



TESTIMONY ON GROWTH, OPPORTUNITY, AND CHANGE IN THE U.S. LABOR MARKET

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Chairman Walberg, Ranking Member Sablan, and members of the Subcommittee on Health, Employment, Labor, and Pensions, thank you for the opportunity to testify on the changing American workforce. My name is Jared Meyer, and I am a senior fellow at the Foundation for Government Accountability (FGA). FGA is a non-profit research organization that focuses on promoting work at both the state and federal levels.

## The Economic Trends Changing the U.S. Workforce

The 21<sup>st</sup>-century American economy has been generating more jobs in which workers are self-employed. High-profile growth in online “sharing economy” platforms such as Airbnb, Lyft, and Thumbtack have brought increased attention to this change in the workforce. While people working through online platform companies account for a small percentage of the U.S. labor force,<sup>i</sup> the individualized work arrangements that these business models embrace make up a much larger, and growing, percentage of overall work.

The key to understanding the rise in the type of independent work seen in the sharing economy is the realization that the driving force behind these changes is not flashy smartphone apps but lower transaction costs.<sup>ii</sup> Lower transaction costs affect every industry, not just for-hire transportation and travel lodging.

The Nobel Prize-winning economist Ronald Coase’s transaction cost theory of the firm helps explain these changes in the American workforce.<sup>iii</sup> In the 20<sup>th</sup> century, the financial and time costs were too high for many firms to benefit from contracting out work. Everything from finding the right provider and coming to an agreement on cost, to determining quality and enforcing contracts, carried higher costs than they do today. As an example, high transaction costs meant that it would have made more financial sense for a company to hire a graphic designer as a full-time employee, even if it would have been ideal to find contract professionals with the specific expertise for each design task.

But today, lower transaction costs, driven by advances in technology, have led to more opportunities for firms to use outside workers rather than in-house employees. Independent contractors are the driving force behind this change. Working as an independent contractor allows someone to choose his or her hours and benefit from flexible work arrangements.

Across all sectors of the economy, technology creates entrepreneurial opportunities for anyone with productive resources. These resources can be anything from physical or intellectual services (such as handyman jobs, academic tutoring, and legal advice) to the use of property (be it a drill, car, or spare room).

It is still difficult to start a business and work for oneself. But prior to the rise of peer-to-peer online interaction, growing a business was even more difficult. By catering to producers of niche products, online platforms like the craft shop Etsy help launch widely successful independent companies. These platform businesses allow independent workers to reach customers all over the world. eBay has provided a similar type of benefit to sellers since 1995. In other words, lower transaction costs make it easier for millions of Americans to work for themselves.

Most U.S. labor policy is designed for a workforce that is comprised primarily of employees.<sup>iv</sup> Though the employee-employer model of work is still the most common work relationship, further advances in technology and changing worker preferences should lead to steadily-increasing levels of alternative work arrangements.

Implementing the right policy changes to accommodate this change will require accurate data on workforce trends. Thankfully, the Bureau of Labor Statistics (BLS) recently released a survey that attempts to measure the prevalence of non-traditional work arrangements. While the committee should applaud BLS for taking this step, several changes would make the survey's results more comprehensive.

## **The Findings of the May 2017 Contingent Worker Supplement**

To more clearly understand how these fundamental changes are affecting the labor market, BLS created the Contingent Worker Supplement (CWS) to the monthly Current Population Survey (CPS).<sup>v</sup> The CPS surveys 60,000 eligible households and provides reliable employment data used by policymakers and the public. The most recent edition of the CWS was released on June 7, 2018. This followed a 13-year break from BLS conducting the CSW, which was released previously in 1995, 1997, 1999, 2001, and 2005.

The survey, based on May 2017 data, estimated the number of contingent workers and workers in alternative arrangements, with the two categories considered separately. As defined in the survey, contingent workers are comprised of those who do not expect their jobs to last or who work temporary jobs. Alternative work arrangements include independent contractors, on-call workers, temporary help agency workers, and workers provided by contract firms. The survey's questions referred to the characteristics of respondents' jobs in which they worked the most hours and were based on work performed during the previous week.

According to the results of the survey, independent contractors are the most common of the four alternative work arrangements. Given the prevalence of independent contractors and the structural changes that are affecting the U.S. labor market, the CWS's measurement of this alternative work arrangement requires additional attention, and my testimony will focus primarily on the measurement of independent contractors. Independent contractors are defined as "Independent contractors, consultants, and freelance workers, regardless of whether they are self-employed or wage and salary workers."

According to the CWS, in May 2017, there were 10.6 million independent contractors, representing 6.9 percent of total employment. Independent contractors were 6.7 percent of the workforce in 1995, 6.7 percent of the workforce in 1997, 6.3 percent of the workforce in 1999, 6.4 percent of the workforce in 2001, and 7.4 percent of the workforce in 2005. All previous surveys were conducted in February, but there is little evidence that conducting the survey in May makes the most recent data not comparable.

Only three percent of independent contractors were also classified as contingent workers. This is the same percentage as workers in traditional arrangements and the lowest number among alternative work arrangement categories. This data point shows that most independent contractors are secure in their line of work, which should allay common concerns that workers outside of the traditional employer-employee relationship face job insecurity.

Median weekly earnings for full-time independent contractors were \$851, which is similar to those for workers in traditional arrangements (\$884). Median weekly earnings for part-time independent contractors were \$333, which is higher than the average earnings for part-time workers in traditional arrangements (\$255). Furthermore, educational attainment among independent contractors was in line with workers in traditional work arrangements, providing evidence that people of all education and skill levels can find work as independent

contractors. Far from only encompassing some of the relatively low-paying jobs found in the sharing economy, the most common industry in which independent contractors work is professional and business services.

It should also be noted that, from 2005 to 2017, inflation-adjusted median earnings for full-time independent contractors decreased at a lower rate than the median for all full-time employed workers. While full-time independent contractor median earnings decreased by 0.5 percent over that time, all the median earnings for all full-time employed workers fell by 1.5 percent.<sup>vi</sup> Similarly, from 1997 to 2005, full-time independent contractor median earnings increased by an inflation-adjusted 1.6 percent while median earnings for all full-time employed workers rose by 0.9 percent. A factor outside of weekly pay that could affect this comparison is the rising share of overall compensation that comes from employer-sponsored health insurance.

## Why the CWS's Independent Contractor Data Are Low

According to the CWS, 84 percent of workers with traditional arrangements had health insurance coverage, and 53 percent of these workers received health insurance benefits through their employers. Among independent contractors, 75 percent had health insurance coverage, which they obtained through another family member's policy, a government program, or purchasing it on their own.

Employers are the principal source of health insurance in the United States, providing health benefits to about 151 million non-elderly people. In 2017, the average annual premiums for employer-sponsored health insurance were \$6,690 for single coverage and \$18,764 for family coverage. For employer-sponsored health insurance, the average single premium increased four percent, and the average family premium increased three percent from 2016 to 2017.<sup>vii</sup>

Outside of the employer-sponsored health insurance market, about 22 million people had individual health insurance coverage in 2017. For this market, premiums per enrollee grew 22 percent over the prior year.<sup>viii</sup> Premiums for individual market coverage have more than doubled from 2013 to 2017.<sup>ix</sup> This difference in health insurance costs is a contributing factor to the stagnation of people who are working primarily as independent contractors.

Employer and employee contributions to employer-sponsored health insurance are excluded from federal and state income and payroll taxes. The estimated tax subsidy for this form of coverage was \$250 billion in 2013.<sup>x</sup> Because this favorable tax treatment is not available for independent contractors, there is an incentive for people to remain in employer-employee relationships to access more affordable health insurance. As health insurance costs continue to increase faster for the individual market, this incentive will grow larger.

Despite the problems with affording individual health insurance, 79 percent of independent contractors identified by the CWS prefer their arrangement over a traditional job and only nine percent would prefer a traditional work arrangement. These preferences are in line with the data from the 1995 CWS release. Workers value flexibility, and this preference can be seen clearly in young workers' priorities.

Deloitte's 2018 millennial survey finds that 78 percent of people born from the beginning of 1983 to the end of 1994 would consider short-term contracts or freelance work to supplement full-time employment. Furthermore, 57 percent would consider this type of alternative work instead of full-time employment.<sup>xi</sup> Beyond the potential

for higher income, flexibility and work/life balance are the top reasons why young workers are interested in alternative work arrangements.

The value of independent contractor work as supplemental income cannot be ignored. For the 70 percent of Americans ages 18 to 24 who experience an average change of over 30 percent in their monthly incomes, the opportunity to smooth out earnings to meet rent, pay down student loans, or fund a new business venture is a clear benefit of alternative work arrangements.<sup>xii</sup>

The main shortcoming of the CWS is that it only measures alternative work arrangements if the jobs are the respondents' primary source of income. This decision likely explains most of the reason why the CWS results differ drastically from other reputable estimates.

Another factor that lowers the CWS's estimates of overall independent work is the decision to exclude self-employed people who are not independent contractors (such as shop or restaurant owners). While there is potential for confusion from some respondents if they owned an Etsy shop, for example, BLS's decision makes sense given that this group of self-employed people is captured under BLS's regular CPS survey. As the CWS's technical note states, "Nearly 9 in 10 independent contractors are self-employed. Conversely, 3 in every 5 self-employed workers are independent contractors."<sup>xiii</sup>

If BLS updates the CWS survey to capture those who use alternative work arrangements for supplemental income, then it should also ask respondents about work done over the previous year. The May 2017 CWS only asks about work in the previous week, and participation in part-time independent contractor work can be seasonal. For example, those who work construction jobs may work as a math tutor over the slower winter, or college students may drive for a ridesharing firm during summer breaks.

Other BLS numbers from the CPS could explain why the number of people who earn most of their income from alternative work arrangements has not risen. The seasonally-adjusted unemployment rate stands at 3.8 percent, a level that was last seen in 2000.<sup>xiv</sup> Some scholars have suggested that alternative work arrangements are counter-cyclical, meaning participation increases when the labor market is weak.<sup>xv</sup> Given the tax-preferred treatment of health insurance for employees, it is understandable why someone would forego flexibility in favor of full-time employment when the job market is as strong as it is today.

It should be noted that BLS added four new questions to the May 2017 CWS. These questions attempt to measure electronically-mediated employment, like those independent contractor jobs found through popular sharing-economy companies. The data from these questions are yet to be released, though they are expected to be made public later this year. While these results should be interesting, it is more important that the CWS captures supplemental independent contractor status work in future editions of the survey, regardless of if it was mediated by online platforms.

## **Other Measures of Alternative Work Arrangements**

During the 13-year gap between CWS releases, a variety of government, nonprofit, academic, and industry organizations attempted to estimate the growth in alternative work arrangements. While estimates vary depending on how alternative work is defined, the consensus reached is that the number of people working as

independent contractors has increased over recent years. This conclusion differs from the conclusion one would reach from CWS's data, lending further evidence to the claim that BLS's statistical picture of alternative work is incomplete.

For example, a 2017 report from Upwork, the Freelancers Union, and Edelman Intelligence estimates that nearly 60 million Americans are freelancing, which translates to 36 percent of the workforce.<sup>xvi</sup> From 2014 to 2017, the growth in freelancing was three times faster than the growth of traditional work. Additionally, the Upwork report projects that a majority of the U.S. workforce will be freelancing by 2027. This estimate is based in part on the 47 percent of millennials who already freelance, the highest percentage of any generation. Oddly, the CWS finds that independent contractor work was rarer among young workers and most common for workers ages 45 to 64. These divergent data suggest that young workers are the most likely to use independent contractor work for supplemental income.

Like Upwork, the American Action Forum (AAF) found that the growth in alternative work arrangements far outpaced the growth of traditional work from 2002 to 2014.<sup>xvii</sup> Between 2010 and 2014, growth in independent contractors alone accounted for nearly 30 percent of all jobs added. The AAF report also showed that workers in alternative arrangements are more likely to be part-time workers, and the prevalence of part-time work among alternative arrangement workers has increased since 2002.

MBO Partners finds that the number of American workers who work independently irregularly or sporadically, but do so at least once a month, increased to nearly 13 million in 2017. This represents a 23 percent increase from 2016.<sup>xviii</sup> The report also finds that because of the strong job market, the number of people who work independently but would prefer traditional work fell to 24 percent, which is the lowest that the percentage has been in the study's seven-year history. Similar to the Upwork report, MBO projects that half of American workers will be independent or have worked independently within the next five years.

The Mercatus Center released a report in 2015 that measures the growth in alternative work arrangements by evaluating 1099-MISC forms issued by the Internal Revenue Service.<sup>xix</sup> 1099-MISC forms are issued to individuals who received between \$600 and \$20,000 from an entity outside the traditional employment relationship. The number of 1099-MISC forms issued by the IRS increased by 22 percent from 2000 to 2014. Over that time, the number of W-2 forms issued by the IRS to employees fell by 3.5 percent. A single worker can be issued multiple 1099-MISC forms, and there were 235 million W-2s issued in 2014 compared to 91 million 1099 MISCs, but the growth in this type of worker classification shows that companies and workers are taking advantage of lower transaction costs.

This data on 1099-MISC forms follows the conclusions of a 2016 paper by Lawrence Katz and Alan Krueger, which finds that 94 percent of the net U.S. job growth from 2005 to 2015 occurred in alternative work arrangements.<sup>xx</sup> The Katz and Krueger paper relies on a survey that resembles the CWS with a smaller sample size, and the authors find that 16 percent of workers were primarily independent contractors in 2015. This result is more than double the level from the May 2017 CWS.

The McKinsey Global Institute estimates that 20 percent to 30 percent of the working-age population in the United States and the EU-15 countries are engaged in some form of independent work.<sup>xxi</sup> This estimate is lower than the Federal Reserve's Enterprising and Informal Work Activity survey, which estimates that 36 percent of workers took part in informal paid work in 2015.<sup>xxii</sup> In its survey of around 8,000 U.S. and EU independent workers,

McKinsey finds that 70 percent of independent workers preferred their work arrangement and 56 percent of respondents use independent work to earn supplemental income.

A Treasury Department report evaluates tax return records from 2014 and finds that nearly 17 million Americans filed returns that showed the profitable operation of a nonfarm sole proprietorship, an increase of a third since 2001 levels.<sup>xxiii</sup> The report shows that essentially all the increase in self-employment came from a growing number of independent contractors, though some of the increase could be accounted for by misclassified employees.

An additional reason besides different definitions of who counts as an independent contractor that could explain the wide variation in the findings of the surveys and studies previously mentioned is that some survey respondents may not realize their worker classification status. For people who identify themselves as wage and salary workers, the CWS asks if last week they were working as “someone who obtains customers on their own to provide a product or service.”<sup>xxiv</sup>

People who work as Uber drivers, for example, could think that they do not obtain customers on their own because they rely on the application as an intermediary. Additionally, there have been administrative changes from the Department of Labor over how courts are supposed to interpret worker classification that could add to workers’ confusion.<sup>xxv</sup> These administrative changes are possible because the Fair Labor Standards Act uses a definition of employee that differs from most other federal statutes, including the National Labor Relations Act, the Equal Pay Act, and the Social Security Act.<sup>xxvi</sup>

## Conclusion

While conducting the CWS is a major undertaking, the data it provides can help policymakers better understand how work is changing. Rather than being a sporadic survey, BLS should work to release an update to the CWS every two years, as it did from 1995 to 2001. However, the CWS’s divergent findings on the prevalence of alternative work arrangements—especially for independent contractors—show that additional measures are needed to capture a complete picture of the changing American workforce.

Alternative work arrangements are desirable to many workers, especially when they are used for supplemental income. Failing to capture this reality through the CWS leads to the impression that independent work is stagnating, a conclusion that is in direct opposition to other reputable estimates and what is expected from economic theory.

I appreciate this committee’s continued interest in understanding how the American workforce is changing and how federal policy can facilitate independent work for those who desire it. Thank you again for the opportunity to testify. I look forward to answering any questions from the committee.

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