

Labour Law and Triangular Employment Growth

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A THESIS SUBMITTED TO THE FACULTY OF GRADUATE STUDIES
IN PARTIAL FULFILLMENT OF THE REQUIREMENTS
FOR THE DEGREE OF MASTER OF LAW
GRADUATE PROGRAM IN LAW,
YORK UNIVERSITY
TORONTO, ONTARIO

October, 2014

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Abstract

This thesis is concerned with understanding the relationship between labour law and triangular employment growth, and particularly in "staffing services" contexts. A review of alternative explanations for growth in triangular employment within three theoretical paradigm (neoclassical, institutionalist, and critical) illustrates the theoretical space for conceiving of a relationship between the particularities of labour law and triangular employment growth. To this end, the thesis develops the concept of a regulatory differential, or ways in which a legal regime may produce differential regulatory effects as between direct and triangular forms of employment. A typology of regulatory differentials is outlined. Further, a discussion of the relationship between these differentials and employer-status rules is provided, and it is suggested that the logic of the framework may helpfully inform analysis of triangular employment growth within a given jurisdiction, as well as comparative analysis of this phenomenon. The theoretical framework is then applied towards examining diverging growth rates in triangular employment as between Canada and the U.S. Legal analysis examining two key sub-fields of labour suggests that the presence (and expansion) of key regulatory differentials in the U.S., absent in Canada, may help explain the observed patterns of triangular employment growth in these countries.

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Introduction and Overview of Portfolio Thesis:

In addition to the brief introductory and concluding thoughts in this linking document, this portfolio thesis is essentially comprised of two separate manuscripts submitted to two academic peer-reviewed journals in the field of labour law. The first manuscript has been accepted for publication by the International Journal of Comparative Labour Law and Industrial Relations and is currently “in press”. The second manuscript has been accepted for publication with the Employee Rights and Employment Policy Journal. The most current versions of the manuscripts are included herein, with citations.

This thesis is concerned with understanding the phenomenon of triangular employment and its growth in recent decades. Growth in forms of triangular employment has contributed to increased precarity in the labour market, a well-documented trend in the modern economy.¹ More specifically, this thesis examines growth in triangular employment in the context of certain types of “staffing services” provided by an increasingly large and global staffing industry, to “user” firms. Triangular employment is understood here as the state in which either the service “provider” or “user” firm purports not to be the (or a) *de jure* “employer” of the worker, but the facts raise objective question or concern as to the allocation of *de jure* employer status.

The content, structure, and objectives of the two manuscripts are deeply intertwined, and constitute a coherent joint project that can be summarized as follows. The first manuscript examines the phenomenon of triangular employment growth largely in theoretical terms. It engages with alternative explanations for triangular employment growth that emerge from three different theoretical perspectives (neoclassical, institutionalist, and critical/Marxist). The first manuscript also puts forth certain challenges or caveats to some prevailing explanations for triangular employment growth based on claims about legitimate “efficiencies” being produced. Overall, the review of alternative theoretical explanations suggests significant space for understanding triangular employment growth as being normatively problematic. The theoretical analysis also supports the view that various characteristics of a given labour law regime are potentially important factors affecting triangular employment growth within a jurisdiction. The manuscript then provides a conceptual framework for considering this relationship based on the concept of a *regulatory differential*, or ways in which a legal regime produces different regulatory effects as between direct and triangular employment forms. A typology of various

¹ A. Bernhardt et al., (eds), *The Gloves Off Economy: Workplace Standards at the Bottom of the American Economy* (Champaign, IL: Labour and Employment Relations Association, 2008); Leah F. Vosko, ed., *Precarious Employment: Understanding Labour Market Insecurity in Canada*, (Kingston: Mc-Gill Queens University Press, 2005).

forms of regulatory differentials is developed, and the difference between *formal*, *contingent*, and *informal* regulatory differentials is discussed. Domestic employer status rules, and their role as additional, independent factors mediating the effects of underlying regulatory differentials upon triangular employment growth, are also discussed. It is suggested that this framework may helpfully inform analysis of domestic sources of triangular employment growth and/or serve as an improved lens for comparative analysis relating to triangular employment growth and/or its regulation.

The second manuscript applies the analytical framework developed in the first, towards understanding triangular employment growth in Canada and the U.S.. Data on growth rates in two key forms of staffing services embodying triangular employment – “temporary help” and “professional employer”² – services are reviewed. Using measures of the aggregate volume of these two services as an indicator of the volume of triangular employment, the data reveals that over the past few decades there has been significant growth in triangular employment in both countries, but much greater growth in the U.S.. Applying the analytical framework from the first manuscript, legal analysis is provided examining trends in relevant employer status rules and in underlying regulatory differentials, in both countries. Due to various constraints, analysis of regulatory differentials is limited to two key labour law sub-fields containing starkly different patterns of regulatory differentials in the two countries: the regulation of retirement plans and the regulation of employer-sponsored healthcare benefits. This legal analysis reveals the existence of significant formal and contingent regulatory differentials³ in each of these sub-fields in the U.S. that are lacking comparators in Canada, and that in each case, the timing of the emergence of regulatory differentials and/or their exacerbation by subsequent legal developments, was fairly consistent with historical patterns of aggregate triangular employment growth. Similarly, diverging developments in employer status rules in Canada and the U.S. are also consistent with these outcomes. Overall, the general consistency between the history of legal developments and patterns of triangular employment growth supports the relevance of the theoretical framework in understanding triangular employment growth in Canada and the U.S..

It is hoped that the theoretical framework developed herein, articulated in the first manuscript and applied in the second, helps further our understanding of triangular employment growth and provides a helpful frame for comparative analysis in this area. Triangular employment growth continues to

² As discussed in this paper, variants of these services were historically sometimes referred to as “employee leasing” services.

³ As argued in the paper, in the case of these two sub-fields, the particular regulatory differentials here seem capable of generating gains from triangular employment that are concrete, measurable, and monetary.

undermine the efficacy of labour law, so understanding the relationship between it and the particularities of labour law remains an important project. As discussed in the concluding section of the second manuscript, in the broader U.S. institutional context, triangular employment may have also served an additional role of assisting policy makers in preserving regressive policy outcomes in the pension and healthcare sub-fields. Future studies may similarly seek to probe the relations between triangular employment growth, labour law, and other aspects of social welfare.

Finally, it should be noted that the Canada-U.S. comparative analysis here was limited to two key sub-fields of law, and analysis could be extended to additional sub-fields. Future research may carry this forward, for additional insight. Finally, it is also suggested that future research probing the nature and consequences of triangular employment generated particularly by professional employer services is important, given the tremendous growth in these arrangements and the lack of research examining this phenomenon to date.

Paper # 1: Timothy J. Bartkiw, “Labour Law and Triangular Employment Growth: A Theory of Regulatory Differentials”, *International Journal of Comparative Labour Law and Industrial Relations*, Vol. 30, Issue 4 (In Press).

I. Introduction

Triangular employment arrangements have become increasingly prevalent in many countries in recent decades.¹ Various models of triangular employment exist in practice, under numerous labels, partly as a result of a proliferation in the range of “services” provided by an increasingly globalized “staffing” industry. Triangular employment growth has been widespread, yet also quite uneven, across numerous jurisdictions.²

This paper seeks to contribute to our understanding of the roots of triangular employment, and its comparatively uneven expansion, in the following ways. Part II of the paper probes the concept of triangular employment, towards clarifying its meaning and recognition, particularly in staffing service contexts. Part III provides a review of how three alternative theoretical perspectives (Neoclassical, Institutional, and Critical) provide competing understandings of triangular employment and explanations for its growth. Building on these insights, Part IV of

¹ Donald Storrie, *Temporary Agency Work in the European Union* (European Foundation for the Improvement of Living and Working Conditions, Luxembourg: Office for the Publications of the European Communities, 2002); Jamie Peck and Nik Theodore, “Flexible Recession: The Temporary Staffing Industry and Mediated Work in the United States”, 31(2) *Cambridge Journal of Economics* 171. (2007); Jamie Peck and Nik Theodore, *Temped Out?* “Industry Rhetoric, Labour Regulation, and Economic Restructuring in the Temporary Staffing Business”, 23(2) *Economic and Industrial Democracy* 143 (May 2002); Jamie Peck, Nik Theodore and Kevin Ward, “Constructing Markets for Temporary Labour: Employment Liberalization and the Internationalization of the Staffing Industry”, *Global Networks* 5, 1 (2005), 3-26. Leah Vosko, *Temporary Work: The Gendered Rise of a precarious Employment Relationship* (Toronto: U of T Press, 2000); Timothy J. Bartkiw, “Baby Steps? Towards the Regulation of Temporary Help Agency Employment in Canada”, 31(1) *Comparative Labor Law and Policy Journal* 163 (Fall 2009); and Britton Lombardi and Yukako Ono, “Professional Employer Organizations: What are they, who uses them, and why should we care?”, *Economic Perspectives* (4th quarter, 2008); Shelley Wallach, “Temporary? Agency Workers in Israel”, *The International Journal of Comparative Labour Law and Industrial Relations*, vol. 24/3, 423-44); Stefan van Eck, “Employment Agencies: International Norms and Developments in South Africa”, *The International Journal of Comparative Labour law and Industrial Relations* 28, no. 1 (2012): 29-44;); L. Mitlacher, “The Role of Temporary Agency Work in Different Industrial Relations Systems — a Comparison between Germany and the USA,” 45 *British Journal of Industrial Relations*, 581 (2007).

² Peck, Theodore, and Ward, *supra* note 1; Storrie, *supra*, note 1.

the paper then addresses the question of the potential relationship between the particularities of labour law and triangular employment growth. The paper provides a conceptual framework for considering this question, based on the concept of “regulatory differentials”, or ways in which a legal regime produces different regulatory effects across direct and triangular forms of employment. A typology of various forms of regulatory differentials is also provided. Part V of the paper provides some concluding thoughts, suggesting that the framework developed may helpfully inform analysis of domestic sources of triangular employment growth, and may be an improved lens for comparative analysis of this sort.

II. What is Triangular Employment?

In a 2006 ILO report, triangular employment arrangements are summarized as comprising two possible sets of contractual relationships: 1) contracts for the performance of work and services, and 2) contracts for the supply of labour services.³ In scenario 1, a so-called “provider” organization contracts with a “third party” organization, referred to as the “user”, to produce and supply some form of work or service. The provider then uses its own equipment and/or personnel to supply this work or service to the user, for use within the user’s production process. In scenario 2, the “supply of labour services” scenario, the commodity supplied under contract by the “provider” is ostensibly “labour” itself, or in other words, work performed by personnel ostensibly “employed” by the provider. In distinguishing the two forms, the classical distinction between “labour” and “labour power” is informative. In this view, organizations actually purchase labour power, which must then be managed within a *labour process*, towards the production of some commodity. Thus, in scenario 1, the provider firm manages the worker within its own labour process, and subsequently sells a commodity to the user firm. In scenario 2, the ultimate utilization of the underlying labour power occurs only within the user firm’s labour process.

Despite the importance of historical trends in “subcontracting” arrangements, this paper focuses on triangular relations found in scenario 2. Here, the user is a party to a commercial contract with the provider, and the user lacks any ostensible/formal employment relationship

³ Report V(1) of the 95th Session of the international Labour Conference, p. 42.

with the worker. For the user, this arrangement serves as a *substitute* for directly “employing” workers. Given forms of triangularity in practice, the term “labour supply” may imply an unnecessary constraint to the definition, since certain otherwise “triangular” relations, for our purposes, may not include any concrete “dispatch” of workers but involve a range of other services.⁴

According to the ILO, triangular employment relationships raise policy concern insofar as they represent either “disguised employment” or “objectively ambiguous employment.”⁵ In the latter case, there may actually be no intention to alter the appearance of the underlying relationship, but the facts of the relationship raise serious questions about the proper allocation of *de jure* employer status and ensuing rights and responsibilities.

The determination and allocation of *de jure* employer status is a function reserved to relevant local authorities of various sorts, empowered to determine the existence of employment relationships as a part of the regulatory function they perform. Local “employer-status rules” in statute, caselaw, and/or practices, institutionalize the concept of “employer” (and/or “employee”, “employment” etc.), and vary across jurisdictions. Most jurisdictions adhere to the “primacy of fact”, meaning that the facts of the relationship, not the label assigned by the parties, is determinative. Overall then, in triangular employment, either the provider or user purports *not* to be the (or a)⁶ *de jure* employer of the worker, but the facts raise some objective question as to the allocation of *de jure* employer status.⁷

The various staffing industry services, or service “bundles”, may be differentiated in terms of both a *qualitative* and *temporal* dimension. In terms of the former, there are different

⁴ The staffing industry provides a diverse bundle of services referred to alternatively as “staffing”, “personnel”, “employment”, “human resources”, or “human capital” services. The American Staffing Association website outlines following service categories: direct placement services; human resources consulting; long term and contract help; managed service provider; managed services; outplacement; payrolling; professional employer organization or employee leasing; recruitment process outsourcing; retained search services; temporary help; temporary to hire; vendor management systems. See <https://americanstaffing.net/commerce/memberJoin.cfm>.

⁵ International Labour Conference, 91st Session, *Report V: The Scope of the Employment Relationship*, 2003, pp. 24-25.

⁶ In other words, under triangular employment, one party may purport not to be the sole employer, nor one of the multiple employers of the worker.

⁷ Importantly, in triangular employment all the parties typically acknowledge that there *is a de jure* “employment” relationship in place.

functions provided under different service bundles. For example, in North America, while employee “screening” and “recruitment” functions are generally included in the “temporary help” service bundle, these functions are less likely included in so-called “employee leasing” or “professional employer” service bundles. Specific services may either supplement or displace functions performed by the user. Service bundles vary in the intensity of this substitution. Certainly, not all staffing services should be understood as generating triangular employment, as many such services would have little impact on the logic of *de jure* employer status. Typically, in order to raise uncertainty about *de jure* employer status, a non-negligible substitution towards staffing services would be required. Secondly, there are important *temporal* distinctions between different staffing service bundles. Although terminology varies, examples of staffing services embodying an important short term *temporal* component include: “day labour” (very short term), “temporary help” (short to medium term), and “temp to perm” (short to medium term). Other services such as “employee leasing”, or “professional employer services” are generally conceived as being non-temporary, or for an indeterminate time period.⁸ In the U.S., there has recently been a tremendous expansion in the use of these explicitly non-temporary triangular relations, particularly involving organizations self-identified as “Professional Employer Organizations” (“PEOs”).⁹ Indeed, the National Association of Professional Employer Organizations (“NAPEO”), openly embraces triangular employment, publicly claiming the ambiguous concept of “co-employment” lies at the heart of its members’ services.¹⁰ Analytical focus emphasizing the qualitatively *triangular* nature of staffing

⁸ See the discussion in Edward A. Lenz, *Co-Employment: Employer Liability Issues In Third-Party Staffing Arrangements*, 7TH ED. (Alexandria, VA: American Staffing Association, 2011). As Lenz points out, the term “employee leasing” is sometimes used as a generic term to refer to all forms of staffing services. However, it is more often (and here) understood as an intricate human resource outsourcing arrangement that purports to transfer employer status to the employee leasing firm, increasingly referred to as “professional employer organizations”.

⁹ Lombardi and Ono, *supra*, note 1.

¹⁰ “Co-employment” is a term created by the PEO industry in the U.S., it is not an independent juridical category, and thus not the same in the U.S. as the concepts of “joint employer” or “single employer” under common law. *De jure* employer status of firms providing PEO services would still generally be determined by application of common law employer status tests and the primacy of fact. As well, the industry itself does not seemingly define “co-employment” as being based on a single precise arrangement.. Rather, co-employment is established by contract between a PEO and a client, and the contract purports to allocate various human resources related functions and responsibilities across the parties. See NAPEO website description of co-employment at <http://www.napeo.org/peoindustry/coemployers.cfm>. Although the use of professional employer service

arrangements, abstracting away from temporal differences, is necessary and feasible. A key question is what causes/consequences underlay growth in those qualitative types of services generating triangular employment, regardless of temporality. In this vein, some academic analysis argues that insufficient attention has been paid to the problematic of the triangular dimension of temporary help services.¹¹ Abstraction of this sort, emphasizing triangularity *per se*, underpins the analysis in this paper, as we turn to examine competing theoretical conceptualizations of the underlying roots of triangular employment growth.

III. Triangular Employment Growth: Alternative Theoretical Explanations

Academic literature has provided a range of explanations for growth in triangular employment, in its particular forms. While some suggest a desire on the part of employers to “avoid” the effects of labour law/policy, others emphasize “legitimate” purposes. This paper adopts the simple normative assumption that where status quo labour policy or the degree of social protection is undermined by triangular employment, this is a *prima facie* problem.

Explanations of triangular employment growth based on the pursuit of “legitimate” purposes emerge from explanations for growth in related staffing services themselves. These explanations are rooted in neoclassical economic analysis, particularly the “theory of the firm.”¹² Storrie provides a helpful summary of such benefits potentially generated by *temporary help services*:¹³

- a) *Economies of scale and an improved “division of labour”* in the provision of certain functions may be captured, where a staffing firm carries out functions across multiple

arrangements would not necessarily alter *de jure* employer status in every circumstance, arguably a significant proportion of PEO arrangements would raise a serious question as to *de jure* employer status. This is heightened by the fact that there is somewhat of an unclear definition of the PEO service bundle in the market, with some firms offering “co-employment” services as part of a continuum of related employment services. See for example the list of employment services offered by the firm XCELHR listed at <http://www.xcelhr.com/BundledServices/ServiceGrid.aspx>.

¹¹ See for example Leah Vosko, “A New Approach to Regulating Temporary Agency Work in Ontario or Back to the Future?,” 65(4) *Relations Industrielles* 632 (2010).

¹² Frank Knight, *Risk, Uncertainty And Profit* (NY: Cosmo Classics, 1921).

¹³ Storrie, *supra*, note 1, at 33-35. See also Steven Willborn, “Leased Workers: Vulnerability and the Need for Special Legislation”, 19 *Comparative Labor law and Policy Journal* 85, (1997) and L.I. Smirnykh, *Labour Leasing: Economic Theory, EU and Russia Experience* (Moscow: Russian-European Centre for Economic Policy, 2005).

firms. Examples include improved recruitment and screening functions, and regulatory compliance capacity.¹⁴ Cost/risk pooling creates efficiencies in the provision of insurance-like benefits relating to health, welfare, injury compensation, and/or retirement.¹⁵

- b) *Diversification of employment risk*. This may be conceived as being essentially a specific example of the economies of scale benefit in (a) above. Firms face both firm-specific and market risks when hiring workers. Staffing firms may face lower risks, given their employment portfolios across multiple firms, of investing in employment.
- c) *Increased “flexibility”* in two main forms. “Numerical” flexibility refers to firms’ ability to adjust the number of workers utilized quickly. “Functional” flexibility refers to the ability to adjust the configuration of skills available to the firm over time.¹⁶
- d) *“Matching” improvements*: Through short term placements, the worker and user may exchange information prior to committing to a lengthier employment relationship.¹⁷

While there remains significant space for normative concerns about triangular employment despite these alleged benefits, there are also several points to consider in interpreting these claims. First, it is important to remember that these claims are raised primarily in relation to one specific variant of triangularity, namely temporary help services. However, much of the potential underlying economic efficiency produced by temporary help services is rooted in its temporal dimension, and not in its triangularity. This is the case for both notions of “flexibility” described in (c) above as well as for the potential “matching” efficiencies referred to in (d), both of which are commonly invoked in the literature and policy debates. These benefits relate to a client firm’s ability to adjust either the numerical quantity, or qualitative nature, of the labour power it requires *over time*. Flexibility is, in an ultimate sense, embedded in the increased capacity for temporal adjustment, and the logical necessity of allowing triangular

¹⁴ See Gregory Hammond, “Flexible Staffing Trends and Legal Issues in the Emerging Workplace”, 10 *The Labor Lawyer* 161 (1994). .

¹⁵ Storrie, *supra*, note 1; and Willborn, *supra*, note 33. In the USA, the National Association of Professional Employer Organizations (“NAPEO”) cites these sorts of benefits flowing from its services. See list of “frequently asked questions” at NAPEO website at <http://www.napeo.org/peindustry/faq.cfm>

¹⁶ Storrie, *supra*, note 1.

¹⁷ Storrie, *supra*, note 1, at 34.

employment to enable such flexibility gains, does not automatically or universally flow, and remains a separate question for further analysis. Again, since triangular employment is in some cases explicitly non-temporary, triangularity *per se* cannot seemingly be justified by reference to these conceptions of “flexibility,” and its justification must stand primarily on other grounds.

At a deeper theoretical level, in considering efficiency claims, it is crucial to take seriously the precise *nature* of the service itself, in an ontological sense, embodied in such analysis. That is, analysis must carefully isolate the actually-existing or “concrete” staffing service provided, *from the law’s response* to it, if any, to identify the efficiency. Here, it is possible that in certain contexts, the imposition of *de jure* employer status may be (or appear to be) *legally* - as opposed to *concretely* – required, in order for the staffing service to produce the efficiency in question.¹⁸ In such contexts, we are dealing with the product of prior policy choices and existing legal arrangements, which are *adjustable constructions*. Arguably, a true “efficiency” ought to be traceable to an underlying quality of the service itself, without entirely depending upon prior policy choices or legal consequences of the arrangement for its existence. Relatedly, the question of how *de jure* employer status is determined and the consequences of these rules under different staffing service arrangements, should be conceived as occupying a separate space, not implicated in (or constituting) the alleged efficiency produced by a given staffing service. Any claims about efficiency gains that necessarily depend upon either the maintenance of prior legal/policy choices, and/or that assume a specific accommodation of the law to the service arrangement, are thus of a much weaker, or “second-order” nature, since these additional constraints on socially-protective policy choices that these alleged efficiencies require for their realization must be taken into account.¹⁹

¹⁸ A recent publication by NAPEO points out that in the U.S. legal context, in order for PEO firms to provide many of the core services they provide (providing workers compensation insurance; sponsoring health insurance plans; remitting income and unemployment taxes) they are legally *required* to be an “employer” in law. See Diane Stanton, Rufus Wolff, and William J. Schilling, “Employer Status and the PEO Relationship,” 6 *NAPEO Legal Review* 1 (2008).

¹⁹ Theron makes an intuitively similar argument in the much more specific context of discussing the consequences of the “fiction” enshrined in South African legislation of the temporary employment service as the *de jure* employer. While he admits possible theoretical support for some benefits of temporary help services generally, noting for example that some workers may prefer temporary work, Theron grasps the significant leap in logic, stating “there is no apparent gain for them [those who prefer temporary work] in designating the TES as

This also raises the question of the proper counterfactual to use in analyzing efficiency claims. Willborn recommends considering how the workers would be treated, *ceteris paribus*, in the absence of the triangular arrangement.²⁰ However, this suggests that in the counter-factual scenario employed, the larger status quo context is held constant. This is a rather limited approach, and a more complete analysis requires consideration of potential alternative legal/institutional arrangements. For example, in a separate article of mine (forthcoming), examining triangular employment growth in the U.S. and Canada, the potential for certain services to create economies of scale for U.S. client firms in health insurance provision is accepted, given the specific background institutional context. However, the market for these services is rooted in various pre-existing policy choices in the regulation of employer-sponsored health care in the U.S., and the logic of that policy framework underpins the potentiality of economies of scale from certain staffing services. Employing a more complete counterfactual analysis, one should consider whether these efficiencies might be produced under alternative organizational forms and/or contracting arrangements; whether existing law privileges the use of triangular employment; and whether efficiency claims assume particular legal responses/consequences.²¹ An example of this kind of analysis is found in Freeman and Gonos' exploration of the case for regulating temporary help services, in which they compare the regulation of temporary help with that of union hiring halls, a rival institution.²²

Further, alleged benefits emerging from neoclassical theory may well be challenged on the same grounds that the neoclassical model is critiqued in general, such as the institutionalist

employer". See Jan Theron, "Intermediary or Employer? Labour Brokers and the Triangular Employment Relationship," 26 *Indus. L.J.* 618 (2005).

²⁰ Willborn, *Supra*, note 33.

²¹ For example, some firms in the U.S. staffing industry are known as Administrative Services Organizations ("ASO"s). These firms provide many of the same underlying services provided by Professional Employer Organizations ("PEO"s), by contract. The key distinction between PEO and ASO service bundles however, seems to be that under ASO contracting arrangements, the parties do not explicitly purport to contract for "co-employment". In other words, they don't attempt to claim an alteration in employer status of the underlying workers as being a component of the service bundle. The existence of these alternative business practices in the U.S. context clearly suggests that the *legal* effects of PEO arrangements form a significant independent benefit in itself for U.S. client firms preferring these services over ASO services.

²² Harris Freeman and George Gonos, "Taming the Employment Sharks: The Case for Regulating Profit-Driven Labor Market intermediaries in High Mobility Labor Markets", 13 *Employee Rights and Employment Policy Journal* 285 (2009).

critique of that paradigm's dependence upon micro-level assumptions of (*inter alia*) a "perfect" degree of information, mobility and rationality. Institutional intuition, with its emphasis on so-called "market failures" may be understood as forming the underlying intuition for some existing critiques of triangular employment, and provides theoretical support for alternative, and less benign, explanations for its expansion.²³ For example, triangular employment relations arguably *exacerbate* the degree of informational asymmetries in employment, as the true state of authority, capacity, and responsibility allocation between the two "employing" entities becomes increasingly unclear to the worker. These additional "transactions costs" imposed upon workers in their initial/ongoing "bargaining" with their "employer(s)", erode worker bargaining power and capacity to *enforce* bargains.²⁴ Likewise, information loss/costs may reduce worker awareness of their extra-contractual legal entitlements within the triangular context. In a similar vein, the theoretical category of "unfree labour" increasingly applied to temporary agency work (particularly as this overlaps with migration) highlights the importance of contractually-imposed mobility restrictions in triangular employment²⁵

Further conceptualizations of triangular employment as a labour policy "problem" exist, drawn from critical/Marxist (generically "critical") literature. Although critical theory shares emphasis with institutionalism on what the latter refers to generically as "information", critical theory provides other insights. Rooted in Marxist conceptions of the "labour process" there is a deeper/broader rejection of the panoply of assumptions underlying neoclassical analysis than institutionalism. The latter, it has been argued, commonly only penetrates a subset, or what has been described as the "protective belt", of such assumptions (re information and

²³ The definitional boundary between the neoclassical and institutionalist paradigms are somewhat unclear in that some ostensibly neoclassical analysis at times seeks to incorporate institutionalist critique into its domain. Examples are neoclassical references to "market failure", and so-called neoclassical analysis based on the work of Coase, which has elsewhere been cited as supporting the impossibility of fundamental tenets of neoclassical analysis. See Bruce Kaufman, "The Impossibility of a Perfectly Competitive Labour Market," 31 *Cambridge Journal Of Economics* 775.

²⁴ Here, we could conceive of the bargain as including legislated terms, since exacerbated informational problems could extend to these. Of course, the impact of these various market failures or transactions costs may also affect the ability of workers to engage in collective action, with these capacities being mediated by the applicable legal framework for collective labour relations in the given jurisdiction.

²⁵ Judy Fudge, and Kendra Strauss, *Temporary Work, Agencies, and Unfree Labour: Insecurity in the New World of Work* (New York: Routledge, 2014).

competition) while typically still adhering to certain “core” behavioural axioms (E.g. exogenous, complete, fully ranked individual “preferences”) inherent in neoclassical analysis.²⁶

In Marxist analysis, the labour process is the ultimate source of social exploitation and wealth production, since it is only here that *surplus value* is produced. Further, the exploitive tendencies of capitalist social relations may be reproduced partly because of their illusory form. In particular the generalized “commodity form” of production, and the associated false conception of labour (as opposed to “labour power”) as being a commodity, results in a corrosive effect upon social consciousness, or what Marx famously refers to as the commodity “fetish”, concealing from workers’ view the true nature of social relations around labour.²⁷ Additional dynamics within capitalism contribute to its ongoing reproduction, and the continued subordination of workers. These include the ability of the capitalist class to preserve (or expand) worker commodification, and the essential, continuous presence of a reserve army of labour.²⁸

Extending Marx’s analysis into advanced capitalism in the modern era, critical theorists, many following Gramsci, have examined processes of “hegemony”, and the construction of worker “consent” to capitalist social relations.²⁹ While the labour process remains understood as objectively exploitive, critical theory emphasizes reliance upon other mechanisms, aside from raw coercive force, in securing workers’ subjective consent. Burawoy, for example, emphasizes the importance of what he calls the “mystification” characterizing advanced capitalism, and particularly obfuscation within the labour process *concealing* the appropriation of surplus value.³⁰

²⁶ Thrainn Eggertson, *Economic Behaviour And Institutions* (New York: Cambridge University Press, 1990).

²⁷ See Karl Marx, *Capital, Volume 1* (1867), chapters 1-3.

²⁸ For a summary of core elements of Marxist political economy’s conception of capitalist employment relations, see Eric Tucker, “Renorming Labour Law: Can We Escape Labour Law’s Recurring Regulatory Dilemmas?” *Industrial Law Journal*, Vol. 39, No. 2, June 2010.

²⁹ See Antonio Gramsci, *Selections From The Prison Notebooks*, (New York: International, 1971).

³⁰ Michael Burawoy, *Manufacturing Consent: Changes In The Labor Process Under Monopoly Capitalism* (Chicago: University of Chicago Press, 1979); Michael Burawoy, “The Roots of Domination: Beyond Bourdieu and Gramsci”, *Sociology* 46(2) 187-206 (2012). Although Burawoy criticizes it as operating at “too deep” a level and as being too universalistic, a similar conception is found in Bourdieu’s theory of “misrecognition.” See Pierre Bourdieu, *Pascalian Meditations*. (Stanford, CA: Stanford University Press, 2000).

In this vein, critical scholarship emphasizes the role of staffing arrangements in supporting obfuscation in the labour process. Gonos argues that the business model of the modern temporary help industry carries the historical and misleading conception that employment agencies' fees are "employer paid" to a heightened level.³¹ Rather, modern temporary help arrangements resurrect the historically banned practice of "fee splitting," where employment agencies charged workers fees for jobs and shared these profits with clients to induce a large-scale "churning" of workers. The modern U.S. temporary help formula, with the agency designated the "employer", provides a secure basis for a long-term flow of fees, in the form of a wage "mark-up" charged throughout the entire "placement".³² Misleading conceptions of the service provided by the agency, and the ability to hide the true "markup", makes the "service" an instrument in intensifying surplus value extraction.³³

Extending this critical theoretical approach, Smith's analysis of temporary employment relations in the U.S. illustrates how this process of concealment goes hand in hand with the deepening of worker (and by extension working class) division and disorganization, and related effects upon workers' own consciousness, identities and aspirations.³⁴ Although she is specifically examining "temporary help" in the U.S., her analysis shows how triangular relations may be constructed that, on the one hand allow for a sufficiently deep and seamless integration of "temporary workers" (read: workers under triangular relations) into processes of production and self-governance in the workplace, while on the other destabilize workers understandings of

³¹ George Gonos, "Never a Fee! The Miracle of Postmodern Temporary Help and Staffing Agency," *Working USA: The Journal of Labor and Society* Vol. 4, No.3 (Winter, 2000-2001), 9-36.

³² *Ibid*; George Gonos, "Fee-Splitting Revisited: Concealing Surplus Value in the Temporary Employment Relationship", *Politics and Society*, Vol. 29, No.4, Dec 2001, 589-611.

³³ Or in even more explicitly Marxist terms, triangular employment may be a special commodity whose particular "use value" is the ability to increase the rate of surplus value extraction in the labour process. Given the cost of the agency markup to the client firm, this logic implicitly necessitates a decline in wages, or some other non-wage compensation, received by the worker. Gonos points to evidence of both wage loss under temporary staffing arrangements, and to the increasingly normal practice of workers in these arrangements receiving no (or fewer) health/welfare benefits in their employment compensation. See Lawrence F. Katz and Alan B. Krueger, "The High Pressure U.S. Labor Market of the 1990's," *Working Paper No. 416, Princeton University Industrial Relations Section, 1999, 43*.

³⁴ Vicki Smith, "The Fractured World of the Temporary Worker: Power, Participation, and Fragmentation in the Contemporary Workplace", *Social Problems*, Vol. 35 (Nov., 1998), pp. 411-430.

their employment status, limit and constrain their expectations, and distort their perceptions of who possesses power or shares in their marginalized status.³⁵

In critical theory then, triangularity generates unique behavioural effects leading to worker (dis)empowerment at the level of the firm/organization, which may constitute an underlying incentive/benefit to user firms. At a broader level, these effects also factor into the logics of class construction, consciousness and solidarity, and into the balance of class forces. These effects feed into prevailing ideological constructs and understandings, reciprocally affecting micro level employment relations.

This review of some of the alternative theoretical perspectives on triangular employment suggests that there is significant space and grounds for accepting the claim that triangular employment growth represents a policy “problem”, regardless of whether we accept the potential for certain efficiencies, in certain contexts. It remains conceivable that a large part of the benefit of some services flows not necessarily from any fundamental or concrete efficiency, but rather flows from favorable legal consequences of the triangular employment relationship that the staffing service constructs or necessitates, or from ensuing shifts in relational power. In the real world of imperfect legal/policy instruments, the possibility of benefits flowing from what I refer to as a *regulatory differential* entering into the mix of benefits facing the user firm, is quite feasible. Existing literature on certain staffing services, like temporary help, points to such effects³⁶ suggesting that user firms gain such benefits, at least as *byproducts* from the service. This reinforces the importance of more carefully examining the relationship between triangular employment growth and the particularities of labour law in a given jurisdiction, the unpacking of which is the subject of the next section.

IV. “Regulatory Differentials” Across Alternative Employment Forms

As discussed above, the claim that triangular employment relations may undermine the function of labour/employment law is not a new one. Much analysis implies that triangular

³⁵ *Ibid.*

³⁶ See for example the summaries of labour policy problems arising from temporary help agency employment provided in Vosko, *Temporary Work*, *supra*, note 1; Peck and Theodore, *Temped Out?*, *supra*, note 1; Bartkiw, *Baby Steps?*, *supra*, note 1.

employment enables firms to “avoid” or “escape” the law or its effects, and it is also suggested that as the burden of employment regulation grows, firms increasingly use triangular relations in response.³⁷ But arguably, our understanding of how triangular employment enables avoidance is incomplete. Indeed, in some accounts, the process of “shifting” employer status onto a 3rd party staffing firm seems to be improperly understood as being *synonymous* with regulatory avoidance.

Here the U.S. case is informative. One of the most important explanations for the historical expansion in temporary help services in the U.S., and how this process is rooted in struggles over legal regulation, is found in the work of Gonos.³⁸ Gonos traces how temporary help firms were successful in a lengthy lobbying campaign throughout the 1960’s and 1970’s over constructing its status as a new type of labour market intermediary. On the one hand, the industry was able to distinguish itself from the historical legal category of “employment agency”, largely winning for itself exemptions from pre-existing regulations on these sorts of firms. Moreover, the industry gradually also succeeded in obtaining recognition of its member firms as the *de jure* “employers” of the workers they assign to client users for temporary work. As an early step, the industry convinced levels of government to accept unemployment insurance and payroll tax remittances concerning “its” employees, establishing the staffing firm as the *de jure* employer for such purposes. The industry was then successful in gradually extending the domain within which its status as *de jure* employer was recognized over time. Gonos argues that user firms’ increasing ability to count on the staffing firm’s *de jure* employer status became a crucial factor in stimulating demand for these services. He argues that this “temporary help formula” constituted a major deregulatory shift in the U.S. beginning in the 1970’s.

While Gonos’ contribution is important, his argument about deregulation ends with the construction of the temporary help formula and the shift in *de jure* employer status to the staffing firm. The more specific details about how this shift in *de jure* employer status achieved

³⁷ David Autor, “Outsourcing at Will: Unjust Dismissal Doctrine and the Growth of Temporary Help Employment,” 23 *Journal Of Labor Economics* 1 (2003).

³⁸ See Gonos, “The Contest over ‘Employer’ Status in the Postwar United States: The Case of Temporary Help Firms,” 31 *Law And Society Review* 81 (1997).

such a deep deregulatory effect, and the scope or limits of this shift, are not articulated. Some subsequent literature cites Gonos' work as seemingly confirming the benefit of regulatory avoidance via the shift in *de jure* employer status.³⁹ The implicit assumption that a shift in *de jure* employer status is synonymous with regulatory avoidance also seems to underlay some comparative analysis of triangular growth across jurisdictions,⁴⁰ and the theory that the greater the regulatory burden imposed by labour law in a given jurisdiction, the greater will be the use of triangular employment, as firms increasingly seek to avoid regulatory burden.⁴¹ Again, neither the precise mechanisms nor the limits of this avoidance are clear.

In reality, the victory of the U.S. temporary help industry in achieving *de jure* employer status, and thus regulatory avoidance, remains somewhat incomplete and contested. Employer status in these contexts is generally determined on an *ad hoc* basis. Legal tests for determining the *de jure* employer continue to be based on the primacy of fact, and common law tests in the U.S. have in most recent years depended substantially upon indicators of "control".⁴² Thus, in contexts where control over workers assigned by a staffing firm is severely lacking, *de jure* employer status may be reserved to the user.⁴³ Further, *de jure* employer status is not necessarily robust across policy sub-fields or regimes, meaning that status may be allocated differently by adjudicators in different regimes or contexts. For example, the capture of *de jure* employer status for staffing firms under payroll tax rules does not guarantee a similar outcome for the purposes of minimum employment standards, collective labour relations, or workers compensation regimes, since variation may remain among the application of the common law tests across adjudicators within specific subfields.⁴⁴

³⁹ See for example the references to Gonos' work in Peck and Theodore, *Temped Out*, *supra*, note 1.

⁴⁰ Mitlacher, *supra*, note 1.

⁴¹ See Autor, *supra*, note 37.

⁴² *Nationwide Mutual Insurance Company v. Robert T. Darden* 503 US 318; 112 Sct. 1344 (1992). ("Darden").

⁴³ This is not to say that a user and supplier firm might not be able to operate taking the contrary *position* in practice. This might be the case because of lack of enforcement, informational deficiencies, and other factors affecting the relative power of the parties under triangular employment. I refer to these factors collectively as "informal regulatory differentials" in my subsequent discussion, *infra*.

⁴⁴ For example, one remaining distinction is that adjudicators under the Fair Labor Standards Act, which primarily addresses issues of minimum wage, and hours of work restrictions, continue to apply the concept of "dependency". See subsequent discussion of employer status case law in Part VI. In terms of tax law, although the common law employer test has been codified, for certain purposes, such as liability for withholding, reporting and

Moreover, even where *de jure* employer status does shift to the staffing firm, avoidance of regulatory effect is neither obvious nor universal. Where the staffing firm becomes the *de jure* employer, it then commonly becomes subject to the normal range of employer obligations in law, such as they are, within the jurisdiction. Here, the question remains why regulatory effect imposed instead on the staffing firm would not hold, and/or why its effects would not be internalized within the staffing service contractual arrangement, and transferred back to the user, as part of a rational contracting exercise. As a very simple example, suppose that employment law universally requires a minimum wage of \$10 per hour. This same rule would apply regardless of whether the user or provider is the *de jure* employer. In the latter case, the provider would be required to pay the minimum wage, and we would expect it to charge the user for this mandated labour cost, plus markup. From the user's perspective here, regulation is formally equivalent across employment forms; there is no regulatory gap as between the employment forms. Note that the same outcome would seem to hold regardless of the size of the minimum wage imposed, so that either a \$10 or \$15 minimum wage would be similarly equivalent in effect across employment forms, there being no obvious regulatory gap to exploit from the triangular employment form in either case.

Overall then, despite fairly widespread acceptance of the basic intuition that a shift in *de jure* employer status enables user firms to *avoid* regulatory effects, these effects are neither universal nor boundless, and such claims require further articulation of how regulatory avoidance occurs, and the mechanisms at work in this process.⁴⁵

To this end, a more helpful concept in grasping the relationship between regulation and triangular employment growth is the concept of a *regulatory differential*, meaning a differential effect of regulation that occurs *across* employment forms. These regulatory differentials alter

remitting payroll taxes, the IRS additionally employs quite a different concept referred to as the "statutory employer" or the "section 3401(d)(1) employer", based on identifying the party with the "control of the payment of wages". See IRC section 3401(d)(1), and see IRS, Internal Revenue Manual Part 5.1.24 "Third-Party Payer Arrangements for Employment Taxes", at http://www.irs.gov/irm/part5/irm_05-001-024r.html. Mere status as a "section 3401(d)(1) employer" for tax purposes would not necessarily translate into common law employer status in a different institutional context.

⁴⁵ For a discussion of some specific examples of user firm cost avoidance under triangular employment, see Davidov, *supra*, note 14.

the effects of law upon actors, creating incentives for users to shift to triangular employment in certain contexts. It follows that in assessing the relationship between law and triangular employment growth, what is required is an extensive analysis of law with a view to deconstructing regulatory differentials embedded within the law or legal regime overall, creating an ultimate benefit for the user.⁴⁶ This analytical approach is required to assess the relationship between law and triangular employment growth within a single jurisdiction, and provides a framework for comparative analysis of law and triangular employment growth across jurisdictions. Here, a broad conception of the nature of law is necessary, recognizing the importance not only of explicit rules but of implied ones as well, establishing not only formal “rights” of parties, but also the various privileges, powers and immunities (as articulated in Hohfeld’s famous typology),⁴⁷ shaped by the overall configuration and interaction of explicit and implicit rules, and patterns of enforcement.

There exists a range of ways in which existing legal configurations and enforcement practices (collectively forming a legal “regime”) create unequal regulatory effects across employment forms, which are potential determinants of triangular employment growth in a given jurisdiction. The multiple ways in which some element of the legal regime overall might constitute a regulatory differential may be categorized according to the different types of mechanisms involved. The following taxonomy of regulatory differentials outlines some of these different mechanisms at play in a given jurisdiction.

1. Formal regulatory differentials. Some aspect of the legal regime may *formally* (i.e. explicitly) mandate some differential treatment as between direct and triangular employment, in some

⁴⁶ Somewhat similar understanding of this more complex relationship between law and triangular employment growth is illustrated in the work of Peck and Theodore, who in their comparative analysis of staffing industry growth across jurisdictions point out that the industry is highly active in *both* less and more regulated countries. They argue therefore that the true domain of the temporary staffing industry lies in what they call the murky “shadow” of regulation. Here, the industry seeks to function as a *relatively less* regulated employment form, exploiting the advantages that flow from “shedding many of the costs, risks, and longer-term responsibilities that accompany de jure employer status, all courtesy of the agencies employer of record designation”. Peck and Theodore, *Flexible Recession*, *supra*, note 1. See also Peck and Theodore, “Temped Out”, *supra*, note 1; Peck, Theodore, and Ward, *Constructing Markets*, *supra*, note 1.

⁴⁷ W.N. Hohfeld, *Fundamental Legal Conceptions As Applied In Legal Reasoning* (New Haven: Yale University Press, 1919).

respect.⁴⁸ These formal distinctions in treatment across employment forms may be further categorized as embodying either a *pro-regulatory* or *de-regulatory* thrust with respect to triangular employment,⁴⁹ with corresponding expected effects on triangular employment growth.

Examples of de-regulatory formal differentials include:

- A. Lower minimum labour standards for workers in triangular employment. These could take a variety of forms, and could reflect a degree of deviation from certain prevailing standards, or outright exemptions from them, and may vary in their salience.⁵⁰
- B. Formal rules affecting the capacity of workers in triangular employment to engage in collective labour relations. These may include restrictions on workers' eligibility to participate in collective bargaining at certain levels, or in concert with other workers, or other rules affecting the particularities of participation by workers in triangular employment. Examples are rules on whether workers under triangular employment may join particular types of "bargaining units", particularly in jurisdictions utilizing a variant of the U.S. "Wagner model" for labour relations.⁵¹ A particularly bald example of this sort of regulatory differential in the U.S. context is the rule established by the 2004 decision of the National Labor Relations Board in *Oakwood Care Centre*, which essentially bars temporary help workers from joining combined bargaining units containing direct-hire employees.⁵²

⁴⁸ Since this paper has attempted to analytically isolate employer status rules from underlying regulatory differentials, statutory provisions that allocate "employer" status to one of the parties are *prima facie* not included in this category. However, rules that allocate *particular obligations* across the parties may fall within this category. For some discussion of both of these sorts of rules, see Leah Vosko, "Legitimizing the Triangular Employment Relationship: Emerging International Labour Standards from a Comparative Perspective," *Comparative Labor Law and Policy Journal* Vol. 19:43, 43-77, at 64-70.

⁴⁹ Similarly one might respectively use the terms "decommodifying" or "commodifying" effect with respect to triangular employment.

⁵⁰ For example, prior to 2009 reforms, temporary help arrangements in the Canadian province of Ontario operated, to a certain extent, exempt from the normal requirements of "termination pay" under the province's employment standards legislation. See Bartkiw, *supra*, note 1, at 172. This regulatory differential (based on a prior exemption for so-called "elect to work" arrangements) was thus formal in nature, although it was not particularly salient in policy dialogue, until temporary agency employment became a much larger phenomenon in the past two decades.

⁵¹ See the discussion of restrictions on worker access to unionization in prevailing labour law regime in Canada in Bartkiw, *supra*, note 1, and Vosko, *Temporary Work, supra*, note 1.

⁵² 343 N.L.R.B. 659, 176 LRRM 1033 (2004).

Pro-regulatory differentials, which may be conceived as remedying somewhat the effects of other differentials, must of course also be taken into account in analysis overall. Examples of pro-regulatory formal differentials include:

A. Restrictions on the use of triangular employment in particular circumstances. These could include the enumeration of circumstances for its allowable use,⁵³ or measures that effectively amount to taxes imposed on triangular employment designed to discourage its use.

B. Revised minimum labour standards for workers in triangular employment. Differentials might be premium worker entitlements imposed upon triangular employment, as a remedial measure.⁵⁴ Another common example of these rules are the additional informational obligations and notice entitlements for workers in triangular employment, which may be conceived of as addressing some of the starkest issues around information deficiencies discussed in the literature review above.⁵⁵

C. Special rules aimed at addressing the comparable treatment of directly employed workers from those under triangular employment. These include provisions relating to the principle of “equal treatment” or non-discrimination” at the firm level.⁵⁶

D. Special rules addressing the ability of workers in triangular employment to engage in collective labour relations. These could include revisions to collective labour relations

⁵³ Storrie, *supra*, note 1, describes the use of these restrictions in certain EU jurisdictions.

⁵⁴ An example of these rules is the requirement in France that temporary agencies pay the worker a lump sum of money at the end of the assignment, in addition to the wage, and dependent upon whether the worker is offered another assignment, referred to in literature as “precarity pay”. See Vosko, “Legitimizing”, *supra* note 72.

⁵⁵ There are various examples of these sorts of rules in practice. Several U.S. states have imposed laws requiring staffing firms to provide workers with enumerated information requirements prior to their being “placed” by the staffing firm. See for example disclosure obligations imposed on “day labor pools” in Florida’s “Labor Pool Act” (FLA. STAT.ANN. s. 31.448.20 to 31.448.25) and in its regulations for “employee leasing companies” (FLA. STAT.ANN. s. 31.468.520 to 31.468.535). In Canada, the province of Ontario similarly imposed certain disclosure requirements relating to aspects of “work placements”, under temporary help arrangements, in 2009. See *An Act to amend the Employment Standards Act, 2000 in relation to temporary help agencies and certain other matters*, c. 9, S.O 2009, ss. 74.5-74.7.

⁵⁶ See for example the rules relating to these concepts in *the EU Directive 2008/104/EC of the European Parliament and of the Council of the European Union on Temporary Agency Work*, Article 5.

regulation with respect to workers in triangular employment, or the construction of particular frameworks for their purposes.⁵⁷

2. Contingent regulatory differentials: Here, the law does not formally impose a different regulatory treatment as between direct and triangular employment. However, law does formally provide for a distinction in some sort of regulatory treatment of an “employer”, which treatment is *contingent* on some other measurable circumstance, *the occurrence of which may be influenced by the use of triangular employment*. Important examples of these are the numerical thresholds of various sorts, where the number of “employees” of a firm determines the impact or applicability of a particular rule.⁵⁸ These contingent differentials may at times appear in a simple “headcount” form. However, they may also take a more complex form, involving calculations and/or comparisons of numerical quantities of employees, or sub-categories of employees, along with related rules for measuring quantities, characteristics, or qualities, of these employee categories.⁵⁹ Other examples of these may be based on measurements of aggregate employment budgets or expenditures. Measurements of this sort have been increasingly applied as a governance tool in public administration in recent decades as part of austerity measures and/or new public management techniques, coinciding with triangular employment growth in the public sphere.⁶⁰ In some forms, the use of triangular

⁵⁷ See *Ibid*, Article 7.

⁵⁸ In Canada, an example of such a headcount-based threshold would be the requirement in the province of Ontario that a firm have at least 50 employees in order for employee entitlements to “emergency leave” to apply. See *Employment Standards Act, 2000*, S.O. 2000, c. 41, s. 50(1). In the U.S., a comparable example would be the threshold that the employer employ “50 or more” employees in order for the *Family Medical Leave Act* to apply. See *Family Medical Leave Act*, 29 USC s. 2611(4)(A)(i).

⁵⁹ See for example the various “non-discrimination rules” employed in U.S. tax law as part of a larger *quid pro quo* for the preferential tax status provided for employer sponsored benefit plans in that country. These rules impose certain egalitarian principles on employers in their distribution of pension and health care benefits across different employee categories. Elsewhere, I discuss the role of these rules as a factor in explaining the divergence in triangular employment as between Canada and the U.S. See Timothy J. Bartkiw, “Regulatory Differentials and Triangular Employment Growth in the U.S. and Canada” (forthcoming).

⁶⁰ For a discussion of recent growth in the use of temporary help agency services by managers throughout the Canadian federal government and the connection to these sorts of budgetary devices, see Timothy Bartkiw, “Temporary Help Agency Employment in the Federal Government”, in Bruce Doern and Chris Stoney, eds., *How Ottawa Spends, 2010-2011*, (Kingston: McGill-Queens University Press, 2010). Similarly, evidence suggests that there has occurred tremendous growth in China of the use, by state-owned enterprises (SOEs), of so-called “dispatched employees” (read: temporary help workers) under China’s Labour Contract Law of 2007. See Wei

employment to shift the *de jure* employer status of only a *subset* of an organization's workers may produce a revised regulatory effect affecting a larger group of workers, including direct-hire employees.⁶¹

3. *Informal regulatory differentials*: Assuming that the various remaining components of the legal regime formally apply consistently across employment forms, for various potential reasons, the *de facto* regulatory effect of law is not perfectly robust across the two employment forms. Without using this terminology, academic literature and ILO Reports have identified numerous sorts of informal or sociological effects of triangularity on the efficacy of labour law. An important concern here is how triangularity impacts regulatory enforcement, considered here as occurring through various sorts of causal pathways, although the concept should be considered as referring not only to enforcement activities themselves but to a broader set of ways in which triangularity may influence actor behavior, itself mediated by regulation. Institutional and Critical theoretical perspectives on triangular employment growth reviewed earlier in this paper provide the foundational logic for understanding this category of regulatory differentials in particular, since these explanations do not necessarily depend upon the specific configuration of rules within the legal regime. Thus, we may conceive of their being *informal* regulatory differentials embedded throughout the legal regime, to the extent that the use of triangular employment within that regime produces, unmitigated by the regime, any of the following conditions:

Quan, Yan Dong, and Ye Jingyi, "Rethinking the Labour Contract Law of China," paper presented to the Labour Law Research Network conference, Barcelona, June 2013. Anecdotal evidence suggests that various headcount rules binding SOEs are a key factor driving this very recent trend.

⁶¹ For example, in the U.S. case discussed above, the use of triangular employment to effect a change in status under U.S. tax law's benefit plan rules, may cause effects experienced by direct hire employees in the degree of regulatory protection they receive with respect to benefit provision.

- A. Triangularity increases worker confusion and obfuscation over formal allocation of employer responsibilities as between the user and provider.
- B. Triangularity increases the cost/burden on workers in seeking to (re)negotiate terms and conditions of work.
- C. Triangularity increases the cost/burden on workers in seeking enforcement of their formal rights and standards.
- D. Triangularity increases the regulatory cost/burden on local authorities in the enforcement of their law/policy domain.
- E. Triangularity may affect workers' self-identity, expectations, social interaction, and solidarity.

Informal regulatory differentials are thus a fairly broad and fluid category of phenomena. Given their seemingly low dependence upon the specificity of labour law, it follows that they likely exist, even if only in latent form, in most (if not all) jurisdictions having a regulated labour market. In other words, each regulated labour market contains internally the seeds of this third potential source of triangular employment growth, to varying degrees, mediated by other domestic social and organizational factors. Thus, because of the existence of informal regulatory differentials, absent explicit remedial policy measures (pro-regulatory formal differentials, discussed above), triangular employment growth may take root, to *some* degree, in virtually any regulated labour market. This is not to say, of course, that the benefits and costs of triangular employment will in any given context *necessarily* align to this result. The point is rather simply that because of the nature of this 3rd category of regulatory differentials, there is a *generalized potential* benefit for users ranging in size across different contexts, and thus a widespread potential source of triangular employment growth. This category then, helps explain why we observe triangular employment growth of some degree across so many different jurisdictions, with a wide range of formally disparate labour law regimes.⁶²

⁶² For example, growth across a large number of EU jurisdictions, despite regulatory diversity, is fairly well established empirically. See Storrie, *supra*, note 1. See also various studies referred to in note 1.

To complete this analytical framework concerning the relationship between labour law and triangular employment growth, the importance of the prevailing employer status rules in a given jurisdiction must be taken into account. In this analytical framework, employer status rules should be understood as serving a sort of bridging or gate-keeping function. That is, the particulars of employer status rules affect the possibility, and thus the regularity or degree, of shifting *de jure* employer status from a user to a staffing firm – and thereby *accessing* the available regulatory differential(s). Assuming a given degree of regulatory differentials for access in a given jurisdiction, the *easier* (or more *likely*) it is to achieve a shift in *de facto* employer status, and the greater will be the expected benefit from triangular employment. Thus, employer status rules in a given jurisdiction *mediate* the relationship between regulatory differentials and triangular employment growth in that jurisdiction. Although they do not themselves constitute the underlying *source* of benefit to the user, and their effect on triangular employment growth is inherently *interactive* with regulatory differentials separately defined, employer status rules remain an important *independent* variable in the relationship between law and triangular employment growth in a given jurisdiction.

V. Concluding Thoughts

The goal of this paper was to contribute to our understanding of growth in triangular employment relations embedded in staffing services, by examining its relationship with labour law. The review of how triangular employment growth may be understood from alternative theoretical perspectives shed light on the potentially problematic nature of this growth. At a minimum, I have hopefully articulated some important limits to which certain theoretical explanations for triangular employment growth, rooted in beliefs about benign “efficiency”, can be used to dismiss such concerns.

Further, understanding of the relationship between labour law and triangular employment growth has hopefully been furthered by the introduction of the concept of a regulatory differential; the articulation of the different forms these may take in the typology provided; and the analytical clarification of the relationship between these phenomena and employer status

rules within a jurisdiction. It is hoped that the framework provided helps clarify the types of analysis required in uncovering the relationship between triangular employment growth and domestic labour law.

This analytical framework may also serve as an improved lens for comparative analysis of triangular employment growth across jurisdictions. Informed by this framework, comparative analysis would likely reduce its emphasis on uncovering regulatory diversity or differences in relevant rule categories around triangular employment (and its variants)⁶³ and on seeking growth patterns across jurisdictions based on notions of their being “more” or “less” employment regulation in a jurisdiction. Rather, comparative analysis would be increasingly anchored in what might be considered a “difference of differences” approach. This involves an extensive review of labour law, across sub-fields, towards uncovering the degree to which it embodies regulatory differentials in different forms that may help explain observed triangular employment growth dynamics.⁶⁴ The extent to which the existence of regulatory differentials helps to explain triangular employment growth is important for policy analysis, since it challenges the conception of such growth as being the natural (and necessary) product of efficiency-enhancing market activities, and helps illuminate the space for alternative labour policy choices.

⁶³ See for example Silvia Spattini, “Agency Work: A Comparative Analysis”, 1 *E-Journal Of International and Comparative Labour Studies* 169 (2012); Aaron B. Sukert, “Marionettes of Globalization,” 27 *Syracuse J. Int’l L. & Com.* 431 (2000).

⁶⁴ In separate work (forthcoming), I provide comparative analysis of this sort, comparing regulatory differentials in certain subfields of Canadian and U.S. labour law, which I argue help explain differences in triangular employment growth patterns in Canada and the U.S.. See Bartkiw, *supra*, note 88. .

Paper # 2: Timothy J. Bartkiw, “Regulatory Differentials and Triangular Employment Growth in the U.S. and Canada”, *Employee Rights and Employment Policy Journal*, vol. 19, Issue 1, 2015 (forthcoming).

I. Introduction:

Over the past few decades, there has been substantial growth in the global “staffing” industry, with considerable variation in its growth across different jurisdictions.¹ This industry provides a range of employment related services² under different labels, supplementing or displacing employment functions performed by “user” firms. Coinciding with this has been growth in “triangular employment.” In a triangular employment relationship,³ functions traditionally performed by a single employer are distributed across a “user” firm and a service “provider” firm such that a non-trivial, objective question exists about the appropriateness⁴ of the allocation of employer status and corresponding rights, obligations, or liabilities in the relationship.⁵ Triangular employment is not a juridical employment category, nor a recognized employment form identified in “official” data. Rather, it is a *theoretical* concept capturing particular policy concerns, including how these types of employment relationships enable a shift in bargaining power and potential erosion in working conditions, in the employment

¹ Jamie Peck, Nik Theodore and Kevin Ward, *Constructing Markets for Temporary Labour: Employment Liberalization and the Internationalization of the Staffing Industry*, 5 GLOBAL NETWORKS 3(2005). See also DONALD STORRIE, TEMPORARY AGENCY WORK IN THE EUROPEAN UNION (European Foundation for the Improvement of Living and Working Conditions, Luxembourg: Office for the Publications of the European Communities, 2002).

² The use of the term “services” is not meant to attribute any particular degree of legitimacy to such business transactions. It has been argued that promulgating the broader “staffing services” label was part of the historical transformation of the temporary help industry into lateral, related services and part of its effort to consolidate its legitimacy in light of its previously stable, yet paradoxical, regulatory regime. See LEAH F. VOSKO, TEMPORARY WORK: THE GENDERED RISE OF A PRECARIOUS EMPLOYMENT RELATIONSHIP (2000), 137-156. See also the discussion of the historical expansion of related services in Robert Parker, FLESH PEDDLERS AND WARM BODIES: THE TEMPORARY HELP INDUSTRY AND ITS WORKERS (1994) at 40-42.

³ Importantly, unlike in some other kinds of relationships involving work, in triangular employment there is “an” employment relationship alleged to exist along at least *one* of the sides of the triangle.

⁴ Here I am not simply considering the question of whether employer status has been allocated under actually existing employer status rules, which vary across jurisdictions. Rather, I also include in this category relationships in which the application of actually-existing employer status rules, such as they are, result in objective policy concerns about the appropriateness of the allocation of employer status.

⁵ For a somewhat similar attempt to define this phenomenon, see International Labour Conference, Report V(1): Scope of the Employment Relationship, International Labour Conference, 95th Session, 2006, p. 13.

relationship.⁶ It is a previously well-established concern that certain staffing services may generate triangular employment,⁷ although not every staffing service should be understood as doing so. For example, in both the U.S. and Canadian contexts, it is fairly clear that firms merely providing “payroll” services to user firms, and nothing more, do not produce triangular employment as understood in this analysis. On the other hand, certain other services embody a contrived attempt to alter employer status allocation, away from the user firm, explicitly embraced as a part, or consequence, of the service provided.

Different types of staffing services vary within both a temporal and a qualitative dimension.⁸ Some services are designed to be short term,⁹ while others are semi-permanent arrangements.¹⁰ While temporality may “matter” in the construction of triangular employment, the main determinant, based on the definition used in this paper, would seem to be the qualitative nature of the services provided, and the overall resulting (re)allocation of employment functions across the user and staffing firm. In the U.S. and Canada, the two most salient examples of services that appear *prima facie* to generate triangular employment are “temporary help”¹¹ (short term) and “professional employer” (long term) services.¹²

⁶ Peck and Theodore argue that growth in temporary agency employment itself has contributed to a generalized deregulation of the employment relationship itself. See Jamie Peck and Nik Theodore, *Flexible Recession: The Temporary Staffing Industry and Mediated Work in the United States*, 31(2) CAMBRIDGE JOURNAL OF ECONOMICS 171. (2007).

⁷ Triangular employment also exists in other contexts, such as in certain subcontracting arrangements. See International Labour Conference, *Id.*

⁸ See Timothy J. Bartkiw, *Labour Law and Triangular Employment Growth: A Theory of Regulatory Differentials*, INTERNATIONAL JOURNAL OF COMPARATIVE LABOUR LAW AND INDUSTRIAL RELATIONS (forthcoming).

⁹ Short term services include “temporary help,” “day labor,” and “temp to perm” services.

¹⁰ More common long term services are “employee leasing” or “professional employer” service. Of course, in practice there are also deviations in temporality from what the service bundle “label” implies. The growth in so-called “perma-temp” arrangements is a key example of this. See ERIN HATTON, *THE TEMP ECONOMY: FROM KELLY GIRL TO PERMATEMPS IN POSTWAR AMERICA* (2011). Other evidence of increasing duration of assignments in so-called temporary help arrangements is also provided in VOSKO, *supra* note 2. See also Matt Vidal and Leann M. Tigges, *Temporary Employment and Strategic Staffing in the Manufacturing Sector*, 48 INDUSTRIAL RELATIONS 55 (2009).

¹¹ Other labels are used to identify similar service bundles elsewhere, such as the use of the term “labor broker” services in South Africa. See Jan Theron, *Intermediary or Employer? Labour Brokers and the Triangular Employment Relationship*, 26 INDUS. L.J. JUTA 618 (2005).

¹² Another label used for a particular long term service arrangement (historically used somewhat interchangeably with the “professional employer” service label) is that of “employee leasing” services. See the discussion in EDWARD A. LENZ, *CO-EMPLOYMENT: EMPLOYER LIABILITY ISSUES IN THIRD-PARTY STAFFING ARRANGEMENTS*, 7TH ED. (2011). As Lenz points out, the term “employee leasing” is sometimes used as a generic term to refer to all

There already exists an extensive literature about the various policy concerns arising out of the growth in temporary help services in the past few decades.¹³ On the other hand, there has been far less analysis, let alone *awareness*, of the growth in “professional employer” services in the U.S.A. recently.¹⁴ A PEO service arrangement involves the contractual provision of a various employment related services, usually on a long term basis, typically *without* the actual *labor supply* component typifying the “temporary help” concept. Through these arrangements, the PEO and its client purport to construct what in the U.S. is commonly referred to as a “co-employment” relationship. The National Association of Professional Employer Organizations (“NAPEO”), the key industry association for “professional employer” organizations, (“PEOs”), explicitly embraces “co-employment” as being at the heart of its member firms’ services.¹⁵ “Co-employment” is a term created by the PEO industry; it is not a juridical category, and is arguably ambiguous.¹⁶ In PEO services, the service contract outlines the basis of co-employment, involving a (re)allocation of employment functions and responsibilities, and the parties’ intended assumptions of employer liability in relation to specific aspects of labor regulation.

This paper traces growth patterns in temporary help and PEO services in the U.S. and Canada, and links them to specific characteristics of regulation, illustrating that certain characteristics of labor law in the two jurisdictions help explain these growth patterns. Various forms of “regulatory differentials” are important contributors to triangular employment growth.¹⁷

Regulatory differentials are differences in regulatory effect, under existing regulation, that

forms of staffing services. However, it is more often (and here) understood to refer to an intricate human resource outsourcing arrangement that purports to transfer employer status to the employee leasing firm, which in more recent years have become increasingly referred to as “professional employer organizations”. The fact that employee leasing services themselves are not generally short term arrangements, ought not to be confused with the fact that the *de jure* definition of a so-called “leased employee”, a concept used in U.S. tax law and discussed in significant detail *infra*, is partly based on the *duration* of services provided by the worker in question. See Internal Revenue Code, s. 414(n).

¹³ See Bartkiw, *supra* note 8; VOSKO, *supra* note 2; STORRIE, *supra* note 1; and HATTON, *supra* note 10. See also Harris Freeman and George Gonos, *Regulating the Employment Sharks: Reconceptualizing the Legal Status of the Commercial Temp Agency*, 8 WORKINGUSA: THE JOURNAL OF LABOR AND SOCIETY 293 (2005).

¹⁴ Britton Lombardi and Yukako Ono, *Professional Employer Organizations: What are they, who uses them, and why should we care?*, ECONOMIC PERSPECTIVES 2 (2008).

¹⁵ See NAPEO website description of co-employment at <http://www.napeo.org/peoindustry/coemployers.cfm>.

¹⁶ Thus, employer status in these arrangements would be determined by prevailing employer status rules and, typically, the primacy of fact.

¹⁷ Bartkiw, *supra*, note 7.

occur across direct and triangular employment forms, from the ultimate perspective of the user.¹⁸ In various ways and contexts, they create incentives stimulating the use of triangular employment. In this framework, there are three conceptually separate categories of regulatory differentials. First, “formal differentials” are differences in effect flowing from explicit formal distinctions in law applied as between direct and triangular employment. Second, “contingent differentials” are regulatory differences contingent on the occurrence of some other particular fact or state formally specified in the law, the occurrence (or not) of which may be affected by the use of triangular employment (e.g. so-called employee “head count” rules). Third, “informal differentials” are *de facto* differences in regulatory effect, despite formal consistency of law across the two employment forms.¹⁹ Further, while existing regulatory differentials represent potential benefits available to user firms, user firm *access* to these benefits is further complicated and *mediated* by the domestic regime of employer status rules, since they determine the feasibility and costs involved in shifting employer status away from the user. In other words, given a certain potential benefit, employer status rules mediate the *expected* benefit of triangular employment.²⁰ This theoretical approach allows for certain analytical gains in isolating the effects of employer status rules from underlying regulatory differentials themselves, in explaining triangular employment growth, and in comparative analysis of this growth across jurisdictions.

The remainder of this paper applies this theoretical framework, to help explain triangular employment growth patterns in the U.S. and Canada in recent decades, by doing the following. First, data analysis provided in the next section shows that there has not only been substantial growth in triangular employment in the U.S. and Canada in recent decades, but that there has also been significantly greater growth in the U.S.. Second, legal analysis is provided to show that certain key regulatory differentials have existed in the U.S., which were effectively absent in Canada, and that the size of these regulatory differentials was magnified by legislative developments over this time period. Here the legal analysis provided is limited to two key sub-fields of labor law: employee pensions law and employer-sponsored health benefits law. Third,

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Id.*

further legal analysis is provided to show that differences in employer-status rules in the U.S. and Canada were also consistent with this theoretical framework, such that user firm access to underlying regulatory differentials was comparably greater in the U.S..

II. Staffing Services & Triangular Employment Growth in Canada and the U.S.:

This section reviews official data illustrating growth in temporary help services and professional employer services, the two main staffing services generating triangular employment in Canada and the U.S.. Official definitions of staffing industry statistical categories have been adjusted over time to attempt to distinguish between different services.²¹

From 1980-1997, official data was organized based on the Standard Industrial Classification (1980) system of industry categories, which included an industry category called “Employment Agencies and Personnel Suppliers”, comprised of the two subcategories “Employment Agencies” and “Personnel Suppliers”, with the latter being the relevant category for our purposes for this period.²² In 1997, Canada and the U.S. adopted the NAICS industrial classification system, redefining the industry into one large category called “Employment Services”, with three subcategories: “Employment Placement Agencies”, “Temporary Help Services,” and “Employee Leasing Services,” the latter being the historical precursor to professional employer services. In 2002, the industry subcategory “Employee Leasing Services” was renamed “Professional Employer Services”, mirroring the “rebranding” of this sub-industry in the U.S..²³

²¹ Canada, the U.S. and Mexico have since at least 1997 used the North American Industrial Classification System for classifying official statistics. In certain instances, efforts have been made to “recode” some earlier data based on NAICS, to create longer time series for comparisons. The degree to which official categorization reflects actual practice is undoubtedly somewhat limited. In an interview, a president of a large Canadian staffing firm stated that there is not a strong understanding of the concept of “PEO” services in Canada, despite this being an official category used by Statistics Canada. Official statistics, reviewed in Part V of the paper, suggest that there is (at most) a very small volume of such services supplied in Canada.

²² Employment Agencies focused primarily on matching and recruitment services, and lacked triangular employment relations.

²³ The only subsequent change in definitions of these industry categories took place in 2007, when the 56131 Employment Placement Agencies title was changed to Employment Placement Agencies and Executive Search Services, to clarify that the latter form of search and matching services fell under this category. Despite the

Table 1: Employment in Employment Services Industry, Canada, 1982-2009, Thousands

Year	SIC 771 Employment	% of Aggregate	NAICS 5613	% Agg.
	Agencies and	Employment	Employment	
	Personnel Suppliers		Services	
1982				
1983	33.4	0.303		
1984	38.3	0.339		
1985	46.7	0.401		
1986	49.1	0.409		
1987	53.9	0.437		
1988	59.8	0.471		
1989	71.7	0.552		
1990	63.6	0.486		
1991	54.1	0.421	58.0	0.451
1992	45.7	0.359	48.7	0.382
1993	59.7	0.467	60.3	0.471
1994	69	0.528	72.6	0.556
1995	79.4	0.597	84.9	0.639
1996	92.3	0.688	98.3	0.732
1997			108.5	0.792
1998			117.8	0.838
1999			126.3	0.877
2000			132.5	0.897
2001			144.2	0.965
2002			145.0	0.947
2003			146.2	0.933
2004			162.2	1.017
2005			169.5	1.048
2006			183.3	1.112
2007			183.8	1.090
2008			179.8	1.050
2009			151.4	0.899

Source: Survey of Employment, Payroll and Hours.

Table 1 contains data on employment²⁴ levels in the aggregate “employment services” industry in Canada for years 1982-2009. The data reveal some important trends. First, it is clear from

adoption of these new categories, there is very limited data on the PEO sub-category in Canada, because of its extremely small size. For example, there is no reliable annual data series on the number of Canadian workers “employed” in this sub-industry.

²⁴ Employment levels reported for these industries would include staff directly employed and working in staffing services firm administration. Nevertheless, the vast bulk of employment reported in these statistics represents workers assigned to clients, and thus most prior literature uses this as one potential proxy for employment levels

the figures in columns 1 and 3 that employment in the industry grew substantially in Canada from 1983 to its peak in 2007. Further, as shown by the calculations in columns 2 and 4, this industry's employment growth was disproportionately greater than aggregate employment growth in Canada, and thus the industry's share of aggregate employment levels similarly experienced a growth trend up until 2005, after which its employment share has declined slightly. Available data does not allow us to decompose these employment levels in Canada across industry subcategories, so they are used as the best available proxy for measuring underlying employment growth in temporary help arrangements, as done in prior analysis.²⁵ Despite the clear growth trend, based on the measures employed in Canadian official data, the industry's share of aggregate employment peaked at about 1.1% in 2006.

Table 2 presents data on employment levels for the U.S. employment services industry for this same period. The U.S. data similarly confirms a substantial employment growth trend from 1982 to 2009, although it does not reveal a comparable peak level. Other important contrasts with Canadian trends also exist. First, the U.S. employment services industry overall appears to be relatively much larger than the Canadian, measured as a share of aggregate employment. Further, until approximately 2000, there was a positive trend in the temporary help sub-industry's share of aggregate employment, but this share subsequently stabilized, or peaked.²⁶ This trend up to, and peak at, the year 2000, is confirmed by both the CES and CBP data sources on the U.S. industry. U.S. data also reveals that despite this bounded growth in temporary help, the *combined* staffing industry's overall employment share nevertheless continued to grow, due to remarkable growth in employment levels in the "professional employer" sub-industry. The CBP data series reveals that employment in this sub-industry grew from approximately 436 thousand employees in 1988 to about 2.07 million employees in 2008, a remarkable growth rate of 374% over two decades!

and growth. Since data may be affected significantly by variations in assignment length, industry revenues are also used as a helpful additional proxy.

²⁵ See for example LEAH VOSKO, *MANAGING THE MARGINS* (2010); and Leah Vosko, *A New Approach to Regulating Temporary Agency Work in Ontario or Back to the Future?*, 65 *RELATIONS INDUSTRIELLES* 632 (2010).

²⁶ Peck and Theodore similarly discuss an upper limit to the growth in the proportionate size of the temporary help industry (without analyzing the other components of the staffing industry) in Jamie Peck and Nik Theodore, *Temped Out? Industry Rhetoric, Labour Regulation, and Economic Restructuring in the Temporary Staffing Business*, 23(2) *ECONOMIC AND INDUSTRIAL DEMOCRACY* 143 (May 2002).

Confirmation of these patterns is provided by separate data on industry revenues, a proxy for the market value of labor supplied under these service arrangements. Table 3 provides data on operating revenue for the employment services industry category in Canada from 1982 to 2010, along with a breakdown of the allocation of these revenues across the industry subcategories beginning in 1998. By the year 1998, the first year for which an annual breakdown across subcategories is available, temporary help services constituted the largest share of industry revenues, by far, at 81%. This distribution of industry revenues remained fairly stable, with some variation through 1998-2005, after which the temporary help share seems to have declined, while the share owing to employment placement and executive search services increased somewhat.

Table 2 – Employment in Employment Services Industry, U.S.A., 1982-2008, Thousands.

Year	SIC 736 Personnel Supply		7361 Employment Agencies		7363 Help Supply Services		5613 Employment Services		56131 Employment Placemen		56132 Temporary Help		56133 Professional Employers (CBP)	
		% Agg.		% Agg.		% Agg.		% Agg.		% Agg.		% Agg.		% Agg.
1982	541	0.6	124	0.14	417	0.47								
1983	618.6	0.69	130.5	0.14	488.1	0.54								
1984	796.7	0.84	154.2	0.16	642.5	0.68								
1985	890.7	0.91	158.7	0.16	732	0.75								
1986	990.2	1	153.7	0.15	836.5	0.84			10467	0.0105%				
1987	1176.8	1.15	187.9	0.18	988.9	0.97			12621	0.0124%				
1988	1350.4	1.28	224.5	0.21	1125.9	1.07			11769	0.0112%	1075730	1.021%	436192	0.41%
1989	1454.5	1.35	238.8	0.22	1215.8	1.13			12031	0.0111%	1154169	1.069%	453642	0.42%
1990	1534.5	1.4	246.4	0.23	1288.2	1.18			12846	0.0117%	1210312	1.105%	489578	0.45%
1991	1484.5	1.37	216	0.2	1268.4	1.17			12750	0.0118%	1230355	1.135%	550395	0.51%
1992	1629.3	1.5	218.6	0.2	1410.6	1.3			12826	0.0118%	1405284	1.293%	534364	0.49%
1993	1906.1	1.72	237	0.21	1669.2	1.51			12423	0.0112%	1816889	1.639%	607861	0.55%
1994	2271.7	1.99	254.6	0.22	2017.1	1.77			12474	0.0109%	2097630	1.835%	648740	0.57%
1995	2475.5	2.11	286.6	0.24	2188.8	1.87			13150	0.0112%	2397181	2.044%	622960	0.53%
1996	2653.5	2.22	301.1	0.25	2352.4	1.97			13067	0.0109%	2478726	2.071%	677234	0.57%
1997	2985	2.43	328.7	0.27	2656.3	2.17			14085	0.0115%	2951235	2.404%	827983	0.67%
1998	3278.1	2.6	352.4	0.28	2925.8	2.32	3614066	2.87%	7444	0.0059%	2549653	2.025%	881170	0.70%
1999	3615.8	2.8	368	0.29	3247.8	2.52	3993443	3.10%	8477	0.0066%	2725800	2.113%	1009768	0.78%
2000	3883.4	2.95	393.8	0.3	3489.6	2.65	4572954	3.47%	9343	0.0071%	3012681	2.286%	1253808	0.95%
2001	3446	2.61	362	0.27	3084	2.34	4363620	3.31%	10261	0.0078%	2676010	2.030%	1338941	1.02%
2002	3169.4	2.42	316.6	0.24	2852.8	2.18	3880888	2.98%	9692	0.0074%	2390634	1.834%	1181080	0.91%
2003							3902177	3.00%	8361	0.0064%	2188383	1.683%	1562943	1.20%
2004							4027646	3.06%	8288	0.0063%	2325501	1.769%	1519585	1.16%
2005							4579822	3.43%	8384	0.0063%	2615315	1.956%	1746555	1.31%
2006							5101697	3.75%	8748	0.0064%	2930520	2.153%	1929137	1.42%
2007							5131446	3.73%	8534	0.0062%	2901213	2.108%	1983451	1.44%
2008							5230878	3.82%	15733	0.0115%	2875337	2.102%	2069045	1.51%

Source: SIC 736, 7361, 7363 data from Current Employment Statistics; NAICS 5613, 56131, 56132, 56133 data from County Business Patterns.

Table 3 – Employment Services Industry, Operating Revenues – Canada (\$000,000's)

Year	Total revenues	Temporary Help %	Placement %	Other ²⁷ %
1982	433.0			
1983	537.0			
1984	713.0			
1985	945.0			
1986	1154.0			
1987	1422.0			
1988	1776.0			
1989	2105.0			
1990	2105.0			
1991	1891.0			
1992	1752.0			
1993	1844.0			
1994	2110.0			
1995	2479.0			
1996				
1997				
1998	4,047.3	81.0	18.0	--
1999	n/a	n/a	n/a	n/a
2000	5144.1	75.7	21.5	2.8 ²⁸
2001	5125.0	79.0	18.4	2.6
2002	5420.7	79.3	18.6	2.1
2003	5689.1	79.7	19.5	0.8
2004	6268.9	79.0	19.3	1.8
2005	7402.0	77.2	21.7	1.1
2006	8217.5	68.9	29.7	1.4
2007	9108.2	59.6	36.4	4.1
2008	9323.1	60.2	36.8	3.0
2009	8583.7	60.7	30.7	8.6
2010	9298.6	56.3	35.6	8.1

Source: Annual Report on the Survey of Services Industry: Employment Services, Statistics Canada

Note: Wherever applicable, "revised" estimates are used for each year published in subsequent annual reports.

Note: Data for 1982-1995 are based on the SIC 1980 industry 3-digit category 771 Employment Agencies and Personnel Suppliers. Data from 1998 are based on the NAICS.

²⁷ The title "Other" is used by Statistics Canada in these annual Reports, and seemingly reflects a view that this latter category is more of a catchall category, one that cannot be said to simply represent revenues relating to employee leasing or professional employer services.

²⁸ Statistics Canada estimates that in 2000, 1.3% of overall industry revenues were from "payroll services" and 1.5% was from "other" services.

Table 4: Employment Services Industry, Operating Revenues, 1997-2007 (selected years) - U.S.A. (\$000,000s)

Year	Employment Services	Placement	Temporary Help	Professional Employer
1997	86,133	4,787 (5.6%)	57,221 (66.4%)	24,125 (28.0%)
2002	128,661	5,940 (4.6%)	68,190 (53%)	54,532 (42.3%)
2007	209,690	18,794 (9.0%)	105,691 (50.4%)	85,205 (40.6%)

Source: Economics Census for applicable years.

At the same time, prior to 2009-10, the data confirms that the “professional employer” services category was a very small and insignificant portion of the Canadian employment services industry. Indeed, it is revealing to note that in its annual publication of these statistics, Statistics Canada has consistently presented this third sub-category of revenues – those resulting from neither placement nor temporary help services – as merely a category of “other” services, suggesting a lack of confidence in its ability to attribute these revenues to “professional employer” services at all. Even as an ambiguous catchall category, the proportion of services represented by this “other” category only grew very recently (during 2007-10).

In contrast, U.S. data on industry revenues confirms the relatively large size of the U.S. professional employer industry, both in comparison to what exists in Canada, and in terms of its share of the U.S. staffing industry. The data shows that extraordinary growth (126%) occurred in the fairly short period between 1997 and 2002, with very high growth rates (40.6%) continuing in the next 5 years, even if this was outpaced by then even more extraordinary growth (216%) in placement related services from 2002 to 2007.

Overall, the data reveal on the one hand a common growth pattern, in an aggregate sense, of triangular employment as embodied in these two forms of staffing services, while on the other hand an important divergence. Triangular employment growth has been far greater in the U.S. in recent decades, where it has been based in two categories of services, rather than just in temporary help services, as in Canada.

III. Regulatory Differentials and Employer Status Rules in the U.S. and Canada:

This section explains the growth patterns reviewed in the previous section by providing legal analysis showing 1) the emergence (and expansion) of key regulatory differentials in the U.S. (in the two subfields of regulation of employer-based pensions and employer-sponsored health care plans) absent in Canada, during the relevant time period, and 2) the role of employer status rules in mediating access to these regulatory differentials. Analysis begins with the latter.

Employer Status Rules in Canada and the U.S.

In both Canada and the U.S., employer status is allocated in accordance with common law rules involving the application of certain types of “tests”. Applying such tests against the underlying facts of a purported, contractual arrangement, employer status allocation adheres to what the ILO refers to as “the primacy of fact.”²⁹ Further, *de jure* employer status is not necessarily uniform across policy sub-fields or regimes, meaning that status may be allocated somewhat differently by adjudicators in different regimes or contexts. For example, the capture of *de jure* employer status for staffing firms under payroll tax rules does not guarantee a similar outcome for the purposes of minimum employment standards, labor relations, or workers compensation regimes.³⁰ Nevertheless, certain patterns are identifiable and in both countries, core common law tests have evolved.

In the U.S., the application of common law tests to triangular relationships may result in there being an employment relationship declared with one or more “employers” meeting the test for

²⁹ International Labour Conference, Report V(1): Scope of the Employment Relationship, International Labour Conference, 95th Session, 2006, p. 24.

³⁰ For example, one remaining distinction is that adjudicators under the Fair Labor Standards Act, which primarily addresses issues of minimum wage, and hours of work restrictions, continue to apply the concept of “dependency”. See subsequent discussion of employer status case law in Part VI. In terms of tax law, although the common law employer test has been codified, for certain purposes, such as liability for withholding, reporting and remitting payroll taxes, the IRS additionally employs quite a different concept referred to as the “statutory employer” or the “section 3401(d)(1) employer”, based on identifying the party with the “control of the payment of wages”. See IRC section 3401(d)(1), and see IRS, Internal Revenue Manual Part 5.1.24 “Third-Party Payer Arrangements for Employment Taxes”, at http://www.irs.gov/irm/part5/irm_05-001-024r.html. Mere status as a “section 3401(d)(1) employer” for tax purposes would not necessarily translate into common law employer status in a different institutional context.

employer status. In this context, the process of applying the test for “employer” status in these contexts may be understood as a simultaneous test for whether the worker is an “employee” of the organization in question. The most common test for determining employer status in the U.S. has been referred to as the “common law agency test”, which relies heavily on indicia of control and supervision, and thus has sometimes been referred to as the “right to control” test.³¹ This approach involves case-by-case application of an extensive, although non-exhaustive list of factors, including thirteen factors cited by the Court in *Community for Creative Non-Violence v. Reid*.³² In this approach “special weight is given to the control of the manner and means by which assigned tasks are completed”.³³

Historically, certain other “tests” have at times been employed by U.S. courts and adjudicators in different contexts, emphasizing somewhat different criteria. While some commentators have argued that there is little substantive difference between the alternatives, conceivably they do signal some subtle emphasis of certain factors over others. Some of these alternatives have been referred to as the “statutory purposes” test, the “economic realities” test, the “hybrid” test, and the “common law entrepreneurial control” test.³⁴ The “statutory purpose” test is an approach that is *broader* than the traditional common law agency test.³⁵ Here the adjudicator expressly looks to factors seemingly beyond the normal indicia of control, to other factors based upon an interpretation of the goals of the particular statute in question and/or the mischief it is aimed at redressing.³⁶ The “economic realities” test purportedly looks beyond indicia of control to examine underlying factors generating “economic dependence” of the

³¹ See *Nationwide Mutual Insurance Company v. Robert T. Darden* 503 US 318; 112 S.Ct. 1344 (1992). (“Darden”).

³² 490 U.S. 730, 751-52 (1989). Darden was a case involving issues of entitlement to employer benefits, while the *Community for Creative Non-Violence* case concerned copyright protection.

³³ See Mitchell Rubinstein, *Employees, Employers, and Quasi-Employers: An Analysis of Employees and Employers Who Operate in the Borderland Between an Employer-And-Employee Relationship*, 14 U. OF PENNSYLVANIA JOURNAL OF BUSINESS LAW 605(2012), at 652.

³⁴ See Rubinstein, *Id.*, at 619-624.

³⁵ Darden, *supra* note 31.

³⁶ See the decision of the U.S. Supreme Court in *NLRB v. Hearst Publications, Inc.*, 322 U.S. 111 (1944). Rubinstein notes that since the Court in this case also referred to “underlying economic facts” and “economic relationships”, the line between this test and the economic realities test is “blurred”, to the extent that some commentators simply refer to this approach taken in *Hearst* as the economic realities test. See Rubinstein, *supra* note 33; Noah D. Zatz, *Beyond Misclassification: Tackling the Independent Contractor Problem without Redefining Employment*, 26 ABA J.LAB. & EMPL. L. 279 (2011).

worker upon the entity.³⁷ While there is some uncertainty and debate about the precise scope of this test and the degree of substantive difference between it and the general common law agency test, it is fair to say that this approach is considered to be a relatively more *expansive* concept of employee status.³⁸ The so-called “hybrid” test is said to combine the common law and economic realities test and attempt to steer a middle ground.³⁹ Here, the court gives significant weight to both indicia of control, and economic dependence.⁴⁰

Since the development of the alternative tests has to a large extent been driven by the question of differentiating employees from workers who are not employees of any employer (i.e. independent contractors) some of the unique aspects of these alternative tests are less relevant in understanding U.S. employer status rules with respect to triangular employment.⁴¹ In any event, the U.S. Supreme Court in *Darden* effectively *narrowed* the acceptable approach to determining employer status in these contexts, by holding that the common law agency test must be the default approach, unless the underlying statute explicitly specifies an alternative definition of “employee”.⁴²

Overall then, employer status rules in the U.S. in recent decades have shunned a broader purposive approach, favoring a more mechanical one focused on indicators of day to day control over work functions.⁴³ This arguably made it easier, over time, for staffing firms to construct service arrangements under which the staffing firm became endowed with *de jure*

³⁷ One court cited the following as additional factors suggesting dependence: relative investments of the worker and alleged employer, the degree to which the worker’s chance of profit or loss is determined by the alleged employer, skill and initiative required in work performed, and the permanency of the relationship. See *Hopkins v. Cornerstone Am*, 545 F.3d 338, 343 (5th Cir. 2008), *cert. denied*, 129 S. Ct. 1635 (2009).

³⁸ *Darden*, *supra* note 31

³⁹ Deanne M. Mosley & William C. Walter, *The Significance of the Classification of Employment Relationships in Determining Exposure to Liability*, 67 MISS L.J. 613 (1998).

⁴⁰ See Rubinstein, *supra* note 33, at 626-628.

⁴¹ For similar reasons, I have not been concerned with the question of whether the factors involved in the tests for employee status are different from tests employed to determine whether workers are employees of the entity. In other words, this paper ignores the relatively more esoteric question of whether *employer* status may somehow exist in the absence of *any* corresponding *employee* status. See Rubinstein, *supra* note 33, at 632-38.

⁴² See *Darden*, *supra* note 31. As noted earlier, courts have seemingly sanctioned the slightly broader approach of applying the concept of “dependency” under the Fair Labor Standards Act. See *Tony & Susan Alamo Found. v. Sec’y of Labor*, 471 U.S. 290 (1985).

⁴³ Rubinstein, *supra* note 33, 626-628. See also Jeffrey Sack, Emma Phillips and Hugo Leal-Neri, *Protecting Workers in a Changing Workworld : the Growth of Precarious Employment in Canada, the United States and Mexico*, in THE EMPLOYMENT RELATIONSHIP: A COMPARATIVE OVERVIEW, 233-285 (Guiseppe Cassale, ed., 2011).

employer status, in place of the user firm. Lobel similarly argues that over time, staffing industry actors have undoubtedly learned to adjust the factual characteristics and contractual provisions in staffing arrangements, in order to maximize the likelihood of the staffing firm being the *de jure* employer.⁴⁴ Lenz also concurs, noting that through the use of onsite managers or “managed services”, it is usually possible to construct the necessary degree of control in the hands of the staffing firm required for it to hold *de jure* employer status.⁴⁵

Canadian tests for *de jure* employer status also involve a review of numerous relevant factors on a case-by-case basis. In Canada, however, the distinction between the analysis used to determine “employer” status within triangular employment contexts and the general tests for whether “employment” exists (i.e. whether the worker is an employee of *someone*) is somewhat greater than in the U.S. Since there is no Canadian common law recognition of a concept analogous to the U.S. “joint employer” concept (see discussion *infra*) in the backdrop, the analytical approach has generally rather been one of more explicitly striving to determine the so-called “true” employer in the triangular relationship. One classic and commonly articulated test for determining the “true” employer, set out in *York Condominium*⁴⁶, involves identifying and considering each of the following:

- the party exercising direction and control over the employees;
- the party bearing the burden of remuneration;
- the party imposing discipline;
- the party hiring the employees;
- the party with authority to dismiss the employees;
- the party who is perceived to be the employer by the employees; and

⁴⁴ Orley Lobel *The Slipperiness of Stability: The Private Employment Agency and Flexible Work Arrangements*, *Symposium: The Role of Contract in the Modern Employment Relationship*, 10 TEXAS WESLEYAN LAW REVIEW 109 (2003).

⁴⁵ Lenz, *supra* note 12.

⁴⁶ *Labourers’ International Union of North America, Local 183 v. York Condominium Corp.*, [1977] O.L.R.B. Rep. 645.

- the existence of an intention to create the relationship of employer and employee.

Although the concept of “control” has been an important factor in Canadian tests for employer status, additional factors supporting a relatively broader analysis are regularly invoked. In 1997, the Supreme Court of Canada in *Pointe-Claire*⁴⁷ identified similar criteria as those in the York Condominium case in its decision concerning the *Quebec Labour Code* which has slightly different criteria for establishing the identity of the employer. However, the Supreme Court further stated that a *broad* or comprehensive analysis is often required, *looking beyond indicators of control or supervision* (referred to as the “legal subordination” criterion). The Court stated:

“According to this more comprehensive approach, the legal subordination and integration into the business criteria should not be used as exclusive criteria for identifying the real employer. In my view, in a context of collective relations governed by the *Labour Code*, it is essential that temporary employees be able to bargain with the party that exercises the *greatest control over all aspects of their work--and not only over the supervision of their day-to-day work*. Moreover, when there is a certain splitting of the employer's identity in the context of a tripartite relationship, the more comprehensive and more flexible approach has the advantage of allowing for a consideration of which party has the most control over all aspects of the work on the specific facts of each case. Without drawing up an exhaustive list of factors pertaining to the employer-employee relationship, I shall mention the following examples: the selection process, hiring, training, discipline, evaluation, supervision, assignment of duties, remuneration and integration into the business.⁴⁸ [emphasis added]

The Supreme Court of Canada also noted that within the extensive jurisprudence on the question of the true employer, over time certain factors have become more important than others.⁴⁹ The most important goal is to try to gauge which entity has the greatest overall

⁴⁷ [1997] 1 S.C.R. 1015.

⁴⁸ *Id.*, para 48.

⁴⁹ *Id.*. The

control over the employment relationship *in its entirety*.⁵⁰ Overall, while there is much consensus in Canada that “control” remains a very important factor, it is fairly clear that no one set of factors is determinative, and that the approach must be a broad and “purposive” one, designed to ascertain the true overall “substance” of the relationship, implying potentially less focus on surface “form”.⁵¹

Compared to U.S. trends, Canadian adjudicators seem to have embraced the broader, expansive and more “purposive” examination of the “essence” of the relationship, reminiscent of the “economic realities” approach in the U.S. that was rejected by the U.S. Supreme Court in 1990 in *Darden*. This suggests that there are comparably fewer degrees of freedom in the hands of US adjudicators to reject the transfer of employer status from user to client, based on the transfer of day-to-day control functions consciously assigned to suppliers under many staffing arrangements. Employer status, or at least a credible claim of employer status under prevailing rules, has been comparably more easily constructed in staffing arrangements in the U.S. than in Canada. Therefore, to the extent that there are regulatory differentials in either country available to user firms, favoring the use of staffing services based on triangular employment, access to such gains has been comparably greater in the U.S..

This general conclusion may need to be qualified slightly by an examination of the additional rules governing recognition of multiple employer status in certain contexts, so a brief discussion of these is also required. The two most common concepts applied in the U.S. to construct a multiple employer nexus are the “joint employer” and the “single employer” concepts, the application of which typically necessitates rather complex, “fact intensive”⁵² litigation, on an *ad hoc* basis. Although their application in practice has been somewhat inconsistent, and at times seemingly overlapping, they are based on formally separate definitions.⁵³ A single employer refers to situations where “two nominally separate entities are actually part of a single

⁵⁰ It should be noted that precise question in the *Pointe-Claire* case was the identity of the “true” employer for purposes of the collective bargaining regime. As noted, the outcome of employer status tests may often vary across different regimes.

⁵¹ See 671122 Ontario Ltd. V. Sagaz Industries ([2001]2 SCR 1983; Rizzo and Rizzo Shoes (Re) [1998] 1 SCR 27. See also Sack, Phillips, and Leal-Negri, *supra* note 41, at 255.

⁵² *Ling Nan Zheng et al. v. Liberty Apparel Company*, 556 F. Supp. 2d 284 (2008).

⁵³ See Rubinstein, *supra* note 33

integrated enterprise,”⁵⁴ and is commonly applied in the parent-subsidary context. The doctrine is designed to address the “fairness of imposing liability for labor infractions where two nominally independent entities do not act under an arm’s length relationship”.⁵⁵ One approach, developed in the labor relations context, is a four-factor test that emphasizes: 1) whether operations are interrelated, 2) whether common management exists, 3) whether the parties have common ownership or financial control, and 4) whether centralized control of labor relations exists.⁵⁶ By contrast, the “joint employer” concept de-emphasizes the question of whether the nominally separate organizations are economically integrated, involving common ownership and/or management. Rather, this test focuses more simply on whether both parties “share or codetermine those matters governing the essential terms and conditions of employment....To establish joint employer status there must be a showing that the employer meaningfully affects matters relating to the employment relationship such as hiring, firing, discipline, supervision, and direction.”⁵⁷

In Canada, the recognition of multiple employers is driven more by statutory provisions specifying, even in very general terms, the factors and contexts that give rise to their recognition, and there is little evidence of such concepts having emerged strictly from the common law.⁵⁸ Further, statutory support for the multiple employer concept varies across provinces, and policy subfields, and statutory support outside of the labor relations regime is very limited.⁵⁹ Further, as Fudge and Zavitz have noted, in Canada, adjudicative recognition of multiple employers has mostly been dependent upon existence of common organization ownership and control.⁶⁰ Thus, the Canadian approach resembles that under the narrower “single employer” concept in the U.S.. This suggests that to some extent, U.S. law provides

⁵⁴ *Asculeo v. On-Site Sales & Mktg, LLC*, 425 F3d 193, (2d Cir 2005), at 198.

⁵⁵ *Dias v. Cmty. Action Project, Inc.* No. 07-CV-5163, 2009 WL 595601, at *2 (E.D.N.Y. , Mar 6, 2009).

⁵⁶ *Paint America Services, Inc.* 353 NLRB No. 100, at *1 (Feb 25, 2009).

⁵⁷ *Laerco Transp. & Warehouse*, 269 N.L.R.B. 324, 325 (1984).

⁵⁸ Despite this being essentially correct, the possibility of the existence of a “common employer” was recognized in the fairly recent decision of the Ontario Court of Appeal in *Downtown Eatery (1993) Ltd. v. Ontario* [2001], 54 O.R. (3d) 161. The court relied heavily upon indicators of common ownership and control within a network of companies with ownership ties, such that this concept more closely resembles the U.S. “single employer” concept.

⁵⁹ Timothy J. Bartkiw, *Baby Steps? Towards the Regulation of Temporary Help Agency Employment in Canada*, 31 COMPARATIVE LABOR LAW AND POLICY JOURNAL 163 (2009).

⁶⁰ See Judy Fudge and Katherine Zavitz, *Vertical Disintegration and Related Employers: Attributing Employment-Related Obligations in Ontario*, 13 CANADIAN LABOUR AND EMPLOYMENT LAW JOURNAL 107 (2006).

adjudicators comparably more degrees of freedom to declare user and staffing firms to be multiple employers.

Overall, this means a slight caveat may be imposed on the conclusion stated above - that U.S. employer status rules overall have provided user firms in the U.S. with comparably greater access to existing regulatory differentials under triangular employment. The caveat is that this assumes that the effect of their being a difference in tests for determining “the” employer is not outweighed by the effect of rules addressing the possibility of multiple “employers.” This is arguably a reasonable assumption, since it is fair to say that in both countries, there has remained a deeply engrained policy paradigm favoring the conception of an employer as a unitary, discrete entity.⁶¹

Regulatory Differentials in Canada and the U.S.

This section outlines the existence of certain key regulatory differentials driving triangular employment growth. While it is possible that regulatory differentials providing a range of advantages from triangular employment (to the user firm) may exist under various policy sub-fields, a complete analysis pertaining to all legal subfields of labor and employment law in Canada and the U.S. is beyond the scope of this paper. Instead, analysis here is limited to two key sub-fields: regulation of retirement plans, and the regulation of employer provided health care benefits. Analysis will show that in the U.S., these two subfields contain stark regulatory differentials, absent in Canada, capable of producing concrete, measurable monetary gains from triangular employment for user firms.

The Regulation of Retirement Plans

Neither Canadian nor U.S. law requires employers to provide their workers with retirement/pension benefits. However, aspects of regulation may affect employers’ incentives when deciding whether to provide benefits, the quantity provided, and the distribution of

⁶¹ Judy Fudge, *Fragmenting Work and Fragmenting Organizations: the Contract of Employment and the Scope of Labour Regulation*, 44 OSGOODE HALL L.J. 609 (2006).

benefits. As well, both countries have, for more than a half-century, provided workers with access to public pension programs providing limited retirement-age benefits.⁶²

In 1974, the U.S. federal government adopted a protective regime establishing various minimum standards in administration, disclosure and content controls in the Employee Retirement and Income Security Act (ERISA),⁶³ which regulated (albeit to quite different degrees) both “pension”⁶⁴ and “welfare” benefits plans of various sorts. In addition to the “labor law” standards set out in the ERISA regime since 1974, the Internal Revenue Code (“IRC”) also contains various other crucially important components of pension regulation in the U.S., in the form of substantial tax subsidies for “qualified” pensions, along with the myriad of rules determining plan qualification.⁶⁵ Some of ERISA’s rules on vesting, service, benefit accrual requirements, and pension content controls were duplicated in the Internal Revenue Code, imposing them as additional requirements for pension qualification, and hence preferential tax treatment.⁶⁶ The aggregate size of this tax subsidy for qualified private pension plans in the U.S. is huge, in the range of \$100 billion annually,⁶⁷ and thus it is generally recognized that the tax rules have “an enormous influence that largely determines the structure and scope of any employer plan (considered singly) and of the entire employment-based pension and health insurance systems of the United States”.⁶⁸

There are three aspects of the preferential treatment flowing from plan qualification under the IRC: the employer may claim the cost of the plan benefit as a tax deduction;⁶⁹ earnings on the

⁶² The Canada Pension Plan is available in Canada, while in the U.S. retirement benefits are available under the Social Security system.

⁶³ P.L. 93-406, 88 Stat. 829 (Sept. 2, 1974).

⁶⁴ The definition of a pension plan under ERISA is quite broad, and is broader than the meaning of a pension plan under the Internal Revenue Code. Under ERISA, a pension plan includes the plans covered by the tax definition of pension plan, plus most profit-sharing, stock bonus, and annuity plans. See PETER J. WIEDENBECK, *ERISA: PRINCIPLES OF EMPLOYEE BENEFITS LAW* (2010), at 6.

⁶⁵ I.R.C. § 401(a).

⁶⁶ The PBGC termination insurance system contained within ERISA was the main exception. See WIEDENBECK, *supra* note 64, at 288. Note also that while some of ERISA is reproduced in the tax code, the opposite is not generally true, in that the I.R.C. rules on tax qualification, such as the non-discrimination measures, are not part of ERISA.

⁶⁷ *Id.*, page 21.

⁶⁸ *Id.*, page 5.

⁶⁹ The employer may claim up to 25% of aggregate employee compensation as defined under IRC § 404 and 401(a)(17).

pension trust funds are exempt from taxes until distributed⁷⁰; and covered employees do not have to pay income tax on the employer's contribution to the plan.⁷¹ The IRC "exclusive benefit rule" requires that funds must be held in trust for exclusive benefit of "employees"⁷² and their beneficiaries, and thus the common law test for "employee" is an important concept in this area.

Given the significant size of the tax subsidy provided to private pension plans, the Internal Revenue Code has also for a long time contained provisions designed to encourage a more egalitarian distribution of retirement benefits than what would otherwise occur. In this vein, U.S. tax law has linked qualification of retirement plans to satisfaction of certain egalitarian principles of "non-discrimination" in coverage and benefits.⁷³ The Revenue Acts of 1938 and 1942 imposed certain basic requirements that qualified plans could not discriminate in favor of "highly compensated employees" (HCEs). In 1942, Congress began to close the "loophole that permitted discriminatory plans" by adopting legislation that "disqualified pension plans that discriminated in favor of officers, shareholders, supervisors, or highly compensated employees."⁷⁴ In 1974, Title II of ERISA amended the IRC in various ways, including the adoption of rules aimed at preventing the skirting of existing non-discrimination provisions through creative (re)arrangements in corporate structure.⁷⁵

⁷⁰ The exception here is where plans are structured as so-called "Roth 401(k) plans", in which taxes are paid up front and there is no tax at distribution. See IRC 402A.

⁷¹ To the extent the employee takes a distribution from a defined contribution plan, like a profit sharing plan, they do pay income taxes when they take a distribution. For a brief overview of ERISA and of the preferential tax treatment of employer plans, see PATRICK PURCELL AND JENNIFER STAMAN, SUMMARY OF THE EMPLOYEE RETIREMENT INCOME SECURITY ACT (ERISA) (2009).

⁷² I.R.C. § 401(a). In other words, employers may not include workers in their plans that are not their common law employees. See Darden, *supra* note 31.

⁷³ PURCELL AND STAMAN, *supra* note 71.

⁷⁴ Jeannette M. Arlin, *Pension Plans and the Employee Leasing Provision: A Proposal for Clarifying Change*, 53 GEORGE WASHINGTON LAW REVIEW 852, at 857.

⁷⁵ *Id.*, at 858. For example, all employees of a commonly controlled group of legally distinct organizations must be treated as being employed by a single employer. In the 1980's Congress also passed legislation recognizing "affiliated service groups" as a single employer for the purposes of plan qualification testing. This was a response to the increasing practice of professional service firms incorporating their individual members and substituting these corporations as partners in the larger organization, enabling each individual corporation to sponsor its own separate retirement plan, potentially solely for its professional employees.

The various IRC pension plan qualification and non-discrimination rules may be conceived of as an important set of contingent regulatory differentials in the U.S. They allow for differences in regulatory effect – different plan qualification outcomes and resulting (and potentially very large) monetary consequences - under direct and triangular employment in various contexts. Staffing services emerged as a tool in accessing these gains. Initially, the IRS applied the traditional common law tests for employer status to scrutinize the “legitimacy” of the growing number of staffing arrangements.⁷⁶ This approach seemingly left space for the construction of staffing arrangements resulting in the transfer of employer status to the staffing firm, in a significant range of contexts. As Cohen notes:

“In these rulings, the IRS typically found a common-law employer-employee relationship to exist between a leasing organization and its leased employees where the organization operated in a manner which was similar to the organization described in [Revenue Ruling 75-41] (e.g., the leasing organization had the right to control and discharge the employees and was in charge of recruiting, hiring and evaluating employees. Notably, many of the rulings found an employer-employee relationship between the leasing organization and the leased employees notwithstanding the organization’s practice of hiring former employees of the subscriber.”⁷⁷

Subsequently, Congress enacted the Tax Equity and Fiscal Responsibility Act of 1982 (“TEFRA”), in order to clarify – and tighten - the application of IRC plan qualification rules in staffing service contexts. TEFRA added section 414(n)(2) to the IRC, which defined the concept of a “leased employee.” TEFRA required that all “leased employees” were to be treated as employees of the “recipient” (user) firm, unless the leasing organization satisfied a safe harbor test by providing a minimum level of pension benefits to the leased employees. Under TEFRA, a “leased employee” was defined as:

“...any person who provides services to the recipient if

⁷⁶ Sheldon S. Cohen, *Employee Leasing: Industry in a Time of Change*, 20 FORUM 657 (1985).

⁷⁷ *Id.*, p.3.

- (A) such services are provided pursuant to an agreement between the recipient and any other person (in this subsection referred to as the “leasing organization”),
- (B) such person has performed such services for the recipient (or for the recipient and related persons) on a substantially full-time basis for a period of at least 1 year,⁷⁸ and
- (C) such services are of a type historically performed, in the business field of the recipient, by employees.”⁷⁹

This language in TEFRA contained multiple ambiguities. One significant issue was the relationship between the traditional common law concept of an employer-employee relationship and this new concept of a “leased employee”. Did one concept preclude, or alternatively presuppose, the existence of the other?⁸⁰ To supposedly aid in the interpretation of this subsection, in 1984 Congress passed a slight revision to 414(n)(2), changing a portion of the language in the s. 414(n)(2) from “any person who provides services to the recipient” to “any person *who is not an employee of the recipient and* who provides services to the recipient”.⁸¹ Although arguably still ambiguous since the word “employee” continued to be undefined, this revised language seemingly suggested that workers would thereafter be treated as “employees” of the recipient/user under the IRC plan qualification provisions to which 414(n)(2) applied, in two separate ways. First, they would be treated as employees wherever traditional common law tests suggested they were employees. Secondly, *even* where they were *not* found to be employees of the recipient/user under the common law, they were to be deemed employees of the user/recipient where the requirements of 414(n)(2)

⁷⁸ Note that this component of the test for “leased employee” is separate from the more general provision that any employee may be excluded from an ERISA qualified pension plan on the basis of service, if the employee has not yet completed a year of service. A year of service is defined as a 12 month period during which the employee has worked at least 1000 hours. See ERISA § 202(a)(1)(A). This more general, latter rule may be conceived of as creating a regulatory incentive in favor of temporary employment, while not necessarily in favor of triangular employment.

⁷⁹ IRC, § 414 (n) (2).

⁸⁰ See Arlin, *supra* note 74. Arlin cites this as a significant ambiguity despite the fact that at the time, IRS Question and Answer Guidelines stated that a common law employee of the recipient “is an employee of the recipient for all purposes and without regard to the provisions of section 414 (n). Notice 84-11, 1984-2, C.B. 269, 270.”

⁸¹ Tax Reform Act of 1984, Pub. L. No. 98-369, § 526 (b)(1), 98 Stat. 494, 874 (codified as amended at 26 U.S.C.A. § 414(n)(2) (West Supp. 1985)).

were satisfied. Although some ambiguity continued to linger over this relationship between the common law tests and s 414(n)(2), this interpretative approach was eventually confirmed by the U.S. Court of Appeals (9th Circuit) in its 1998 decision in *Burrey v. Pacific Electric & Gas*.⁸²

Beyond the question of the relationship between s. 414(n)(2) and the common law definition of employee, additional ambiguity embedded in this provision remained salient for some time, particularly with respect to subsection (c).⁸³ That is, it was quite unclear how the requirement that the “services are of a type historically performed, in the business field of the recipient, by employees” was to be applied. First, there was no clear understanding of the threshold level of regularity that was meant by work being “historically performed” by employees. Arlin notes that proposed Treasury regulations in the early 1980’s

“consider services to be historically performed by employees in a recipient’s service organization or business field if it was ‘not unusual’ for employees to perform the services. This language implied that if services are performed perhaps thirty percent of the time by unleased employees, it is ‘not unusual’ for employees to perform those services. The IRS may, therefore, treat a leased employee as an employee under section 414(n), even though he provides services that are predominantly provided by leased employees in the relevant business field.”⁸⁴

Further, the scope of activities that should be deemed to constitute the “business field” within which comparison must take place was uncertain, and this could significantly affect the application of the provision. These significant ambiguities in the interpretation of IRC 414(n)(2) remained intact until an important revision to this section occurred in 1996, discussed *infra*. Importantly, each of these ambiguities in the definition, which remained intact throughout much of the 1980’s, may be understood as having produced a relatively more *expansive* conception of a “leased employee,” as of 1982. This expanded the potential

⁸² 159 F.3d 388.

⁸³ See Arlin, *supra* note 74 for an analysis of the various interpretive issues under this section that persisted throughout the 1980’s and much of the 1990’s.

⁸⁴ Arlin, *supra* note 74 at 867.

scope of enforcement of s 414(n)(2), and thus effectively *narrowed* the available space for using staffing services to access the regulatory differentials in the IRC plan qualification and non-discrimination rules.

The three subsections in IRC 414(n)(2) are conjunctive, meaning that they all must be satisfied prior to supplied workers being deemed “leased employees” and counted as the user’s employees under the pension qualification tests. The requirement in subsection (B) that the definition of a “leased employee” would not be applied to workers unless they have supplied services to the recipient on a “substantially full-time basis for a period of at least 1 year” has from the outset narrowed the scope of the provision, expanding the possibility of using staffing services to access IRC-based regulatory differentials, where it is feasible to utilize supplied workers on either a temporary (less than 12 months) or part-time (or less than “substantially full-time”) basis. This subsection mirrors the more general qualifying rule allowing for exclusion of workers from plan participation, where they work on either a temporary (less than 12 months) or part-time basis (the “1000 hour rule”).⁸⁵

In 1986, Congress revised the underlying IRC plan qualification rules themselves, adopting stricter coverage tests for retirement plans beginning in 1988.⁸⁶ Lenz summarized the new non-discrimination rules as follows:

“A plan must cover (1) a percentage of rank-and-file employees equal to at least 70% of the percentage of higher paid employees benefited, or (2) a nondiscriminatory classification of employees based on objective standards and provide lower-paid employees an average benefit that is at least 70% of the average benefit provided to higher-paid employees... employers can no longer provide qualified retirement benefits

⁸⁵ I.R.C. § 202 (a)(1)(A).

⁸⁶ 1986 Tax Reform Act, Pub.L. 99–514, 100 Stat. 2085.

simply by covering a nondiscriminatory classification of employees (e.g. full-time salaried employees).”⁸⁷

This prohibition of discrimination in favor of highly compensated employees applies with regard to coverage, amount of benefits, and availability of benefits, and applies to both “defined benefit” and “defined contribution” plans.⁸⁸ A highly compensated employee is defined as any employee who owns 5% or more of the firm, or whose compensation in 2009 exceeded \$110,000 (indexed to inflation).⁸⁹

In addition to these changes, the 1986 Tax Reform Act also contained radical reductions in income tax rates, particularly on higher income earners, with the top bracket marginal tax rate falling from 50 to 28 percent. Together, these two reforms embodied a contradictory tension. The new non-discrimination requirements tightened and *increased the redistributive dimension* of plan qualification rules. So, on the one hand, the new rules imposed a relatively more egalitarian standard of redistribution, via pension coverage and distribution, from higher to lower income earners. On the other, however, the reduction in the underlying marginal tax rate effectively reduced the size of the “subsidy” provided to high income earners, in the form of tax savings that comes from being a participant in a qualified (read: egalitarian) pension plan. The higher the underlying marginal tax rate on income, then the higher the value of the tax subsidy under plan qualification. Effectively, the higher the underlying marginal tax rates on high income earners operating in the background within this system, the greater the space for a net gain to high income earners from participating in qualified plans, even after the redistributive effect of the plan qualification and non-discrimination rules. Thus, while the 1986 tax reforms imposed relatively more egalitarian qualification rules, the simultaneous,

⁸⁷ Lenz, *supra* note 12, at 26. Precise details of the coverage tests are in IRC § 410(b). The definition of the concept of “highly compensated employee” is provided in IRC § 414 (q). For a much more detailed overview of the specifics of the non-discrimination tests, see WIEDENBECK, *supra* note 64, pp 306-332.

⁸⁸ See PURCELL AND STAMAN, *supra* note 71 page 50.

⁸⁹ As well, “an employer may elect to count as HCEs only employees who rank in the top 20% of compensation in the firm, but must include anyone who owns 5% or more of the company.” For a more detailed summary of the various tests, including tests relating to “actual contribution percentages” measuring the relative contribution rates for employee 401(k) plans, see PURCELL AND STAMAN, *supra* note 71, page 51.

dramatic cut in marginal tax rates on higher income earners reduced the overall amount of value available for redistribution under plan participation, leaving much less residual value to induce/coerce continued participation in egalitarian plans.⁹⁰

The overall combined result is that post-1986, there was likely a substantial decline in willingness of employers, and high earning employees, to participate in egalitarian qualified pension plans, increasing pressure on employers to reduce (or discontinue) pension benefits provision altogether, and/or to develop strategies for avoiding the redistributive effects of the plan qualification rules. In other words, these developments expanded the size of regulatory differentials potentially provided by triangular employment. Increasingly, with further legal developments working in tandem, staffing services became an instrument to access these gains. The pressure to access these regulatory differentials became increasingly salient post-1986, and other developments increasingly liberalized user firm access to them.

The first of these subsequent developments occurred in 1992 when, as discussed earlier in this paper, the U.S. Supreme Court issued its decision in *Darden*. To the extent that this decision narrowed the space for broader interpretive approaches to determining employer status, it further expanded the space for constructing staffing arrangements enabling the transfer of *de jure* employer status to staffing firms. As noted already, as a result of this Supreme Court ruling, a similar interpretive shift could reasonably be assumed to have occurred subsequently in the application of the common law test within the taxation field.

An additional significant development occurred in 1996, when Congress enacted the *Small Business Job Protection Act*, which further revised the definition of “leased employee” in IRC 414(n)(2) as of Jan 1, 1997, by removing the requirement in subsection (C) that services performed by workers be of the type historically performed by employees in the recipient’s field of business. This removed two arguably ambiguous aspects of the prior test that had the practical tendency of expanding the scope of application of the “leased employee” concept.

⁹⁰ This insight about the interaction between the marginal tax rate and the degree of coercion that the non-distributive rules embody is from WIEDENBECK, *supra* note 64, at 306-311.

In the new subsection (c), this element of the test was replaced with the requirement that “such services are performed under *primary direction or control* by the recipient” (emphasis added). This narrowed the definition of a “leased employee”, thus narrowing the circumstances in which supplied workers would have to be included in user firm plan qualification tests. As Lenz confirms: “This test [the previous subsection (C)] was widely criticized as being too broad in its application. The control test significantly narrows the scope of the leased employee rules”.⁹¹ Logically, the “leased employees” test only applies to those workers who were not already deemed employees of the user under the common law, and this interpretive logic was confirmed in the case of *Burrey v. Pacific Electric & Gas*. But as we have already seen, the U.S. common law employer status tests *already* placed primary emphasis on indicators of control. Therefore, it is hard to even conceive of the particular kinds of factual circumstances in which workers deemed staffing firm employees (and not recipient/user firm employees) under common law tests that are based primarily upon indicators of control, would then subsequently nevertheless be deemed to be “leased employees”, given that the latter test now required that “*primary direction or control*” reside with the user/recipient.⁹² It would seem then that the 1996 statutory revision was akin to *repealing* the requirements in subsection (c) that had previously enabled the leased employee concept in s. 414(n)(2) to function as a broader test, to capture staffing arrangements *beyond* those caught by existing common law. Again, this is in addition to the fact that, as discussed above, the common law itself had already evolved in a manner liberalizing the ability to use of staffing arrangements to access regulatory differentials in retirement plan regulation in the IRC.

Although staffing firms have sometimes faced a relatively heavier burden of proof on the question of “control” with respect to certain classes of workers (e.g. office and clerical service workers),⁹³ in general the new definition of a “leased employee” in s. 414(n)(2) clearly favored

⁹¹ See Lenz, *supra* note 12 at 28.

⁹² Additionally, as Lenz points out, in the area of employee benefits, the concept of joint employment is generally not recognized, and thus the interpretive approach focuses on selecting the “true” common-law employer.

⁹³ *Id.*

staffing arrangements in which day-to-day direction and control was in the hands of the staffing firm. Further, Lenz also points out that even clients using “professional” workers supplied by a staffing firm, are also likely able to avoid the scope of application of 414(n)(2). Here, Lenz notes that various kinds of professional workers (e.g. computer programmers, system analysts, engineers, doctors, lawyers, accountants, actuaries, etc.) will generally not be considered “leased employees”:

“if they regularly use their own judgment and discretion on matters of importance in the performance of their services and are guided by professional, legal, or industry standards. They do not have to be counted by the client, even though the staffing firm does not closely supervise them on a continuing basis and even though the client requires their services to be performed on site and in accordance with client-determined timetables and techniques.”⁹⁴

While it may be that professionals are more often likely to be “highly compensated employees,” staffing arrangements involving professionals are no less relevant as a potential tool in avoiding coverage requirements, since the exclusion of highly compensated employees (and thus their pensions) from the calculations may in various contexts improve user firms’ ability to meet the non-discrimination rules, preserving the tax subsidy for the employer and high income earners, while avoiding the provision of more egalitarian pension benefits.

Further, the “safe harbor” rules, which allow for exclusion of “leased employees” where a pension meeting certain alternative tests is provided by the staffing firm,⁹⁵ do not significantly

⁹⁴ Lenz, *supra* note 12.

⁹⁵ One aggressive PEO industry practice that sought to push the boundaries of the “safe harbor” rules seems to have been the practice of providing client employees with retirement benefits provided under a so-called “single employer” plan provided solely by the PEO, even in contexts resembling the classic “payrolling” structure (in which the workers remain common law employees of the client) that purported to exempt the employees from the client’s IRS pension coverage calculations. The IRS provided a protocol for plan re-structuring, and clarified the tax administrative options available to PEO’s providing such plans, in its Revenue Procedure 2002-21, which included the options of terminating the plan, transferring its assets to a client plan, or creating a “multiple employer” plan. In the latter case, the employees of each client are tested separately, and clients have to include supplied workers in their pension coverage calculations.

alter the analysis or conclusions of this section, given that the nature of the rules has almost completely eliminated the existence of qualified “safe harbor” plans in the U.S.⁹⁶

The overall trajectory described here can be summarized as follows. Various retirement plan qualification and non-discrimination rules in U.S. pensions law have for decades formed an important set of regulatory differentials likely stimulating triangular employment in the U.S.. Under 1986 reforms, the gains from accessing these differentials expanded. Yet further developments in both common law employer status rules, and revisions to the particular “leased employee” rules, liberalized user firm access to these differentials through staffing services.

By contrast, Canadian law regulating employer-based pension plans does not contain any set of rules that may be conceived of as being analogous regulatory differentials like those in U.S. tax law⁹⁷ that might theoretically stimulate triangular employment growth. Pension standards rules in provincial legislation do not generally mandate the provision of any sort of employer minimum plan coverage, nor impose analogous qualification rules concerning distribution amongst different groups of employees. The only weak analogue in Canadian pension regulation might be certain rules specifying that *within classes* of employees, which classes employers are essentially free to structure in their plans as they see fit, employees must be treated “equally” in certain regards. However, since there are essentially no rules requiring equitable treatment as between different classes, and there is also freedom in the creation of

⁹⁶ Lenz summarizes the effect of these provisions as follows: “Employees will not be treated as leased employees for pension plan purposes if they participate in a safe harbor pension plan provided by the leasing organization that meets the following conditions: The leasing organization must contribute at least 10% of the employee’s compensation to the plan. The employee must be 100% vested in the contribution. In general, all leasing organization employees who provide services to clients must participate in the plan without any waiting period. This provision prevents a leasing organization from providing safe harbor plans that cover only the employees assigned to certain clients. If for any plan year, leased employees constitute more than 20% of an employer’s non-highly compensated workforce, all of the leased employees furnished to the recipient will have to be counted, notwithstanding the existence of a safe harbor plan. Of course, a safe harbor pension plan does not relieve recipients of the obligation to count leased employees for any other benefits plan subject to coverage testing. Few, if any safe harbor plans exist.” See Lenz, *supra* note 12, at 29.

⁹⁷ More precisely, it can be said, at least, that it does not contain any “formal” or “contingent” differentials, two of the three categories in this typology. See Bartkiw, *supra* note 8. Trying to grasp the precise nature of informal differentials in this (or any) area of regulation arguably requires other methodological approaches.

alternative plans for different classes, these constraints would seem to barely, if at all, restrict employer freedom in allocation of pension benefits, and thus would not amount to regulatory differentials as conceived herein.⁹⁸ As well, Canadian pension law generally does not utilize analogous sorts of “headcount” rules, where regulatory effect is conditioned by certain counts of employees, nor measurements of treatment between different employee groups.

Overall then, comparative analysis of regulation in this subfield reveals that for several decades there has existed significant regulatory differentials stimulating triangular employment in the U.S. that are absent in Canada, and that beginning in 1986, law reform seems to have on the one hand exacerbated the magnitude of these regulatory differentials, while on the other liberalizing user firm access to them via staffing services. This is highly consistent with the observed patterns of triangular employment growth reviewed above.

The Regulation of Employer Sponsored Healthcare Benefits

U.S. law also does not require employers to provide employees with health benefits. However, employment relations in the U.S. are influenced by the absence of universal health care, with the allocation of healthcare resources being relatively more determined by market mechanisms and private insurance schemes than in many other countries, including Canada. The U.S. system relies substantially upon private employer provision of health insurance coverage, along with forms of employment-based regulation, to achieve healthcare policy goals.⁹⁹ However, even the U.S. system ought to be understood as being at most *semi*-private in nature, given the preferential tax treatment (i.e. subsidy) that it involves. Recent estimates of the U.S. tax expenditure associated with exclusion of employer contributions towards medical insurance

⁹⁸ Some provinces have rules that prevent discrimination against part-time workers, which are similarly, not directly relevant. Among other rule categories, there is some emphasis placed on capping the size of tax savings that may be captured with respect to benefits provided to each *individual* employee, such as maximum contribution limits and related rules. In Canada, there is a Registered Retirement Savings Plan contribution limit of 18% of an individual employee’s income, up to a maximum aggregate contribution of \$22,970. In the U.S., analogous rules exist in IRC § 415. For defined benefit plans, there are also rules limiting the maximum pension that may be paid to an individual employee under such plans. None of these sorts of rules would seem to embody regulatory differentials favoring triangular employment.

⁹⁹ Medicare and Medicaid are available for the elderly and poor, respectively. In 2007, 61% of non-elderly Americans received health insurance coverage through an employer-sponsored program. See Henry J. Kaiser Family Foundation, *Health Insurance Coverage in America, 2007*, at 1, cited in WIEDENBECK, *supra* note 64 at 383.

premiums and medical care range from \$137-155 billion in 2010,¹⁰⁰ making health care benefits the most costly of all types of employer welfare benefits.¹⁰¹

While the tax preference given to retirement benefits is tax deferral, employer healthcare expenses are granted an outright tax exemption in the current year.¹⁰² Further, tax treatment of *employer-sponsored* health benefits is comparably favorable to other health care financing arrangements like individual self-insurance,¹⁰³ reinforcing the historical practice in the U.S. of using employment as a key platform for health care governance.¹⁰⁴

This rather deep policy preference in the U.S. for employer provision of health care insurance coincides with a number of related dynamics in the U.S. market for “fully insured” health plans (i.e. plans purchased by employers from insurers) that are important for understanding the nature of the regulatory differentials in this field. The market for employer health insurance plans has historically been quite influenced by the fact that there is great variation in employer sizes as well as quasi-fixed costs for insurers in the sale, service and administration of each separate employer health plan. Thus, significant economies of scale exist, enabling larger firms to reduce their costs, while smaller firms pay substantially more, per worker.¹⁰⁵ In addition, the U.S. government also became increasingly concerned that small employers were being disproportionately discriminated against, or otherwise mistreated by insurers. As a result, insurance law in the U.S. has for several decades bifurcated the market for employer health

¹⁰⁰ WIEDENBECK, *supra* note 64, at 7.

¹⁰¹ *Id.*, at 6.

¹⁰² *Id.*, at 384.

¹⁰³ Here both income and payroll tax advantages work to favor employer sponsored plans. See WIEDENBECK, *supra* note 64, at 387-9. As well, preferential tax treatment in favor of employer provision also applies with respect to “income replacement” or “disability insurance” benefits. See WIEDENBECK, *supra* note 64 at 398.

¹⁰⁴ As healthcare costs have risen and cost-sharing arrangements have evolved, many employees have been increasingly required to contribute portions of the total costs of coverage. While the various rules are complex, in some cases this has led to a reduction in the tax advantage overall, since employee expenditures generally received less favorable treatment. However, certain other arrangements may allow for employee contribution to be structured as part of a so-called “cafeteria plan”, such as a “flexible spending arrangement”, which may largely preserve preferential tax treatment for employee expenditures as well. See WIEDENBECK, *supra* note 64 at 390-2. Beginning in 2013, the PPACA limits the maximum amount that an employee can elect to contribute to a health care FSA to \$2,500 per year.

¹⁰⁵ Interviews with key informants from industry, and a policy consultant from the National Association of Insurance Commissioners confirm that (outside of PEO arrangements) small employers continue to face substantially higher costs of insuring their workforces on a per employee basis.

insurance into two notional product markets, namely “small group” and “large group” markets, and has imposed a relatively greater regulatory burden on insurers in the small group market.¹⁰⁶ This regulatory approach was intensified in 1996 with the passage of the Health Insurance Portability and Accountability Act (“HIPAA”)¹⁰⁷, intensifying regulatory requirements, disproportionately directed towards small group plans.¹⁰⁸ In this context, it is not surprising that larger employers in the U.S. have a much higher healthcare benefits coverage rate.¹⁰⁹

Given this background regulatory context in the U.S., there are significant latent economies of scale that are at least potentially¹¹⁰ available for realization through coordinated systems of insurance purchasing/provision across multiple smaller firms. Staffing firms, particularly those more commonly identified as PEOs, have been emerging as an increasingly popular tool for this task. Using the economies of scale from having multiple clients, PEOs may be able to purchase health insurance plans covering each client’s “worksite employees”, and provide clients’ with greater insurance purchasing power.¹¹¹ Indeed, this healthcare insurance pooling function forms one of the key stated grounds for why the PEO industry embraces the concept of “co-employment”, and struggles to preserve the PEO’s status as “an” (if not at times “the”) *de jure* employer of its clients’ workforces.¹¹² To see why this is so, further understanding of background regulation in this area is helpful.

Employer provided health insurance plans are a form of “welfare plan” regulated under ERISA, a federal enactment, which largely pre-empts state regulation of employer sponsored health

¹⁰⁶ While there are some variations, the most commonly used definition of a “small group” policy is one that covers from 2-50 employees, while a “large group” policy covers greater than 50 employees. Key informant interview, National Association of Insurance Commissioners.

¹⁰⁷ Pub.L. 104–191, 110 Stat. 1936, enacted August 21, 1996.

¹⁰⁸ Under HIPAA, small group plans face certain additional “mandates” or mandatory benefits; limits on pre-existing condition exclusions; and rules concerning guaranteed issue and renewal.

¹⁰⁹ MARK MERLIS, *THE AFFORDABLE CARE ACT AND EMPLOYER-SPONSORED INSURANCE FOR WORKING AMERICANS* (2012).

¹¹⁰ That is, to the extent legally allowed.

¹¹¹ Consistent with this, NAPEO claims that the average workforce size of PEO clients in the U.S. is approximately 19 employees. See NAPEO, 2009 Financial Ratio and Operating Statistics Survey. Note however that there is some concern about the reliability of measures of size of client firms measured by employee counts. For example, it is not clear in such surveys whether client self-reported headcounts include or exclude the very employees supplied by (or “co-employed” by) the staffing firm. See also Lombardi and Ono, *supra* note 13.

¹¹² See Diane Stanton, Rufus Wolff, and William J. Schilling, *Employer Status and the PEO Relationship*, 6 NAPEO LEGAL REVIEW 1 (2008).

insurance. However, state-level insurance regulation also applies, addressing insurance contracts and the relationship between the insurer and insured. The dividing line between state and federal authority in this area is fairly complex. So called “self-funded” schemes are excluded from the federal preemption, while “fully-insured” arrangements more clearly fall under state regulation.¹¹³ Further, since 1983, ERISA also exempted from preemption plans defined as “multiple employer welfare arrangements” (“MEWAs”), reinforcing state-level authority to regulate these particular insurance arrangements.¹¹⁴ With certain exceptions, ERISA defines a MEWA rather broadly to be an

“employee welfare benefit plan or any other arrangement ... established or maintained for the purpose of offering or providing any benefit described in paragraph 1 [welfare benefit plans] to the employees of two or more employers, including one or more self-employed individuals, or to their beneficiaries...”¹¹⁵

Although a plain reading of these provisions would seem to suggest that a PEO-constructed health plan arrangement, in which the PEO purports to sponsor a health insurance plan for the employees of its multiple clients, would constitute a MEWA, the PEO industry has long struggled to resist this classification. Instead, the industry has sought to have PEO health plans recognized as being “single employer” plans, regulated by ERISA and not falling under the scope of state MEWA regulation. In terms of the theoretical framework used here, the different regulatory systems for single and multiple employer plans create regulatory differentials favoring triangular employment, particularly for small/medium sized firms.

A major challenge to the industry is that the federal Department of Labor has consistently applied the traditional common law employer status rules in this context, and has thereby typically concluded that PEO plans fall within the definition of MEWAs set out in ERISA.¹¹⁶

Varying somewhat with the specific context, being designated a MEWA would almost always

¹¹³ WIEDENBECK, *supra* note 64, pp. 204.

¹¹⁴ Public Law 97-473.

¹¹⁵ 29 U.S.C. § 1002 (40)(A).

¹¹⁶ U.S. DEPARTMENT OF LABOR, MULTIPLE EMPLOYER WELFARE ARRANGEMENTS UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT (ERISA): A GUIDE TO FEDERAL AND STATE REGULATION, available at <http://www.dol.gov/ebsa/Publications/mewas.html>.

result in a PEO-sponsored health plan arrangement facing a greater regulatory burden, oversight, and typically cost, resulting from state MEWA regimes.¹¹⁷ This generates significant pressure on PEOs to try to function at the margin of MEWA regulation, and to try to structure arrangements, in the shadow of the normal common law employer concept, so as to defend the position that they are (at least) “an” employer of the worksite employees, and that insofar as all client workforces *share one* employer (the PEO), their plans ought to be deemed single employer plans. Towards this goal, NAPEO has pro-actively fashioned some additional insurance oversight rules into its “model PEO statute” for which it lobbies at the state level, along with model statutory provisions clarifying that fully-insured PEO plans are to be treated as single-employer plans under state insurance law. Many states have adopted these regulatory compromises promoted by NAPEO.¹¹⁸

Various other aspects of regulation in this field also constitute regulatory differentials. Basic rules governing fiduciary standards, reporting and disclosure requirements, and procedures for appealing denied benefit claims have been in effect in the health policy field, as part of ERISA, since its adoption in 1974. Similar to the approach taken with retirement plans, tax rules relating to health benefit plans largely mirror ERISA’s “labor law” standards on health plan content controls and process requirements. Although over-arching “non-discrimination rules” like those pertaining to retirement plans have not, at least until very recently under PPACA, not been imposed,¹¹⁹ there have been three exceptions to this fact. First, s. 105(h) of the IRC prohibits discrimination in favor of highly compensated individuals under employer “self-insured” plans (in which the employer, rather than an insurer, assumes the risk of benefits costs). Second, where health benefits are offered as an option under the “cafeteria plan” rules, those rules also prohibit discrimination. Third, a final set of rules prohibit contributions to “health savings accounts” in favor of highly compensated employees, without comparable

¹¹⁷ Interview with key informant from National Association of Insurance Commissioners.

¹¹⁸ See Stanton et al., *supra* note 112.

¹¹⁹ PPACA reinstated limited non-discrimination rules for welfare plans starting in 2010 or 2011. See discussion of PPACA *infra*.

contributions to rank and file employees.¹²⁰ Each of these sets of rules is contingent regulatory differentials.

Subsequent legislation created additional regulatory differentials. The Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) added a new Part 6 to ERISA, which included various new rules requiring employers providing health coverage to temporarily *continue* plan coverage for plan participants and beneficiaries in various “qualified events”, which would otherwise result in coverage loss.¹²¹ These qualified events included the death of the covered employee, a reduction in the employee’s working hours, and termination (except in the case of employee gross misconduct). Generally, continued coverage must be the same as that provided to similarly situated employees that have not experienced a “qualified event.”¹²² Notably, COBRA applied these new coverage continuation requirements only to plans maintained by an employer with *20 or more employees*.¹²³ Thus, COBRA’s “headcount” rule and the benefits of avoiding the higher premiums associated with plans caught by COBRA’s extended coverage requirements are contingent regulatory differentials.

In 1996, two other legislative revisions further increased the regulatory burden on employer sponsored health care plans. The Health Insurance Portability and Accountability Act, amended Title 1 of ERISA by limiting the circumstances under which a health plan may exclude a participant with a preexisting condition from coverage,¹²⁴ prohibiting group health plans from basing coverage eligibility rules on certain health-related factors, such as medical history or disability, and prohibiting higher premiums based on such health related factors.¹²⁵ The Mental Health Parity Act (“MHPA”), also adopted in 1996, imposes new rules requiring that plans

¹²⁰ See WIEDENBECK, *supra* note 63, at 395-7. The “leased employee” rules in IRC 414(n)(2) apply to pension plans, life insurance plans, and so-called “cafeteria” plans. To qualify, a cafeteria plan must allow employees to choose from a selection of two or more benefits consisting of cash or qualified benefit plans. See IRC § 125(d)(1).

¹²¹ Time limits for continuation of coverage requirements are contained in 29 U.S.C. s 1162 (2). Purcell and Staman note that under this section the typical requirement is that coverage continue for [up to] 18 months, but may be longer in certain circumstances. See PURCELL AND STAMAN, *supra* note 71, p. 46.

¹²² ERISA 602(1).

¹²³ 29 U.S.C. § 1161, E.R.I.S.A. 601.

¹²⁴ 29 U.S.C. § 1181 (a) (1)-(3). Such exclusions are now no longer permitted under PPACA.

¹²⁵ 29 U.S.C. § 1182(b)(1).

offering mental health benefits must not impose lower annual and lifetime limits placed on medical and surgical benefits. Plans covering employees with 50 or fewer employees are exempt from the requirements of the MHPA, creating yet another additional, albeit minor, contingent regulatory differential.

The recent overhaul of healthcare regulation adopted in The Patient Protection and Affordable Care Act (the “ACA”)¹²⁶ contains three additional new rule categories embodying regulatory differentials, or reinforcing the effect of those already discussed. First, the ACA adds a new section 45R to the IRC¹²⁷ providing a tax credit for employee health insurance expenses of “eligible small employers”, defined as employers with fewer than 25 full-time equivalent employees (“FTEs”), who earn average annual wages of less than \$50,000 per FTE, for whom the employer maintains a “qualifying arrangement”.¹²⁸ The latter is a plan for which the employer pays a uniform percentage of the premium cost for each employee enrolled.¹²⁹

Secondly, the ACA’s “Shared Responsibility” rules impose penalties on large employers, defined as those with 50 or more FTEs, who don’t make appropriate health insurance coverage available to their employees. Such large employers who fail to provide any insurance face a fine of \$2000 per full-time employee in excess of thirty employees.¹³⁰ Alternatively, employers who provide coverage that is inadequate or unaffordable as established by the ACA,¹³¹ are subject to a the lesser of the above fine or \$3000 per eligible employee that instead purchases federally subsidized health insurance on a state health insurance exchange.¹³²

¹²⁶ Pub.L. 111–148, 124 Stat. 119 (2010). The ACA was amended by the Health Care and Education Reconciliation Act of 2010 (“HCERA”), Pub. L. No. 111-152, 124 Stat. 1029 (2010). References to ACA throughout paper refer to the ACA as amended by HCERA.

¹²⁷ Enacted by § 1421 of PPACA.

¹²⁸ I.R.C. 45R(d)(1).

¹²⁹ IRS Technical Release No. 2012-01. , pp. 1-2.

¹³⁰ This fine occurs once one full-time employee purchases federally subsidized insurance on a state health insurance exchange. PPADA s 1513, 10106(3), 124 Stat. 119, 253-56, 910; m

¹³¹ For coverage to be adequate under the ACA, the employee’s premium contributions must not exceed 9.5% of her salary, and the insurance plan must cover 60% of allowable expenses covered by the plan. See ACA § 1401(a) 124 Stat. 119, 216-17; HCERA § 1001 (a) (2) (A), 124 Stat. 1029.

¹³² IRS Technical Release No. 2012-01. , pp. 1-2. See ACA, § 1513, 10106 (e) 124 Stat. 119, 253-56, 910; HCERA s 1003, 124 Stat. 1029, 1033 (2010).

Thirdly, ACA extends the scope of plans covered by “non-discrimination” testing rules. While previously the only plans affected by non-discrimination rules were self-insured plans (under I.R.C. s. 105(h)) and cafeteria plans, PPACA prohibits discrimination in provision of health benefits in favor of highly compensated employees, by applying rules similar to those in I.R.C. s. 105(h)¹³³ to (non-grandfathered) fully-insured group health plans as well. These new provisions in PPACA create and/or reinforce various incentives for user firms to seek to adjust their employee headcount and/or employer status in various contexts.

This historical background structure of U.S. regulation of employer-sponsored health insurance can thus be seen as having embodied a plethora of regulatory differentials favoring triangular employment in various contexts. Indeed, similar to the *modus operandi* of regulatory differentials in the area of retirement plan regulation, the gains under triangular employment are concrete, measurable, monetary gains. The historical trajectory of regulation suggests that over the time period reviewed, the scope of regulatory differentials in the U.S. in this field has expanded.

Canadian health policy is substantially different in nature, given the existence of universal public health care provision in every province. In this context, although some employers provide extended health related benefits of various sorts that provide coverage beyond what is provided by the public system,¹³⁴ employer provided health care plays comparably minor role in the health care system overall.

Indeed, given state provision of health care as backdrop, regulation of employer sponsored health care benefits is quite minimal in Canada. The only comparable laws in Canada that may be conceived as embodying any regulatory differential favoring triangular employment are certain rules within payroll tax systems established towards financing the general healthcare system. In some cases, tax rates are levied in a progressive manner, with higher rates being levied on larger employers, defined by payroll size. However, using the Ontario rules as an example for analysis, there is very little reason to believe these rules would have a significant

¹³³ See Public Health Service Act § 2716.

¹³⁴ Dental plan coverage is one of the most common examples of such benefits.

effect on triangular employment growth. The Ontario Employer Health Tax Act imposes a levy on the aggregate payroll of employers, with differential treatment being applied only to the first \$400 thousand in payroll. Thus, differential treatment only occurs at very small payroll levels, affecting only very small employers. “Eligible employers” under the Act may be entitled to an exemption on this first \$400 thousand, while others face a progressive scale of tax rates ranging from .98% on the first \$200 thousand to 1.95% on payroll above \$400 thousand. Here, there would seemingly be very few circumstances in which user firms would ever save substantially on employer status transfer, and furthermore the pooling of workers into being employees of a staffing firm (assuming this could be constructed given the broader employer status rules in Canada) would in most cases result in the staffing firm having a payroll above the \$400 thousand threshold, which cost would presumably be passed on to the user in any event.¹³⁵

Since health care costs are prohibitive, economies of scale in their delivery and/or financing are important concerns in any jurisdiction. In Canada, state provision generates these economies. In the U.S. however, the existing model of health insurance provision by tax-subsidized employers highlights the problem of “small” employers. Triangular employment relations, particularly through PEO services, may be conceived of as a mechanism for addressing the problem of scale, emerging within the confines of background regulation. In the language of the “varieties of capitalism” literature, triangular employment here constitutes an institutional arrangement that complements the broader pattern of coordination in this “liberal market economy,” and may deliver a *ceteris paribus* “stretching” of health insurance coverage in the U.S..¹³⁶ From a more critical lens though, this same triangular employment growth may on the other hand increasingly empower firms to avoid existing egalitarian rules. This may be done not only through formal liability avoidance from shifting *de jure* employer status, but also

¹³⁵ The only remaining possibility for savings from employer status arbitrage under these rules would be from the use of an extremely small staffing firm, involving diseconomies of size.

¹³⁶ This remains an important empirical question, for further research.

because of the symbolic importance that the concept of “employer” plays in a jurisdiction so heavily dependent upon employment as a social policy platform.¹³⁷

IV. Concluding Thoughts

This paper has outlined how significant regulatory differentials in two key subfields of regulation in the U.S., largely absent in Canada, combined with comparably more liberal access to these regulatory differentials under U.S. employer status rules, help explain diverging triangular employment growth patterns in in these countries.

Broader reflection on U.S. developments in particular suggest that regulatory differentials and resulting triangular employment growth have contributed to a regressive shift in U.S. employment relations¹³⁸ and social policy. Prior research suggests the importance of the *salience* of fiscal instruments (both tax and spending related) in determining public *consent* for the instrument, and also suggests that tax-expenditure-based spending measures often have comparably lower salience than other more direct forms of spending.¹³⁹ The relaxation of the “leased employee” rules with the resulting eroded effect of the non-discrimination rules in retirement plan regulation over the past few decades, eroded the potentiality of the non-discrimination rules as an egalitarian, redistributive policy instrument. However, the fact that this shift took place within the income tax system likely reduced its salience significantly. Similarly, triangular employment growth (under PEO services) may be interpreted as a response to coverage pressures in the U.S. employer-based health insurance system, and a tool for maintaining sufficient social consent for a system overall, while its egalitarian effect declined for decades. Thus, triangular employment growth itself may be conceived as an instrument that assisted U.S. policy makers somewhat in maintaining legitimacy of decades of regressive

¹³⁷ In this vein, it has been previously argued that triangular structures like PEO “co-employment” arrangements increase user firms’ capacity to “wash their hands” of responsibility in the face of employee morale issues, bolstering their relational power and ability to further transfer the cost of insurance to the workers themselves, and/or to impose less egalitarian, tiered systems of coverage. See CENTRE FOR A CHANGING WORKFORCE, PEOS AND PAYROLLING: A HISTORY OF PROBLEMS AND A FUTURE WITHOUT BENEFITS (2001).

¹³⁸ See Peck and Theodore, *Supra*, note 6.

¹³⁹ A helpful summary of this literature is provided in Gillian Lester, *Keep Government out of my Medicare: The Elusive Search for Popular Support of Taxes and Social Spending*, in WORKING AND LIVING IN THE SHADOW OF ECONOMIC FRAGILITY (Michael Sherraden and Marion Crain, eds., 2013).

policy in both the retirement and healthcare regimes, and preserving the increasingly regressive tax- subsidies embodied in both these regimes. The lack of significant policy response to the expansion of triangular employment in the U.S., and the accommodation of certain policy development to the privately generated concept of “co-employment”, is consistent with these views.