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COMMENTARY-How California's Prop 22 on gig employment could impact financial services

By Azish Filabi
7 MIN READ

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Viewed from the perspective of financial services, the explosion of "gig economy" jobs and associated shifts in the provision of employment-related benefits may eventually reduce the pool of customers considered creditworthy using traditional standards. This will challenge the industry to innovate to meet customer needs.

The ride-sharing platforms Uber and Lyft continue their legal battle against California Assembly Bill 5 (AB5), which took effect January 1 and defines most workers as employees. It also prevents firms from misclassifying their workers as unprotected "independent contractors". The issue will come to a head this November, as California voters consider Proposition 22, a new ballot initiative that would redefine app-based transportation and delivery drivers as contractors subject to separate wage and labor policies.

While this may seem like a case limited to California, British courts in London are also debating the employment status of Uber drivers. The outcome in California will be a forerunner for other jurisdictions considering how best to support gig economy workers during uncertain times.

WHAT'S AT STAKE

At stake is the question of whether Uber, Lyft, and similar companies treat their drivers as employees, instead of independent contractors. While tech companies advocate they are just operating platforms that connect drivers and passengers, California legislators determined that drivers are fundamental to the platform's business.

If the state government view prevails, these companies will be responsible for providing the same employee protections and benefits required of other employers in the state.

IMPLICATIONS FOR FINANCIAL SERVICES

The battle also foreshadows an important implication for the financial services sector.

Breaking up the worker-employer relationship will increase economic risks faced by workers, who are also consumers of financial services. This will make it progressively more difficult for institutions to allocate capital and services to creditworthy customers, which is a fundamental purpose of banking. Moreover, prolonged fallout from the COVID-19 crisis will amplify this risk.

We are already seeing how some systemic changes in the economy are frustrating the banking sector's ability to fulfill its mission. In April, the Wall Street Journal reported that the coronavirus pandemic was hampering the long-standing function of banks in allocating and distributing capital to households.

CONVERGING TRENDS

Two trends are now converging. First, on the heels of the 2008 global financial crisis, banks have a reduced appetite for risk, partly due to the regulatory response to the excessive lending that contributed to that crisis. Consequently, some consumer finance activity has been pushed

out of the traditional banking sector into less-regulated “non-bank” lenders, such as on-line lending platforms.

Second, people’s financial lives are becoming more precarious through unstable employment and the changing features of labor protections, such as those prevailing in the gig economy.

The financial services sector should pay attention, because the developments impact not only the consumer base, but also reduce the number of people classified as fully employed.

Providing financial services, such as disability insurance, unemployment insurance, access to 401-Ks, and other similar benefits, is most efficiently done through employment relationships. As access to jobs grows outside of the traditional employer-employee relationship through the gig economy, connecting with consumers becomes increasingly challenging.

Stable employment and wages are key criteria when banks evaluate a customer’s creditworthiness, and that absent that, banks will need to come up with new ways of evaluating a potential borrower or reduce their lending.

IMPLICATIONS FOR WORKERS

While the gig economy may offer added flexibility, it requires workers to forfeit benefits that accompany traditional employment relationships. Jobs provide not only income, but also serve as the pillar for the provision of health insurance, retirement planning, disability and life insurance, as well as other support services. Such benefits are not perks; they are essential to survival.

The stability provided by W-2 employment is indispensable to buying a house, renting an apartment, or enrolling in a 401(k). It also provides access to other social resources, including education and personal well-being through networks. According to the JP Morgan Chase Institute,

the risks associated with contractor relationships are most acute for individuals relying on gig economy jobs to generate full-time employment income.

The legal battle in California could set an important precedent for other technology platform-driven sectors, such as media, professional services, or education.

In theory, the flexibility provided by platform-based jobs, and other sharing economy technologies like AirBnb or Etsy, provide new opportunities for "self-assembled careers," reducing dependence on large corporations. Arguably, these jobs are necessary to fill the employment void created as the social contract of employment has frayed through corporate outsourcing, globalization, or adherence to cost-cutting models of finance, enabling individuals to take steps towards self-sufficiency.

PLATFORMS SEEK GOVERNMENT-FUNDED EMPLOYMENT BENEFITS

Leadership at Uber and Lyft appear to understand this dynamic, lobbying Congress earlier this year to expand their drivers' access to traditional, government-funded "employment" benefits – ironically advocating for the rights of drivers they insisted were not employees.

Their legislative stance is telling. By asking Congress to extend publicly funded benefits to their drivers, Uber and Lyft acknowledged the inherent vulnerability of those workers, particularly in an economic crisis. It is a vulnerability banks are sure to note.

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