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# The FTC's Foray Into Worker Classification Is Misguided and Unlawful

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When it comes to the FTC's comprehensive effort to reshape business in America, the agency's recent public efforts have largely focused on merger regulation, making its proceedings more accessible to the public and policing pandemic predators. Yet, in the background, the FTC has been quietly laying the foundation for an unprecedented attack on long-standing worker-classification norms, which could harm millions of Americans and thousands of small and large businesses that depend on independent contractors. Specifically, the FTC is preparing to unilaterally limit who qualifies as an independent contractor and prosecute violations under Section 5 of the FTC Act.

At present, the Department of Labor, National Labor Relations Board and U.S. Treasury (through the Internal Revenue Code) enforce employee classification. These agencies, pursuant to express statutory grants of authority, remedy misclassification through enforcement action. But according to labor and antitrust activists, including panelists at the FTC's "Workshop on Promoting Competition in Labor Markets," the current classification tests used by those other agencies inadequately protect workers. Rather than seeking to remedy this alleged "deficiency" before the labor agencies, activist groups have urged the FTC (an antitrust and consumer protection agency) to adopt its own, more restrictive, classification test and challenge "misclassification" as an unfair method of competition under Section 5 of the FTC Act, a broad statute that may, in principle, be used to stop all manner of anticompetitive business tactics.

It appears that certain FTC commissioners agree. Chair Lina Khan has spoken in favor of FTC enforcement in the labor sphere, and Commissioner Rebecca Slaughter endorsed aggressively challenging misclassification in an open letter to the Department of Labor. Of even greater concern, the FTC appears to be actively laying the foundation for regulating employee classification as an unfair method

(Courtesy photos)

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of competition. First, the FTC rescinded a 2015 policy statement which had committed the FTC to challenging a method of competition as unfair only if the business practice harmed consumer welfare. Then, the FTC created a rule-making group to "activate its unfair methods of competition authority" and adopted new procedures to streamline rule-making under Section 18 of the FTC Act.

The FTC should not pursue this course of action. Not only would regulating employee classification exceed the FTC's congressionally delegated authority, it would disrupt the balance Congress struck between consumer and labor welfare and likely violate substantive and procedural due process. Beyond that, it's simply bad policy.

At the "Labor Market Competition Workshop," panelists identified two procedural tools through which the FTC could regulate employee classification as an unfair method of competition: adjudication under Section 5 of the FTC Act and rule-making under Section 18 of the FTC Act. However, the FTC can only regulate classification through Section 5 adjudication or Section 18 rule-making if it can demonstrate that misclassification causes, or will likely cause,

substantial injury *to consumers*. As with all administrative agencies, the "[FTC] may exercise only the power granted to it by [Congress]." *FTC v. Nat'l Lead Co.*, 352 U.S. 419, 428 (1957). Under Section 5(a)(2) of the FTC Act, Congress has granted the FTC the power to enjoin economic entities from using unfair methods of competition and unfair or deceptive acts or practices. 15 U.S.C. § 45(a)(2). Likewise, under Section 18, the FTC may prescribe "rules which define with specificity acts and practices which are unfair or deceptive acts and practices." 15 U.S.C. § 57(a)(1)(b). The FTC has some authority to define unfair methods of competition and, when setting a definition, may consider general public policy objectives. *See FTC v. Indiana Fed'n of Dentists*, 476 U.S. 447 (1986). But this power is not infinite. Under Section 5(n), the FTC has "no authority" to declare an act or practice unlawful on the grounds that it is unfair unless it "causes or is likely to cause substantial injury to consumers which is … not outweighed by countervailing benefits to consumers or to competition." 15 U.S.C. § 45(n). Moreover, the FTC does not have statutory authority to issue rules concerning unfair methods of competition, which severely limits its ability to address through rulemaking any purported competitive advantage held by companies that partner with independent contractors.

Therefore, the FTC may only challenge misclassification as an unfair method of competition through its adjudicatory procedures if it can demonstrate misclassification harms consumer welfare. Yet, nobody at the conference was focused on consumer welfare when discussing classification issues, nor have labor and antitrust activists advanced a compelling consumer welfare justification. Nor is it likely that the FTC will be able to establish a consumer-welfare justification for regulating misclassification. For example, research shows that classification of app-based drivers as employees would increase the price consumers pay for rideshare services from 25.9% to 100% and food/grocery delivery services from 35.2% to 100%. This is consistent with basic economic theory; a profit-maximizing firm subject to increased variable costs (such as labor) will try to pass a portion of that cost to consumers. Consequently, if the FTC were to intervene, consumers would likely pay *higher* prices.

The reason for which the FTC and commentators have yet to adduce a credible consumer welfare justification for challenging employee misclassification underscores why it would be poor public policy for the FTC to regulate labor issues—there is often tension between the antitrust law and the labor laws. The purpose of the antitrust laws is to preserve competition, the "central nervous system of the economy" and thereby protect consumers from artificially high prices. *United States v. Socony-Vacuum Oil Co., Inc.*, 310 U.S. 150, 193 (1940). Labor laws, on the other hand, seek to protect workers from exploitation by bolstering workers' negotiating power through collective bargaining and providing prophylactic protections, such as workplace safety and wage protections. Consequently, labor laws and antitrust laws may find themselves at cross-purposes, with one seeking greater worker compensation while the other promotes lower consumer prices.

To balance the policy tension between competition and labor law, Congress designed a bifurcated regulatory framework in which labor and competition statutes are enforced by separate agencies. While the FTC enforces the Sherman, Clayton and FTC acts, the DOL, NLRB and other labor agencies enforce the Fair Labor Standards Act, the Occupational Safety and Health Act and other labor laws. Statutory exemptions and prophylactics mediate where these laws and policies conflict. If the FTC were to regulate employee classification, it would be inserting itself into multiple statutes at once, in a policy area in which it has no expertise, to enforce federal statutes already enforced by other agencies.

Additionally, intervention by the FTC into employee classification raises significant due process concerns. If the FTC adopts any legal standard other than those currently used by the DOL and NLRB, companies would be forced to comply with inconsistent standards of conduct. Further, under the FTC's civil enforcement procedures, judicial review is only available after the FTC Commission issues a final decision. Consequently, companies might be faced with a situation where they must either concede or withstand years of costly investigation and litigation without judicial review.

The express mandate other agencies have to regulate employee classification indicates that Congress never intended for the FTC to regulate employee classification. Given that the FTC has neither the expertise nor the authority to regulate classification, the FTC should not do so.

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