

Flexible Benefits for a Flexible Workforce: Legalizing Access to Portable Benefits for Independent Workers

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Subcommittee on Workforce Protections

Unlocking Opportunity: Allowing Independent Contractors to Access Benefits

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Good morning, Chairman Kiley and members of the Subcommittee on Workforce Protections. It is an honor to testify before you.

My name is Liya Palagashvili, and I am a labor economist at the Mercatus Center at George Mason University. I am also on the Data Users Advisory Committee for the US Bureau of Labor Statistics. I study the independent workforce and the evolving nature of work. My research on flexible benefits for independent workers has motivated state legislative reforms over the past year, and I would like to share some of those insights with you.

My testimony today focuses on legalizing independent contractors' access to fringe benefits. The three key themes are the following:

1. Regardless of worker classification policy debates, there will continue to be millions of independent contractors and self-employed workers whose lives would be enhanced if they had access to benefits.
2. States and localities are experimenting with various portable benefits models so that workers are not forced to choose between structured employment with benefits or flexible work without benefits.
3. Federal policy can provide a safe harbor for state and local experimentation with these portable benefits systems.

1. Enhancing the Lives of Independent Contractors

It is a rare chance when your research so closely connects to your personal life, so before I dive into the subject matter, I would like to share a brief story.

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In January 2020 my father lost his work. He had been a driver his whole life—even before coming to the United States. The US company he had been contracting with told him they are moving away from an independent-contractor model to an employment-based model.

My father was offered a position to become a full-time employee at the company. He turned it down, even though he didn't have another job opportunity in hand. He continued to remain without work until he found an opportunity to be an independent contractor again.

What my father's story illustrates is that regardless of worker-classification policies that may tip the scale in one direction or the other—such as the Department of Labor's recent independent-contractor rule or California's Assembly Bill 5 (AB5)—there will still be millions of US workers who will continue to engage in independent contracting or self-employed work just because they want to. Indeed, according to the Bureau of Labor Statistics, almost 80 percent of all independent contractors prefer their work arrangement over an employment arrangement, and fewer than 1 out of 10 would like to be employees.¹

For some, like my father, being a contractor rather than an employee gives them freedom to work on side projects and side businesses. For others, it is out of necessity—some workers have disabilities or life circumstances that hinder their participation in the labor market. And for the vast majority of independent contractors, especially those using app-based delivery and transportation platforms, being a contractor rather than an employee is simply about the opportunity to make side income to meet financial needs. In fact, according to IRS tax records, most independent contractors are already employed full time and contracting as a side hustle.²

So, the question before us is how to address the challenges confronting millions of independent contractors who will choose to remain self-employed regardless of the broader worker-classification policy debates.

2. How States Are Legalizing Access to Benefits for Independent Contractors

This is where portable, or flexible, benefits reforms can be monumental.

Many decades ago, tax incentives were created to encourage fringe benefits to be tied to traditional employment jobs, and labor laws were designed in a way that restricted the flow of benefits to non-traditional workers.³ Back then, this was not a big issue because most workers were traditional, W-2 employees. But now that the circumstances have changed, these laws are failing a large and growing sector of the workforce.

¹ US Bureau of Labor Statistics, "Contingent and Alternative Employment Arrangements—May 2017," news release no. USDL-18-0942, June 7, 2018.

² Brett Collins et al., "Is Gig Work Replacing Traditional Employment? Evidence from Two Decades of Tax Returns" (Working Paper, Internal Revenue Service, Washington, DC, March 25, 2019).

³ Liya Palagashvili, "Flexible Benefits for a Flexible Workforce: Unleashing Portable Benefits Solutions for Independent Workers and the Gig Economy" (Mercatus Policy Brief, Mercatus Center at George Mason University, Arlington, VA, February 3, 2023); Liya Palagashvili, "Barriers to Portable Benefits Solutions for Gig Workers" (Policy Paper No. 2020.010, The Center for Growth and Opportunity, Logan, UT, October 2020).

One of the key challenges today is that federal and state regulations restrict organizations from providing independent contractors with benefits precisely because these benefits conventionally have been tied to a traditional employer-employee relationship.

If an organization were to provide benefits to their independent contractors, it would risk the worker being reclassified as an employee.⁴ This means companies would have to pay fines for “misclassifying” workers. As the IRS states, one of the factors that determines whether a worker is an employee or independent contractor is whether an organization is providing benefits to that worker.⁵ If that worker is receiving benefits, that is a “checkmark” for the employee side.

This discourages companies and organizations from providing benefits to independent contractors. It also forces independent workers into an awkward position where they must choose a structured employment position with fringe benefits on the one hand, or self-employment or a flexible contracting job without fringe benefits on the other.

In other words, our current regulatory framework does not provide an option for workers to have access to both independent jobs and benefits.

That is why states are now beginning to experiment with various portable benefits models. Last year, Utah passed a bill that removes the presence of benefits as a factor in worker classification tests.⁶ That means if a company were to provide benefits to independent contractors in Utah, the presence of those benefits does not tip the scale on the question of whether the worker is an employee or an independent contractor.

Other states are exploring different variations of enabling access to portable benefits. Sometimes state solutions are like Utah’s bill, and other times states offer tax credits that can put independent contractors and employees on more equal footing. Yet another aspect of portable benefits is about allowing independent contractors to unite as a group to buy health insurance at group rates.

And, just last week, with the backing of Pennsylvania’s Governor, the platform company DoorDash launched a first-of-its-kind pilot portable benefits program: DoorDash will begin making monthly contributions into an individual’s flexible savings account managed by the benefits company Stride. Delivery drivers can use those funds toward retirement savings, paid time-off, or health insurance premiums.⁷

These are just a few ideas for how states are implementing reforms to help all workers—not just employees—better step into the future.

3. How Federal Policy Can Unleash Portable Benefits Reforms

There is an important role for federal policy to help legalize access to benefits for independent contractors. This past year, I co-led the Utah Flexible Benefits Working Group under the leadership of

⁵ “Type of Relationship,” Internal Revenue Service, last updated March 15, 2024, <https://www.irs.gov/businesses/small-businesses-self-employed/type-of-relationship>.

⁶ Utah S.B. 233 Portable Benefit Plan of 2023 (passed Mar. 23, 2023).

⁷ Natalie Lung, “DoorDash Launches Benefits Program for Pennsylvania Delivery Drivers,” *Bloomberg*, April 3, 2024.

Utah Senator John Johnson.⁸ One of the key takeaways was that the biggest barrier to flexible benefits implementation in Utah was fear that federal agencies such as the IRS and the Department of Labor would nevertheless use the presence of benefits for worker classification determinations. That discouraged companies from providing benefits to independent contractors in Utah regardless of the new state law.

Therefore, there is a need for federal policymakers to create a safe harbor so that providing any type of benefits to independent contractors does not trigger worker classification issues at the federal level. A policy would need to explicitly state that no federal agency can use the presence of benefits to independent contractors in worker classification determinations. This type of directive at the federal level would allow for continued growth of state and local experimentation with portable benefits systems.

This is just one example—there are other ways for federal policy to support creating a more equitable system that puts independent workers and employees on more equal footing. As I have discussed here, legalizing access to benefits for independent contractors is a small but necessary step that could (1) help unleash the flow of benefits to independent contractors and (2) allow states and localities to experiment to find the systems that works best for their citizens.

Conclusion

Self-employment and independent work are beneficial and desirable for many working Americans. We should embrace and welcome the new reality that many Americans choose and prefer these types of nontraditional work arrangements. At the same time, we must aim to fix the shortcomings that exist in these nontraditional work arrangements, namely, that workers do not have access to the same benefits afforded to traditional employees.

These limitations have led to policy battles across states and on the federal level because our current system continues to prioritize the immobility of benefits (e.g., healthcare being tied to one employer) in a world where worker preferences have shifted toward more choice and portability. Indeed, a survey found that 80 percent of self-employed respondents would like access to flexible or portable benefits—benefits that are not tied to a particular job or employer.⁹

To better meet the needs of the growing independent workforce, federal policymakers could take a simple and small step to legalize access to benefits for independent contractors by directing agencies not to use the presence of benefits in worker classification tests. Embracing innovative policy reforms will create a fairer system for all workers—both traditional employees and self-employed workers. Such reforms would not harm existing employees, but only enhance the livelihoods of independent contractors.

⁸ Liya Palagashvili and Caden Rosenbaum, “Findings and Recommendations of the Utah Flexible Benefits Working Group” (Policy Analysis, Libertas Institute, Lehi, Utah, February 21, 2024).

⁹ Tito Boeri et al., “Solo Self-Employment and Alternative Work Arrangements: A Cross-Country Perspective on the Changing Composition of Jobs,” *Journal of Economic Perspectives* 34, no. 1 (Winter 2020): 170–95.