the new SBD, then withhold appropriate taxes on the remaining wages. (Proposals differ on the "appropriate" level of taxes withheld—based on workers' estimates or a simpler flat rate—but this detail need not be determined here.) Voluntary withholding would further simplify the tax code and do away with quarterly estimated payments—and penalties—for workers who choose to opt-in to the system and work primarily for companies, not individuals. Thus, for example, a wedding photographer hired by an engaged couple might not have taxes withheld, but a fashion photographer hired by a magazine could opt for withholding.[44]

Third, Congress and the states also should repeal the new $600 minimum for 1099-K reporting, which is unnecessary and burdensome (for workers, companies, and the IRS). Rather than return to the previous $20,000 or 200 transactions thresholds, which may have missed significant taxable income, policymakers could choose a middle ground—low enough to capture taxable income from individuals frequently engaging in independent work but high enough to exempt occasional sellers and hobbyists from needless paperwork. For example, both the National Taxpayers Union and congressional Democrats' Cut Red Tape for Online Sales Act have suggested setting the threshold at $5,000.[45] Congress should also reinstate a set number of transactions needed to trigger 1099-K reporting but lower the threshold to 25 or 50 transactions, thus again only subjecting those who are routinely engaged in the gig economy to IRS filing requirements.

Finally, many policy recommendations in other chapters would also benefit independent workers. For example, expanding the size and scope of health savings accounts as the Health Care chapter proposes would help independent workers, especially those who lack health insurance or health care savings, and might also encourage current "job-locked" employees to venture out on their own. Tax-advantaged universal savings accounts, as recommended in the Employee Benefits chapter, would help independent workers save for potential lulls in new business (or for any other reason). The Occupational Licensing chapter explains that eliminating and reforming licensure would increase access to, and support the viability of, many independent work professions that are currently restricted by law, such as freelance hair braiders, florists, and tour guides. And standardizing income tax and tax nexus requirements, as discussed in the Remote Work chapter, would benefit independent workers who sell their services or goods across state lines (or engage in interstate travel to do so).

ACTION PLAN

Given millions of Americans' clear preference for independent work and the economic benefits of these arrangements, legislators at both the state level and federal level should reduce regulatory and tax burdens on both independent workers and gig platforms.

Congress should

- refrain from passing legislation like the Protecting the Right to Organize Act or any other bill that expands the definition of an "employee" to include common independent work arrangements;
- enact an SBD of 60 percent of an independent worker's earnings, thus simplifying tax filing and compliance (workers could elect not to claim the deduction and could then continue to utilize the existing itemized tax system);
- allow companies and independent workers to agree to withhold a portion of the workers' earnings from the 1099 form as an estimated tax payment to further simplify tax filing and compliance;

- repeal the new $600 minimum for 1099-K reporting, replacing it with a significantly higher (e.g., $5,000 or 25 transactions) threshold for tax reporting; and
- allow independent workers to open and contribute tax-free funds to large health savings accounts and universal savings accounts, as the Health Care and Employee Benefits chapters respectively propose.

State governments should

- repeal laws that expand the definition of "employee," such as California's AB 5, or refrain from implementing such laws; and
- repeal minimum 1099-K reporting requirements and match them to the new federal standard recommended above.

Governments should also implement the reforms recommended in the other chapters, such as the Occupational Licensing and Remote Work chapters, which includes recommendations that would further benefit independent workers.

NOTES

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