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PARTICIPATION AS A THEORY OF EMPLOYMENT

Matthew T. Bodie*

ABSTRACT

The concept of employment is an important legal category, not only for labor and employment law, but also for intellectual property law, torts, criminal law, and tax. The right-to-control test has dominated the debate over the definition of “employee” since its origins in the master-servant doctrine. However, the test no longer represents our modern notion of what it means to be an employee. This change has played itself out in research on the theory of the firm, which has shifted from a model of control to a model of participation in a team production process. This Article uses the theory of the firm literature to provide a new doctrinal definition for “employee” based on the concept of participation rather than control. The participation test better delineates the boundaries of employment and provides a framework for addressing the stresses on firms and workers that are rife within the modern economy.

INTRODUCTION

The concept of employment plays an important role across the legal landscape. Most obviously, labor and employment law protections provided under local, state, and federal law are limited to those

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* Professor, Saint Louis University School of Law; Co-Reporter, Restatement (Third) of Employment Law. This Article reflects my own views and not those of the American Law Institute or my fellow reporters. Many thanks to the students in the seminar “Law and Theories of Employment” at Notre Dame Law School in Fall 2012. Their thoughts and insights provided significant contributions to this paper. Thanks as well to Rick Garnett and the Notre Dame faculty for their feedback through their workshop series, as well as to commentators at the 2013 American Law & Economics Association, Law & Society Association, and Midwest Law and Economics Association annual meetings. I am also much obliged to Guy Davidov, Matt Dimick, Cindy Estlund, Michael Fischl, Tim Glynn, Rebecca Hollander-Blumoff, Brishen Rogers, and Charlie Sullivan for their very helpful comments. And special thanks to Jay Tidmarsh for lending me volume 2 of the Restatement (Second) of Torts.
contracting parties that are defined as employees. However, many other areas of law draw distinctions based on the fact that the actor was an employee, or that the actions were taken within the scope of employment. Common law doctrines or statutory provisions in intellectual property, criminal law, torts, and tax use the concept of employment in assigning critical rights and liabilities. Although these regimes are not generally thought of as labor and employment law, they invest the employment relationship with even further legal meaning.

Because the same concept of “employment” is used across legal contexts, one’s intuition is that the concept would remain largely consistent even in its variegated uses. And this has largely been true. The concept of control has served as the unifying idea behind the use of “employee” and “employment” in different contexts. The common law “control test” comes out of the original conceptions of master and servant from pre-industrial English law, and the Supreme Court has used this test as the default definition of the term “employee” in federal statutes. However, the control test is not the unanimous answer,


2 The “work-for-hire” doctrine is the most prominent. See 17 U.S.C. § 201(b) (2006). For further discussion, see infra Section I.D.

3 The doctrine of “enterprise liability” renders an organization liable for the crimes of its employees. See infra Section I.C.

4 Employers have long been liable for the torts of their employees committed within the scope of employment under the doctrine of respondeat superior. See infra Section I.B.

5 Employees are treated differently within tax law for a variety of purposes, including withholding, benefit plans, and social security payroll taxes. See infra Section I.E.

6 It should also be noted that the definition of “employment” is limited to those relationships that courts have deemed to be “economic” or “market-oriented” in character. For example, prison labor, work within families, and student labor have been excluded from the definition because they do not take place within the labor market. As Noah Zatz has pointed out, “employment law systematically faces disputes over both how to draw a market/nonmarket distinction and whether that distinction matters legally.” Noah D. Zatz, Working at the Boundaries of Markets: Prison Labor and the Economic Dimension of Employment Relationships, 61 VAND. L. REV. 857, 862 (2008). This Article addresses the issue of whether work that is considered “economic” is conducted within or outside of an employment relationship.

7 See Clackamas Gastroenterology Assocs., P.C. v. Wells, 538 U.S. 440, 448 (2003) (interpreting employee under the Americans with Disabilities Act (ADA)); Nation-
and in fact it may be losing its firm grip on the category. Courts have long used the “economic realities” test in interpreting the broader definition provided under the Fair Labor Standards Act (FLSA).8 In addition, the D.C. Circuit recently installed an “entrepreneurial opportunities” test that has received support from the Restatement (Third) of Employment Law.9 Foreign jurisdictions have looked to the concept of “economic dependence.”10 Other jurists and scholars have argued that there should not be any one definition of employment, and that instead the term should be adapted to fit the needs of the particular statutory, regulatory, or common law regime.11

This Article argues that there is a consistent meaning to the idea of employment, but it is not the control test. The meaning comes not from looking at employees but rather at the firm that employs them. Ever since Ronald Coase’s The Nature of the Firm,12 economists and legal scholars have puzzled over why the law created firms that stand outside the market. The purpose of firms, Coase famously answered, is to avoid transaction costs by allowing the parties to organize in a hierarchical manner without the need for prices or specific contracts.13 As Coase put it: “If a workman moves from department $Y$ to department $X$, he does not go because of a change in relative prices,

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8 See, e.g., Sec’y of Labor v. Lauritzen, 835 F.2d 1529, 1544 (7th Cir. 1987) (using the “economic realities” test to interpret “employee” in the context of the FLSA).

9 FedEx Home Delivery v. NLRB, 563 F.3d 492, 497 (D.C. Cir. 2009) (arguing that the Board and the circuit had “shift[ed] the emphasis away from the unwieldy control inquiry in favor of a more accurate proxy: whether the putative independent contractors have significant entrepreneurial opportunity for gain or loss” (alteration in original) (internal quotation marks omitted)); RESTATEMENT (THIRD) OF EMPLOYMENT LAW § 1.01 (Tentative Draft No. 2, 2009), available at http://www.ali.org/00021333/Employment%20Law%20TD%20No%202%20-%20Revised%20-%20September%202009.pdf.

10 See Guy Davidov, Who is a Worker?, 34 INDUS. L.J. 57, 59 (2005) (discussing the use of the concept of dependence in British law).

11 See, e.g., Lauritzen, 835 F.2d 1529, 1543 (7th Cir. 1987) (Easterbrook, J., concurring) (suggesting that the economic realities test be exchanged for a test as to the statute’s purpose); Lehigh Valley Coal Co. v. Yensavage, 218 F. 547, 552 (2d Cir. 1914) (“It is true that the statute uses the word ‘employed,’ but it must be understood with reference to the purpose of the act, and where all the conditions of the relation require protection, protection ought to be given.”); Richard R. Carlson, Why the Law Still Can’t Tell an Employee When It Sees One and How It Ought to Stop Trying, 22 BERKELEY J. EMP. & LAB. L. 295, 356 (2001) (arguing that the concept of employment should be disregarded and other proxies for coverage should take its place).


13 Id. at 388.
but because he is ordered to do so.”¹⁴ Less well known is that Coase
then looked to the legal definition of employee to determine whether
his transaction costs theory was supported in practice.¹⁵ He found
that it was. Since the “control” test was based on the employer’s ability
to require its employees to take specific actions, he concluded, “[w]e
thus see that it is the fact of direction which is the essence of the legal
concept of ‘employer and employee,’ just as it was in the economic
concept which was developed above.”¹⁶

Coase’s approach to the theory of the firm was only the begin-
ing. In fact, Armen Alchian and Harold Demsetz famously rejected
Coase’s workman example.¹⁷ Scholars have continued to place impor-
tance on the role of employees within the firm in defining what a firm
is and why it has independent existence.¹⁸ This rich literature, how-
ever, has been largely ignored when it comes to defining the concept
of employment.¹⁹ This Article seeks to correct that failing. The the-

¹⁴ Id. at 387.
¹⁵ Id. at 403 (“We can best approach the question of what constitutes a firm in
practice by considering the legal relationship normally called that of ‘master and ser-
vant’ or ‘employer and employee.’”).
¹⁶ Id. at 404.
¹⁷ Armen A. Alchian & Harold Demsetz, Production, Information Costs, and Eco-
nomic Organization, 62 Am. Econ. Rev. 777, 777 (1972) (“Telling an employee to type
this letter rather than to file that document is like my telling a grocer to sell me this
brand of tuna rather than that brand of bread. I have no contract to continue to
purchase from the grocer and neither the employer nor the employee is bound by
any contractual obligations to continue the relationship.”).
¹⁸ See, e.g., Eric W. Orts, Shirking and Sharking: A Legal Theory of the Firm, 16 Yale L.
& Pol’y Rev. 265, 284 (1998) (“From the point of view of their internal organization,
firms are aggregates of individuals . . . . From the point of view of the markets in
which they act as purchasers and sellers, firms act as entities.”).
¹⁹ A notable exception is Guy Davidov, who has discussed the concept of joint
production and incomplete contracts in developing a theory of employment. Guy
Davidov, The Three Axes of Employment Relationships: A Characterization of Workers in Need
(citing and discussing the works of prominent figures in the field of law and econom-
ics such as Alchian and Demsetz, Coase, and Williamson). Tim Glynn has discussed
how Coase’s work on the firm explains the shift to smaller firms and enterprise disag-
gregation. Glynn argued that the rise in transaction costs from legal regulations such
as labor and employment laws led many employers to outsource the employment relation-
ship onto fly-by-night subcontractors, who often dissolve or disappear when faced
with litigation. Timothy P. Glynn, Taking the Employer Out of Employment Law? Account-
ability for Wage and Hour Violations in an Age of Enterprise Disaggregation, 15 Emp.
Rts. & Emp. Pol’y J. 201, 207–15 (2011). Scott Masten examined the definition of employ-
ment in assessing the legal significance of the firm in practice. See Scott E. Masten,
A Legal Basis for the Firm, in The Nature of the Firm 196 (Oliver E. Williamson & Sidney
G. Winter eds., 1991). I endeavor to do the converse: examine the theory of the firm
literature in assessing the definition of employment.
ory of the firm contains a critical insight: the idea of employment is based not on our notions of employees, but rather on our notions of employers. There can be no employee without an employer. The theory of the firm literature demonstrates that the employer is a firm, and that the concept of employment is critical in determining what a firm is and why it continues to exist.

Using the theory of the firm literature to demarcate the boundaries between employee and independent contractor may appear at first to be a tedious and inconsequential exercise. But its theoretical and practical implications are massive. The sociological stability of the employment relationship has seen significant erosion, as more companies seek to outsource their chain of production and more workers enjoy only temporary employment. At the same time, nationwide firms are placing greater importance on their economic brands, and employees are critical representatives of their companies when it comes to their brand’s value and influence. We grow closer to a potential “death of employment” at the same time that multinational corporations have more economic power (and employees) than ever. These pressures ask us to consider what, if anything, about the concept of “employment” is worth saving.

This Article argues that the proper definition of employee is not the control test, the economic realities test, or the entrepreneurial opportunities test. Instead, the concept of employment has in fact been and should henceforth be used to differentiate between members and nonmembers of an economic firm. In other words, employees are participants in a common economic enterprise organized into a business entity. This participation-based definition provides the best rationale for the use of the “employee” category in areas of law such as

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20 In fact, the standard statutory definition of “employee” is the following exercise in passive voice: one who is employed by an employer. See, e.g., 29 U.S.C. § 1002(6) (2006) (defining employee as “any individual employed by an employer”).

21 See, e.g., Julia Tomassetti, Who Is a Worker? Partisanship, the National Labor Relations Board, and the Social Content of Employment, 37 LAW & SOC. INQUIRY 815, 843 (2012) (“The long-term, direct, full-time, wage-labor bargain between one employer and a group of employees within proprietary firm boundaries was briefly—between the 1950s and 1970s—the politically dominant, concrete form that relations in production assumed within capitalist relations of production in the United States.”); Peter Coy et al., The Disposable Worker, BLOOMBERG BUSINESSWEEK, Jan. 18, 2010, at 33 (discussing trends of temporary employment in the wake of the financial crisis).


23 Alan Hyde, Employment Law After the Death of Employment, 1 U. PA. J. LAB. & EMP. L. 99, 100 n.4 (1998) (explaining that, along with other changes in the labor market, the use of “nonemployment” work relations is increasing).
intellectual property, tax, and torts. Moreover, the participation theory explains why labor and employment law protections are based on employment status: these protections are designed to make firms more economically responsible for their participants. Because employees participate in the common economic enterprise as organized into a firm, the firm in turn must take care of its employees within that common enterprise.

Part I of the Article examines where (and why) the concepts of “employee” and “employment” are used within the law. Part II sets out the different doctrinal definitions of the terms “employee” and “scope of employment,” and also examines the theories behind these definitions. Part III provides an overview of the theory of the firm literature and the role of employees within that literature. Part IV uses the theory of the firm to develop a new definition of employment within the law based on participation. Finally, Part V briefly considers the future of the concept of “employment” in the law.

I. THE CONCEPT OF EMPLOYMENT IN THE LAW

The role of “employment” within the law extends beyond the easily identifiable categories of labor and employment law. This Part examines the role that employment serves in defining a variety of legal regimes.

A. Labor and Employment Law

Lawmakers have used the concept of employment to create a set of rights within the law that provide protections to those defined as employees. Prohibitions against race, sex, age, and disability discrimination, below-minimum wages, dangerous working conditions,


   It shall be an unlawful employment practice for an employer—
   (1) to fail or refuse to hire or to discharge any individual, or otherwise to discriminate against any individual with respect to his compensation, terms, conditions, or privileges of employment, because of such individual’s race, color, religion, sex, or national origin; or
   (2) to limit, segregate, or classify its employees or applicants for employment in any way which would deprive or tend to deprive any individual of employment opportunities or otherwise adversely affect his status as an employee, because of such individual’s race, color, religion, sex, or national origin.

retirement funding requirements, and attacks on collective activity, among others, are limited to employees. State employment provisions such as workers’ compensation and unemployment compensation are also limited to employees. These statutory schemes are designed to provide protections to employees as employees and not to any other groups, even if those outside the employee category might benefit from the scheme.

Along with using employment to define vicarious liability (discussed below in Part B), the common law also has certain doctrines that are limited to employment. The tort of wrongful discharge, for example, provides rights to employees—not independent contractors. And employment at-will is a common law doctrine that is arguably separate from the traditional set of rules for contract interpretation. In addition, under agency law employees have a fiduciary duty of loyalty to their employers. This duty generally requires the

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26 See id. § 654(a) (requiring employers to “furnish to each of his employees employment and a place of employment which are free from recognized hazards”).
27 See, e.g., id. § 1053 (providing for minimum vesting standards for employee retirement accounts).
28 See id. § 158(a)(1), (3) (“It shall be an unfair labor practice for an employer—
(1) to interfere with, restrain, or coerce employees in the exercise of the rights guaranteed in section 157 of this title; . . . (3) by discrimination in regard to hire or tenure of employment or any term or condition of employment to encourage or discourage membership in any labor organization . . . .”).
29 There are other federal statutory protections, as well as numerous state and local protections, that are limited to employees.
31 The employment at-will rule is a default provision in employment contracts that the relationship can be terminated at any time by either party. See Restatement (Third) of Employment Law § 2.01 (Tentative Draft No. 1, 2008). The at-will rule may even be considered a “sticky” default—namely, a default rule that requires more explicit or onerous expressions of intent to overcome. See Deborah A. DeMott, Investing in Work: Wilkes as an Employment Law Case, 33 W. New Eng. L. Rev. 497, 498 (2011) (arguing that employment at-will may be a “sticky” default); David Millon, Default Rules, Wealth Distribution, and Corporate Law Reform: Employment at Will Versus Job Security, 146 U. Pa. L. Rev. 975, 1028–30 (1998) (exploring the argument that the default rule should be changed from at-will employment to a “just cause” regime because the just cause regime may better represent an efficient outcome between the parties).
employee not to compete directly with the employer while still an employee.33

B. Vicarious Liability in Tort

The concept of employment is used as the basic dividing line in the doctrine of respondeat superior. An employer is liable for the acts of its employees committed within the scope of employment, but it is generally not liable for the acts of independent contractors that are working with it.34 Respondeat superior has its roots in early master-servant doctrine, in which a master was liable for harms caused by the actions of his servant.35 The doctrine continues in the modern common law, with most courts using the term “employee” in place of “servant.” Although many different justifications for the doctrine have been given, most center around the responsibility for or control of the employer over the employee.36 Employers can also be liable for the torts of independent contractors, but generally only under one of three conditions: (1) the employer is negligent in “selecting, instructing, or supervising the contractor;” (2) the employer has a nondelegable duty of care to the public as a whole or the particular plaintiff; or (3) the work done by the contractor for the employer is “specially” or “inherently” dangerous.37 United States common law used to follow the “fellow servant” rule, in which the employer was

("All employees owe a fiduciary duty of loyalty to their employer—be the employer a sole proprietor, a partnership, a close corporation, or a large, publicly traded corporation.").

33 O'Neill, supra note 32, at 695 (“Until his employment has terminated, . . . he may not engage in actual competition against his employer.”). Enhanced remedies, including disgorgement of compensation paid during the period of disloyalty, are available in some jurisdictions under the “faithless servant” doctrine. See, e.g., Astra USA, Inc. v. Bildman, 914 N.E.2d 36, 47 (Mass. 2009) (explaining that an employee’s violation of duty to the employer results in forfeiture of “any right to compensation for services” (quoting Murray v. Beard, 7 N.E. 553 (N.Y. 1886))); Charles A. Sullivan, Mastering the Faithless Servant?: Reconciling Employment Law, Contract Law, and Fiduciary Duty, 2011 Wis. L. Rev. 777, 779–80 (discussing the elements of breach and remedy associated with faithless servant doctrine).

34 Restatement (Third) of Agency § 2.04 (2006) (“An employer is subject to liability for torts committed by employees while acting within the scope of their employment.”); Restatement (Second) of Torts § 409 (1965) (“Except as stated in §§ 410–429, the employer of an independent contractor is not liable for physical harm caused to another by an act or omission of the contractor or his servants.”).

35 1 William Blackstone, Commentaries *417 (1765).


37 Restatement (Second) of Torts § 409 cmt. b (1965). These are the three primary circumstances; the employer is also liable when it has performed a contract
absolved of liability to an employee for an injury caused by a fellow employee. However, this rule has generally been abolished and/or rendered obsolete by workers’ compensation statutes.

C. Criminal Liability

Business organizations may be criminally responsible, as well as liable in tort, for the misdeeds of their employees under the doctrine of respondeat superior. Corporations and other business entities are guilty of crimes committed by their employees if such crimes were committed in the scope of employment. In order to satisfy the mens rea requirement, courts have additionally required that the employee have acted with the intent to benefit the business entity. Although the doctrine has faced steady criticism over the years, it has become “firmly entrenched as, more or less, the across-the-board rule of enterprise liability for all manner of crimes.” However, the de jure rule masks a more complex reality. Courts and prosecutors have in practice adopted a narrower standard of liability when it comes to institutional guilt. At the front end, a series of Department of Justice memos over the last decade chronicled the attempts to demarcate when using independent contractors when those services were accepted in the belief that they were to be performed by the employer and its employees. Id. § 429.

38 See Restatement (Second) of Agency § 474 (1958): A master is not liable to a servant or subservant who, while acting within the scope of his employment or in connection therewith, is injured solely by the negligence of a fellow servant in the performance of acts not involving a violation of the master’s non-delegable duties, unless the servant was coerced or deceived into serving, was too young to appreciate the risks, or was employed in violation of statute.

39 Keeton et al., supra note 36, at 575–76; J.M. Balkin, Too Good to Be True: The Positive Economic Theory of Law, 87 Colum. L. Rev. 1447, 1487 (1987) (reviewing William M. Landes & Richard A. Posner, The Economic Structure of Tort Law (1987)) (“[T]he fellow servant rule is like a mastodon preserved in a glacier—it was rendered obsolete by workers’ compensation, and, given the general trend of twentieth century tort law, there can be no question that if workers’ compensation were abolished today few courts would follow the fellow servant rule in industrial accident cases.”).


41 See, e.g., Standard Oil Co. v. United States, 307 F.2d 120, 128 (5th Cir. 1962) (describing the requirements as elements of liability taken from civil tort law).

42 Samuel W. Buell, The Blaming Function of Entity Criminal Liability, 81 Ind. L.J. 473, 475–76 (2006); see also Jennifer Arlen, The Potentially Perverse Effects of Corporate Criminal Liability, 23 J. Legal Stud. 833, 836 (1994) (stating that the existing legal regime closely approximates a rule of “pure strict vicarious liability” (citations omitted)).
orporations should be charged with crimes.\textsuperscript{43} All of these guidelines required more than mere respondeat superior liability.\textsuperscript{44} At the back end, the U.S. Sentencing Guidelines assessed punishment for corporate guilt based on whether “an individual within high-level personnel of the unit participated in, condoned, or was willfully ignorant of the offense; or tolerance of the offense by substantial authority personnel was pervasive throughout such [entity].”\textsuperscript{45} Commentators have noted a change from vicarious liability to more of a negligence standard as to corporate management’s role in overseeing internal investigations.\textsuperscript{46} This move has had both supporters and critics.\textsuperscript{47} However,

\begin{footnotesize}
\begin{itemize}
\item\textsuperscript{44} The Thompson Memorandum listed the following factors in determining when to charge a corporation:
\begin{itemize}
\item 1. the nature and seriousness of the offense . . .;
\item 2. the pervasiveness of wrongdoing within the corporation . . .;
\item 3. the corporation’s history of similar conduct . . .;
\item 4. the corporation’s [cooperation and willingness to waive] attorney-client [privilege] and work product protection . . .;
\item 5. the existence . . . of [a] compliance program . . .;
\item 6. the corporation’s remedial actions . . .;
\item 7. collateral consequences [of a charge, such as] . . . harm to shareholders, pension holders and employees . . .;
\item 8. the adequacy of [prosecuting the individuals involved;] and
\item 9. the adequacy of civil or regulatory enforcement.”
\end{itemize}
\end{itemize}
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the prevalent criminal liability rule remains based on respondeat superior.

D. Intellectual Property

The term “intellectual property” refers to a wide range of information to which specific legal rights have attached. In some cases, intellectual property is generated by a single individual: an author writing alone in her home, or an inventor toiling away in the garage. However, in many cases, intellectual property is generated by specific individuals who are working within the context of a larger firm. How the rights to that “property” are divvied up has significant legal and economic ramifications, particularly for firms and individual employees.48

Federal law establishes ownership rights for copyrighted works. The “work-for-hire” doctrine was originally established in the 1909 Copyright Act, as that law specified that the author of a copyrighted work “shall include an employer in the case of works made for hire.”49 The Copyright Act of 1976 continued this doctrine, specifying that the employer is considered the author of any work made for hire unless expressly agreed otherwise.50 The 1976 Act defines “work made for hire” as “a work prepared by an employee within the scope of his or her employment.”51 This rule of ownership can only be altered by a signed, written document that expressly changes it.52

been moving away from a system of strict vicarious liability toward a system of duty-based organizational liability."

47 For support for a deterrence-based approach, see Vikramaditya S. Khanna, Should the Behavior of Top Management Matter?, 91 GEO. L.J. 1215, 1224 (2003) (“Corporate liability improves deterrence when agents are judgment-proof because it places corporate assets at risk and thereby forces the corporation to internalize the social costs of wrongdoing.”). For criticism of the monitoring-based approach, see Krawiec, supra note 46, at 614 (“I conclude that the U.S. legal regime’s move away from strict vicarious liability to internal compliance-based liability is unjustified by either theory or empirical evidence.”).


50 17 U.S.C. § 201(b) (2006) (“In the case of a work made for hire, the employer or other person for whom the work was prepared is considered the author for purposes of this title, and, unless the parties have expressly agreed otherwise in a written instrument signed by them, owns all of the rights comprised in the copyright.”).

51 Id. § 101.

52 Id. § 201(b).
The default rule for patent law is that the employee who invents the patent is the author, not the employer. However, the employer is free to contract with employees explicitly for the rights to all inventions created within the scope of employment. Even without an explicit contract, judges have found something akin to a work-for-hire doctrine when an employee is hired to work on a specific invention or problem; courts are more likely to conclude that the employee was hired to invent and therefore the firm owned all patents through an implied contract. In addition, under the shop-right doctrine, employers enjoy a nonexclusive right to use the patent without having to compensate the employee. A shop right arises when the employee has created the invention on the job using the employer’s materials.

Trademark presents a special connection among the firm, its employees, and intellectual property. Trademark protection enables a group of people to join together and be recognized as a common enterprise without fearing that their brand name and reputation will be poached by outsiders. Just as patent and copyright protections concern the allocation of information rights between employee and firm, trademark concerns the allocation of good will and reputational rights between employee and firm. Trademarks enable firms to use and transfer reputational assets over to the firm, and thus deprive individual employees of their ability to hold up the firm or exploit the trade dress separately.

Finally, trade secret law allocates the ownership of softer intellectual capital between employees and the firm. The Uniform Trade Secret Act defines misappropriation of a trade secret as acquiring the trade secret either by improper means or “under circumstances giving

53 The patent must be registered by the individual inventor. See 35 U.S.C. §§ 111, 115 (2006) (discussing oath taken as part of patent process that the registrant is the “original and first inventor”).


In the absence of explicit contractual terms requiring an assignment, an implied duty to assign may be found. Courts have tended to recognize such an implied duty to assign patent rights in situations where an employee hired to solve a problem engages in research, and the invention relates to that effort.

55 Fisk, supra note 54, at 118; Burk, supra note 54, at 16.


57 Id. at 376.
rise to a duty to maintain its secrecy or limit its use."58 Although the Act applies to any “person,”59 employees in particular are expected to keep confidential any of the employer’s trade secrets to which they are exposed during the course of employment.60 Indeed, employees are primary targets for the protections against trade secret misappropriation. A study of trade secret litigation found that over eighty-five percent of trade secret cases involved alleged misappropriators who were either current or former employees or business partners.61 Employees are generally presumed to have an implied duty to keep any trade secrets to which they are exposed confidential.62 Moreover, the doctrine of “inevitable disclosure of trade secrets” has applied in some jurisdictions to employees who leave the company but (according to the court) must inevitably use the trade secrets they have learned at their old position.63

58 Uniform Trade Secrets Act § 1(2)(ii)(B)(II) (amended 1985) [hereinafter UTSA]. The Act is model civil legislation that has been adopted at least in part by forty-seven jurisdictions.
59 UTSA, supra note 58, § 1(3) (defining “person” as “a natural person, corporation, business trust, estate, trust, partnership, association, joint venture, government, governmental subdivision or agency, or any other legal or commercial entity”).
60 O’Neill, supra note 32, at 695 n.65 (“Courts have held that when an employer discloses its trade secret to an employee in the course of employment, the employee is bound by his fiduciary duty of loyalty not to use or reveal it for his own personal benefit.”).
61 David S. Almeling et al., A Statistical Analysis of Trade Secret Litigation in Federal Courts, 45 GONZ. L. REV. 291, 294 (2010). The study also found that trade secret owners were “twice as likely to prevail on a motion for preliminary relief when they sued employees as when they sued business partners.” Id. However, owners were also “over 70% more likely to lose a motion to dismiss when they sued employees than business partners.” Id.
62 See Unistar Corp. v. Child, 415 So. 2d 733, 734 (Fla. Dist. Ct. App. 1982) (“The law will import into every contract of employment a prohibition against the use of a trade secret by the employee for his own benefit, to the detriment of his employer, if the secret was acquired by the employee in the course of his employment.”); Derek P. Martin, Comment, An Employer’s Guide to Protecting Trade Secrets from Employee Misappropriation, 1993 BYU L. REV. 949, 953 (“For most employees the law presumes a confidential relationship between employer and employee for the purposes of protecting trade secrets.”).
63 See, e.g., PepsiCo, Inc. v. Redmond, 54 F.3d 1262, 1269 (7th Cir. 1995) (“[A] plaintiff may prove a claim of trade secret misappropriation by demonstrating that defendant’s new employment will inevitably lead him to rely on the plaintiff’s trade secrets.”); Rebecca J. Berkun, Comment, The Dangers of the Doctrine of Inevitable Disclosure in Pennsylvania, 6 U. PA. J. LAB. & EMP. L. 157, 157 (2003) (“The doctrine of inevitable disclosure restricts an employee’s future employment if that employee will inevitably use a former employer’s trade secrets in the course of the future employment.”).
E. Tax

Firms are expected to differentiate between employees and independent contractors over a host of provisions, including whether taxes need to be withheld, whether the firm must pay a share of Social Security and Medicare (FICA) and unemployment (FUTA) taxes, and whether the workers count as employees for benefit plan purposes. The IRS defines employees based on the common law control test. The consequences of a misclassification can be extremely costly, as the business is then subject to the mandatory backtax formula. In fact, Congress was moved to create a “safe harbor” for employers when it came to the employee-independent contractor distinction. The upshot of these requirements is to give the firm tax responsibilities for its employees, while giving independent contractors tax responsibilities for themselves.

II. The Definition of Employment in Doctrine and Theory

The categories of “employee” and “the scope of employment” define certain contours within various areas of the law. For many statutory schemes, the “employee” category does all of the work; once the identity of the person as an employee has been established, that person is entitled to the rights conveyed upon employees and can bring claims for violations of those rights. In other areas of the law, however, the person and the context are relevant to establishing the legal category; therefore, both “employee” and “scope of employment” are necessary to establish. Both categories are considered below.

65 Id. §§ 3101, 3121(d).
66 Id. §§ 3301, 3306(i).
67 Id. § 410(a).
68 Id. § 3121(d)(2) (defining an employee as, among other definitions, “any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee”); 26 C.F.R. § 31.3121(d)-1(c)(2) (2012) (finding an employment relationship “when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished”); see 26 U.S.C. § 3306(i) (stating that “the term ‘employee’ has the meaning assigned to such term by section 3121(d)’); Rev. Rul. 87-41, 1987-1 C.B. 296, 298–99 (laying out a twenty-factor test to aid in “determining whether an individual is an employee under the common law rules”).
A. Defining “Employee”

1. The Common Law “Control” Test

The “control” test is the dominant standard for employment, both nationally and internationally.71 The test finds its historical roots in the definition of “servant” in English common law. William Blackstone describes the relationship between master and servant as one of the three “great relations in private life,” along with husband and wife and parent and child.72 The relationship was used primarily not for contractual purposes, but rather to establish the duties each owed to the other and to establish when a master was liable for the actions of the servant. The master was certainly liable if the servant committed the act “by the command or encouragement of his master,”73 but liability extended beyond such direct orders. Blackstone offered the following example and justification: “If an innkeeper’s servants rob his guests, the master is bound to restitution: for as there is a confidence reposed in him, that he will take care to provide honest servants, his negligence is a kind of implied consent to the robbery . . . .”74

Under what circumstances would one who contracts for labor be liable for the acts of the laborer? Respondeat superior does not apply generally to the agency relationship; such vicarious liability is reserved for the master-servant relationship.75 English courts based the defini-
tion of this relationship on the notion of control. The basics of the 
collection test are straightforward. A servant is one who is “under the 
duty of rendering personal services to the master or to others on behalf of the master.”76 In addition, the master must have the “right 
to control the servant’s work,” which means “being entitled to tell the 
servant when to work (within the hours of service) and when not to 
work, and what work to do and how to do it.”77 This right of control is 
what separates the master-servant relationship from the principal-
agent relationship.

The Restatement (Second) of Agency is perhaps the most widely rec-
ognized source in American law for the principal-agent and master-
servant doctrines.78 Section 220 defines a servant/employee as: “a 
person employed to perform services in the affairs of another and 
who with respect to the physical conduct in the performance of the 
services is subject to the other’s control or right to control.”79 As the 
commentary acknowledges, however, this relationship is “one not 
capable of exact definition.”80 The Restatement provides a ten-factor 
test to further determine whether the potential master/employer is 
exercising control:

(a) the extent of control which, by the agreement, the master may 
exercise over the details of the work;
(b) whether or not the one employed is engaged in a distinct occu-
pation or business;
(c) the kind of occupation, with reference to whether, in the local-
ity, the work is usually done under the direction of the employer or 
by a specialist without supervision;
(d) the skill required in the particular occupation;
(e) whether the employer or the workman supplies the instrumen-
talities, tools, and the place of work for the person doing the work;
(f) the length of time for which the person is employed;
(g) the method of payment, whether by the time or by the job;
(h) whether or not the work is a part of the regular business of the 
employer;

Id. § 2.04 cmt. b.
76 Coase, supra note 12, at 403–04 (quoting Francis Raleigh Batt, The Law of 
Master and Servant 6 (1929)).
77 Id. at 404.
78 Stephen M. Bainbridge, Agency, Partnerships & LLCs 19 (2004) (“In general, 
the single most influential source of legal rules in this area remains the American Law 
Institute’s Restatement of Agency.”).
79 Restatement (Second) of Agency § 220(1) (1958).
80 Id. § 220 cmt. c.
(i) whether or not the parties believe they are creating the relation of master and servant; and

(j) whether the principal is or is not in business.81

Master-servant doctrine makes no exceptions or differentiations based on the relative status of the “servant” vis-à-vis the “master.” It may seem that high-ranking employees would not meet the test, as their actions are not controlled in the same way as rank-and-file workers. However, no such exception exists. Instead, control “indicates the closeness of the relation between the one giving and the one receiving the service rather than the nature of the service or the importance of the one giving it.”82 Accordingly, “ship captains and managers of great corporations are normally superior servants, differing only in the dignity and importance of their positions from those working under them.”83 The Restatement (Third) of Agency uses the same example but frames the justification a bit differently:

In some employment relationships, an employer’s right of control may be attenuated. For example, senior corporate officers, like captains of ships, may exercise great discretion in operating the enterprises entrusted to them, just as skilled professionals exercise discretion in performing their work. Nonetheless, all employers retain a right of control, however infrequently exercised.84

The Supreme Court has made the common law “control” test into the default definition for “employee” whenever used without further explanation in a federal statute. In Community for Creative Non-

81 Id. § 220(2). These factors have significant overlap with the criteria to determine “conditions of dependency or subordination” included in a set of International Labor Organization (ILO) draft recommendations. Davidov, supra note 19, at 402 (internal quotation marks omitted). The Restatement (Third) of Agency has modernized the language of these doctrines by changing “servant” to “employee,” but the doctrines remain relatively the same. See Restatement (Third) of Agency § 7.07(3)(a) (2006) (“[A]n employee is an agent whose principal controls or has the right to control the manner and means of the agent’s performance of work . . . ”). The primary difference in language, beyond the change from servant to employee, is the removal of “physical” as a modifier for control. Compare Restatement (Second) of Agency § 220 (1958), with Restatement (Third) of Agency § 7.07(3)(a) (2006). The Restatement (Third) of Agency also moves the ten-factor test into the comments section. Id. § 7.07 cmt. f.

82 Restatement (Second) of Agency § 220 cmt. a (1958).

83 Id.

84 Restatement (Third) of Agency § 7.07 cmt. f (2006). The Restatement then provides the example of a CEO who has bad vision but still wants to drive; the board can compel the CEO to use a driver when on company business, despite the CEO’s authority over the company. Id. § 7.07 cmt. f, ex. 15.
Violence v. Reid, the Court said that “[i]n the past, when Congress has used the term ‘employee’ without defining it, we have concluded that Congress intended to describe the conventional master-servant relationship as understood by common-law agency doctrine.” It further found it appropriate to rely on the general common law of agency, rather than the doctrine of any particular state, in order to create a national, uniform law of copyright, and it based its definition on the Restatement (Second) of Agency’s test. The thirteen factors used in Community for Creative Non-Violence to illustrate the common law test largely come from the Restatement (Second) of Agency’s ten-factor test.

The factors have been applied in the labor and employment context as well. The Employee Retirement Security Act’s (ERISA) nominal definition of “employee” is “any individual employed by an employer,” without any further direction. Following Community for Creative Non-Violence, the Supreme Court adopted the common law test and cited to the thirteen-factor test provided in that decision. While acknowledging that “the traditional agency law criteria offer no paradigm of determinacy[,]” the Court argued that the common law test “generally turns on factual variables within an employer’s knowledge” and comports “with our recent precedents and with the common understanding, reflected in those precedents, of the difference between an employee and an independent contractor.”

The Court rejected the lower court’s definition, which was similar to the “economic realities” test, because it found that ERISA’s statutory defini-
The federal employment antidiscrimination statutes—Title VII of the Civil Rights Act of 1964, the Age Discrimination in Employment Act (ADEA), and the Americans with Disabilities Act (ADA)—all share the same definition of employee as ERISA: “an individual employed by an employer.”94 Up until the Supreme Court’s decision in Darden, circuit courts had applied different tests to determine employee status. Some applied the common law test,95 some the economic realities test,96 and some a hybrid test looking at both control and economic realities.97 After the Court’s holding in Darden, circuit courts largely saw the writing on the wall and applied the common law test to antidiscrimination statutes.98 The Supreme Court confirmed

93 Darden, 503 U.S. at 326–27 (internal quotation marks omitted).
95 See, e.g., Cobb v. Sun Papers, Inc., 673 F.2d 337, 340–41 (11th Cir. 1982) (“Absent guidance from the Supreme Court, we conclude that the term ‘employee’ in cases under Title VII is to be construed in light of general common law concepts.”).
96 See, e.g., Armbruster v. Quinn, 711 F.2d 1332, 1340 (6th Cir. 1983) (“[O]ne must examine the economic realities underlying the relationship between the individual and the so-called principal in an effort to determine whether the individual is likely to be susceptible to the discriminatory practices which the act was designed to eliminate.”); see also Patricia Davidson, Comment, The Definition of “Employee” Under Title VII: Distinguishing Between Employees and Independent Contractors, 53 U. CIN. L. REV. 203, 219–22 (1984) (discussing the Armbruster case at length).
97 See, e.g., Mares v. Marsh, 777 F.2d 1066, 1067 (5th Cir. 1985) (“The third test is a hybrid which considers the ‘economic realities’ of the work relationship as an important factor in the calculus, but which focuses more on ‘the extent of the employer’s right to control the ‘means and manner’ of the worker’s performance . . . .” (alteration in original) (quoting Spirides v. Reinhardt, 613 F.2d 836, 831 (D.C. Cir. 1979))). The hybrid test was arguably “the favored standard for claims under both Title VII and the ADEA” prior to the Darden decision. Lewis L. Maltby & David C. Yamada, Beyond “Economic Realities”: The Case for Amending Federal Employment Discrimination Laws to Include Independent Contractors, 38 B.C. L. Rev. 239, 250 (1997).
98 See, e.g., Wilde v. Cnty. of Kandiyohi, 15 F.3d 103, 105–06 (8th Cir. 1994) (“Application of the economic realities test results in Title VII coverage for some common-law independent contractors because they are vulnerable to discrimination arising in the course of their work. Because the economic realities test is based on the premise that the term should be construed in light of Title VII’s purpose and the construction is broader than at common law, Darden precludes the test’s application.”); see also Maltby & Yamada, supra note 97, at 253 (noting that “[t]he Darden decision has significantly influenced judicial interpretations under Title VII and ADEA”). But see Frankel v. Bally, Inc., 987 F.2d 86, 90 (2d Cir. 1993) (adhering to the hybrid test). The Frankel court found “that in practice there is little discernible differ-
this approach in *Clackamas Gastroenterology Associates v. Wells*,\(^\text{99}\) which applied the common law test and cited to *Darden*.\(^\text{100}\) Thus, the common law test has now been ensconced.\(^\text{101}\) The Court specified that “[w]e think that the common-law element of control is the principal guidepost that should be followed in this case.”\(^\text{102}\) OSHA offers its statutory protections to “employee[s] of an employer who is employed in a business of his employer which affects commerce.”\(^\text{103}\) Given the similarities between this definition and the definition used in ERISA and the antidiscrimination statutes, it seems almost indisputable that the common law agency test should apply. This has been the admis-
However, at least one court continued to apply the “economic realities” test post-\textit{Darden}, finding the analysis to be the same under both tests.\footnote{104} The National Labor Relations Act (NLRA) does not itself provide a definition of the term “employee”; instead, the statute simply provides a laundry list of exclusions.\footnote{105} The Act did not originally exclude independent contractors, and both the National Labor Relations Board and the Supreme Court originally held that so-called “newsboys” were statutory employees for purposes of the Act, even though they were considered independent contractors.\footnote{107} However, Congress rejected this interpretation of the Act and added independent contractors specifically to the list of excluded categories.\footnote{108} The Board then adopted the common law right-to-control test in excluding independent contractors. The Supreme Court sanctioned this test in \textit{NLRB v. United Insurance Co. of America},\footnote{109} making clear that the Board had a range of discretion in implementing the test.


\footnote{105} Loomis Cabinet Co. v. Occupational Safety & Health Review Comm’n, 20 F.3d 938, 942 (9th Cir. 1994) (“Here, the Commission used the economic realities test . . . , but determined that the result would be the same under the \textit{Darden} test. We agree.” (citations omitted)).

\footnote{106} Excluded employees include: agricultural workers, domestically-employed healthcare or family care employees, public-sector employees, railroad, airline, and other transportation workers covered by the Railway Labor Act (RLA), independent contractors, and supervisors. 29 U.S.C. § 152(3).

\footnote{107} \textit{NLRB v. Hearst Publ’ns, Inc.}, 322 U.S. 111, 131–32 (1944). The Court explicitly rejected the common law distinction between employees and independent contractors, holding that the news vendors in question were “subject, as a matter of economic fact, to the evils the statute was designed to eradicate.” \textit{Id.} at 127.


\footnote{109} 390 U.S. 254 (1968). Noting that “[t]here are innumerable situations which arise in the common law where it is difficult to say whether a particular individual is an employee or an independent contractor,” the Court required courts to uphold reasonable determinations “even though [a] court would justifiably have made a different choice had the matter been before it \textit{de novo}.” \textit{Id.} at 258, 260 (quoting Universal Camera Corp. v. \textit{NLRB}, 340 U.S. 474, 488 (1951)).
The Board has had occasion to rule on employee status in a variety of contexts: newspaper carriers, nightclub performers, gas station operators, and novelty vendors. It has taken care to emphasize that the common law agency test, although often called the “control” test, has many factors in play beyond control. Thus, while control may be important in determining employee status, it is not the controlling factor. Instead, the variety of factors listed in *Restatement (Second) of Agency* § 220 are to be considered. And although it is not specifically part of the list of factors in § 220, the Board has used the presence of entrepreneurial opportunities as another factor in evaluating the independence of the workers. The Board has rejected the addition of the FLSA’s “economic dependence” or “economic realities” test, however, despite a recent dissent.

Despite the doctrinal popularity of the “control” test, it remains something of an enigma. Courts and commentators continue


111 Harrah’s Club v. NLRB, 446 F.2d 471, 480 (9th Cir. 1971) (finding such performers to be independent contractors).

112 Am. Oil Co., 188 N.L.R.B. 438, 440 (1971) (finding operators to be independent contractors).

113 ARA Leisure Servs., Inc. v. NLRB, 782 F.2d 456, 461 (4th Cir. 1986) (upholding the Board’s conclusion that such workers were employees).

114 The *Roadway Package System, Inc.* Board stated:

> While we recognize that the common-law agency test described by the Restatement ultimately assesses the amount or degree of control exercised by an employing entity over an individual, we find insufficient basis for the proposition that those factors which do not include the concept of “control” are insignificant when compared to those that do. Section 220(2) of the Restatement refers to 10 pertinent factors as “among others,” thereby specifically permitting the consideration of other relevant factors as well, depending on the factual circumstances presented. . . . Thus, the common-law agency test encompasses a careful examination of all factors and not just those that involve a right of control.


116 *Id.* at 481–82.

117 *Id.* at 484 (Liebman, Member, dissenting).

118 Courts have often relied on the federal definition of “employee” for state statutes that mirror and/or supplement federal employment protections. See, e.g., Strother v. S. Cal. Permanente Med. Grp., 79 F.3d 859, 866 (9th Cir. 1996) (*California courts have interpreted [the California Fair Housing and Employment Act] in accordance with cases interpreting the [ADEA] and the federal Civil Rights Act . . . [and therefore] we look to federal cases in those areas that have addressed whether*
to bemoan its inability to deliver clear answers.\textsuperscript{119} In its initial rejection of the control test in the context of the NLRA, the Supreme Court said that “the assumed simplicity and uniformity, resulting from application of ‘common-law standards,’ does not exist.”\textsuperscript{120} Perhaps more fundamentally, there is a concern that the idea of control is not the proper proxy for the concept of employment. For some courts and commentators, “control” is too expansive a term, going beyond the root notion of supervision that represents the employment relationship.\textsuperscript{121} For others, control is no longer critical to employment, an individual labeled as a partner can be considered an employee for the purpose of employment discrimination laws.” (footnotes omitted) (citations omitted)); Lilley v. BTM Corp., 958 F.2d 746, 750 n.2 (6th Cir. 1992) (“ADEA standards governing employment status also apply to Michigan’s Elliot-Larsen Act, Mich. Comp. Laws, § 37.2101 et seq.”); Frishberg v. Esprit De Corp., Inc., 778 F. Supp. 793, 798 (S.D.N.Y. 1991) (“Since New York law distinguishes between employees and independent contractors in a sufficiently similar manner, the court will use the federal test for both state and federal claims.”).

\textsuperscript{119} See, e.g., NLRB v. United Ins. Co. of Am., 390 U.S. 254, 258 (1968) (“There are innumerable situations which arise in the common law where it is difficult to say whether a particular individual is an employee or an independent contractor . . . .”); NLRB v. Hearst Publ’ns, Inc., 322 U.S. 111, 121 (1944) (“Few problems in the law have given greater variety of application and conflict in results than the cases arising in the borderland between what is clearly an employer-employee relationship and what is clearly one of independent, entrepreneurial dealing.”); FedEx Home Delivery v. NLRB, 563 F.3d 492, 496 (D.C. Cir. 2009) (“While this seems simple enough, the Restatement’s non-exhaustive ten-factor test is not especially amenable to any sort of bright-line rule, a long-recognized rub.” (footnotes omitted)); Kisner v. Jackson, 132 So. 90, 91 (Miss. 1931) (“There have been many attempts to define precisely what is meant by the term ‘independent contractor’; but the variations in the wording of these attempts have resulted only in establishing the proposition that it is not possible within the limitations of language to lay down a concise definition that will furnish any universal formula, covering all cases.”); Carlson, supra note 11, at 299 (“After nearly two hundred years of evolution, the multi-factored ‘common law’ test begs the question of employee status as much as answers it.”).

\textsuperscript{120} \textit{Hearst Publ’ns}, 322 U.S. at 122.

\textsuperscript{121} The D.C. Circuit argued:

Although this “right-to-control” test requires an evaluation of all the circumstances surrounding the relationship between the company and the worker, the extent of the actual \textit{supervision} exercised by a putative employer over the means and manner of the workers’ performance is the most important element to be considered. It is important, however, to distinguish such company supervision from company efforts merely to monitor, evaluate, and improve the results or ends of the worker’s performance. Supervision of the means and manner of the worker’s performance renders him an employee, while steps taken to monitor, evaluate, and improve the results of his work, without supervision over the means by and manner in which he does his work, indicates that the worker is an independent contractor.
but rather an expression from a bygone era.\textsuperscript{122} Several other alternatives have arisen from various areas of the law to try to take at least some share of the control test’s domain.

2. The “Economic Realities” Test

The primary alternative to the control test, particularly in the realm of employment law, is the “economic realities” or “economic dependence” test. It is generally interpreted to provide a more expansive definition to the term “employee,”\textsuperscript{123} one that covers more vulnerable workers who may have some aspects of separation from the firm but lack true economic independence. It has its roots in the interpretation of critical New Deal statutes soon after their passage.\textsuperscript{124} While clearly rejecting the common law control test, these cases did not craft a specific and readily cognizable alternative. Instead, they looked to the purpose of the statutes and attempted to glean an approach that harmonized with that purpose. Interpreting the NLRA, the Court noted that it was “not necessary in this case to make a completely definitive limitation around the term ‘employee.’”\textsuperscript{125} But the Court did distinguish between the traditional common law definition and a broader perspective based on the ills at which the statute was directed. In other words, the term “employee” was “to be determined broadly, in doubtful situations, by underlying economic facts rather than technically and exclusively by previously established legal classifications.”\textsuperscript{126} That reference to “economic facts” became “economic reality” in later cases defining the category of “employee” in the context of the Social Security Act\textsuperscript{127} and the Fair Labor Standards Act.

\textsuperscript{122} FedEx Home Delivery, 563 F.3d at 497 (“Gradually, however, a verbal formulation emerged that sought to identify the essential quantum of independence that separates a contractor from an employee, a process . . . where we used words like control but struggled to articulate exactly what we meant by them. . . . In other words, ‘control’ was close to what we were trying to capture, but it wasn’t a perfect concurrence. It was as if the sheet music just didn’t quite match the tune.”).

\textsuperscript{123} See Bran Noonan, The Campaign Against Employee Misclassification, 82 N.Y. St. B.A. J. 42, 46 (2010).

\textsuperscript{124} Id.

\textsuperscript{125} Hearst Publ’ns, 322 U.S. at 130.

\textsuperscript{126} Id. at 129.

\textsuperscript{127} United States v. Silk, 331 U.S. 704, 713 (1947) (“We concluded that, since that end was the elimination of labor disputes and industrial strife, ‘employees’ included workers who were such as a matter of economic reality.” (discussing Hearst Publ’ns, 322 U.S. at 120, 123, 124, 128, 129, 131)).
(FLSA).\textsuperscript{128} This test—lacking any factors or even specific doctrinal definition—was something of a gestalt or eyeball standard, designed to look at the overall economic relationship and determine whether Congress intended such a relationship to come under the purview of the particular statutory scheme.

Although the Court’s “economic reality” definition was overturned by statutory amendments to both the NLRA\textsuperscript{129} and the Social Security Act,\textsuperscript{130} it has remained in place with regard to the FLSA. That statute’s definition of employee is the circular one found in many statutes: “the term ‘employee’ means any individual employed by an employer.”\textsuperscript{131} However, the Act also defines “employ” to include “suffer or permit to work.”\textsuperscript{132} Because employ is defined differently and more broadly, the Supreme Court has recognized that the FLSA may extend to cover workers beyond the reach of the common law agency test.\textsuperscript{133} The definition of “employee” under the FMLA incorporates the standard from the FLSA by reference,\textsuperscript{134} and thus courts have applied the same “economic realities” test.\textsuperscript{135}

\textsuperscript{128} Goldberg v. Whitaker House Coop., 366 U.S. 28, 33 (1961) (“[T]he ‘economic reality’ rather than ‘technical concepts’ is to be the test of employment.”).


\textsuperscript{130} Social Security Act of 1948, Pub. L. No. 80-642, § 2(a), 62 Stat. 438 (changing definition of employee to exclude those who “under the usual common-law rules applicable in determining the employer-employee relationship, have[ve] the status of an independent contractor”).


\textsuperscript{132} Id. § 203(g).

\textsuperscript{133} See Nationwide Mut. Ins. Co. v. Darden, 503 U.S. 318, 326 (1992) (noting that the FLSA “stretches the meaning of ‘employee’ to cover some parties who might not qualify as such under a strict application of traditional agency law principles”); see also Tony & Susan Alamo Found. v. Sec’y of Labor, 471 U.S. 290, 301 (1985) (“The test of employment under the Act is one of ‘economic reality’ . . . .” (citing Goldberg, 366 U.S. at 33)).

\textsuperscript{134} 29 U.S.C. § 2611(3) (“The terms ‘employ’, ‘employee’, and ‘State’ have the same meanings given such terms in subsections (c), (e), and (g) of section 203 of this title.”).

\textsuperscript{135} Nichols v. All Points Transp. Corp., 364 F. Supp. 2d 621, 630 (E.D. Mich. 2005) (“Because the statutory definition of FMLA, unlike the definition found in ERISA, incorporates the FLSA’s broader definition of ‘employee’ and ‘employ,’ the court will continue to apply the ‘economic realities’ test as described by the Sixth Circuit . . . .”). According to one survey, however, courts have not applied a consistent test when it comes to individual liability under the Act. See Sandra F. Sperino, Chaos Theory: The Unintended Consequences of Expanding Individual Liability Under the Family and Medical Leave Act, 9 EMP. RTS. & EMP. POL’Y J. 175, 177 (2005) (finding that courts have utilized at least seven different tests in determining individual liability for owners, executives, and supervisors).
Outside of these contexts, however, the Supreme Court has made it clear that the “control” test is to apply as the default rule.\textsuperscript{136}

According to the “economic realities” test, “employees are those who as a matter of economic reality are dependent upon the business to which they render service.”\textsuperscript{137} Courts have generally looked to a number of factors in calculating coverage under the “economic realities” test. One popular test, developed in \textit{Bonnette v. California Health \& Welfare Agency},\textsuperscript{138} asks whether the employer: “(1) had the power to hire and fire the employee; (2) supervised and controlled employee work schedules or conditions of employment; (3) determined the rate and method of payment; and (4) maintained employment records.”\textsuperscript{139} Other circuits have more closely mirrored the control test.\textsuperscript{140} But in recognition of the FLSA’s broader coverage, courts have either implicitly or explicitly looked to the “reality” of the worker’s dependence on the putative employer.\textsuperscript{141} Such dependence

\textsuperscript{136} See supra notes 85–88 and accompanying text.


\textsuperscript{139} Id. at 1470 (citation omitted); see Benjamin F. Burry, Testing Economic Reality: FLSA and Title VII Protection for Workfare Participants, 2009 U. CHI. LEGAL F. 561, 564 (“The Bonnette factors have been utilized by most federal circuits, including the Second Circuit.”).

\textsuperscript{140} See, e.g., Sec’y of Labor v. Lauritzen, 835 F.2d 1529, 1534–35 (7th Cir. 1987) (“Among the criteria courts have considered are the following six: 1) the nature and degree of the alleged employer’s control as to the manner in which the work is to be performed; 2) the alleged employee’s opportunity for profit or loss depending upon his managerial skill; 3) the alleged employee’s investment in equipment or materials required for his task, or his employment of workers; 4) whether the service rendered requires a special skill; 5) the degree of permanency and duration of the working relationship; 6) the extent to which the service rendered is an integral part of the alleged employer’s business.”); Hopkins v. Cornerstone Am., 545 F.3d 338, 343 (5th Cir. 2008) (“To aid us in this inquiry, we consider five non-exhaustive factors: (1) the degree of control exercised by the alleged employer; (2) the extent of the relative investments of the worker and the alleged employer; (3) the degree to which the worker’s opportunity for profit or loss is determined by the alleged employer; (4) the skill and initiative required in performing the job; and (5) the permanency of the relationship.”).

\textsuperscript{141} Lauritzen, 835 F.2d at 1538 (describing economic dependence as “the focus of all the other considerations”); Hopkins, 545 F.3d at 346 (“As a matter of economic reality, the Sales Leaders were dependent upon Cornerstone to such an extent that they could not plausibly be considered ‘in business for [themselves].’” (alteration in original) (quoting Herman v. Express Sixty-Minutes Delivery Serv., Inc., 161 F.3d 299, 303 (5th Cir. 1998))).
is often manifested through the economic weakness of the workers, and the focus on economic reality is meant to cut through formalistic trappings to get at the heart of the relationship.\textsuperscript{142} In \textit{Secretary of Labor v. Lauritzen},\textsuperscript{143} for example, the court held that migrant workers on a pickle farm were employees because they “depend on the [employer’s] land, crops, agricultural expertise, equipment, and marketing skills.”\textsuperscript{144}

Some commentators have argued that the economic realities test should replace the control test, because its focus on economic dependence provides more protection to vulnerable workers.\textsuperscript{145} However, in the United States the test has thus far remained limited to the FLSA and FMLA. The concept of dependency has been more successful in foreign jurisdictions, which have adopted concepts such as “dependent contractors” and “employee-like” persons in certain worker-protection regimes.\textsuperscript{146} In the United Kingdom, for example, several employment law regimes have expanded to include those working relationships “whereby the individual undertakes to do or perform personally any work or services for another party to the contract whose status is not by virtue of the contract that of a client or customer of any profession or business undertaking carried on by the individual.”\textsuperscript{147} At present, the extended protections include minimum wage requirements, overtime limitations, grievance processes,

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\item \textsuperscript{142} Mednick, 508 F.2d at 301 (characterizing the ultimate inquiries as: “Is [the worker] the kind of person meant to be protected by the F.L.S.A.? Is he dependent upon finding employment in the business of others . . . , [one of] those who themselves are least able in good times to make provisions for their needs when old age and unemployment may cut off their earnings?” (second alteration in original) (internal quotation marks omitted)).
\item \textsuperscript{143} Lauritzen, 835 F.2d at 1529.
\item \textsuperscript{144} Id. at 1538.
\item \textsuperscript{145} See, e.g., U.S. COMM’N ON THE FUTURE OF WORKER-MGMT REL., THE DUNLOP COMM’N ON THE FUTURE OF WORKER-MANAGEMENT RELATIONS 63 (1994), available at http://digitalcommons.ilr.cornell.edu/cgi/viewcontent.cgi?article=1004&context=key_workplace (“The definition of employee in labor, employment, and tax law should be modernized, simplified, and standardized. Instead of the control test borrowed from the old common law of master and servant, the definition should be based on the economic realities underlying the relationship between the worker and the party benefiting from the worker’s services.”).
\item \textsuperscript{146} Davidov, supra note 10, at 61 (discussing Canada and Germany).
\item \textsuperscript{147} Davidov, supra note 19, at 371 n.54 (quoting Employment Rights Act, 1996, c. 18, § 230(3)(b) (U.K.); National Minimum Wage Act, 1998, c. 39, § 54(3) (U.K.); Working Time Regulations, 1998, § 2 (U.K.); Employment Relations Act, 1999, c. 26, §§ 12(6), 13(1) (U.K.); Part-Time Workers (Prevention of Less Favourable Treatment) Regulations, 2000, § 1 (U.K.) (internal quotation marks omitted)).
\end{itemize}
\end{footnotesize}
and restrictions on wage deductions. However, the definition of “worker” has only extended these protections to an additional set of laborers; it has not replaced the concept of “employee” in the law.

3. The “Entrepreneurial Opportunities” Test

Despite the Supreme Court’s explicit approval of the common law agency test in the context of the NLRA, the D.C. Circuit appears to have adopted a new test based on the “entrepreneurial opportunities” afforded to workers. The circuit first adopted this test in Corporate Express Delivery Systems v. NLRB, in which it held that the determination of employee status should “focus not upon the employer’s control of the means and manner of the work but instead upon whether the putative independent contractors have a significant entrepreneurial opportunity for gain or loss.” The court justified the shift on the following grounds:

[T]he latter factor better captures the distinction between an employee and an independent contractor. For example, as the Board points out, “the full-time cook is regarded as a servant [rather than as an independent contractor] although it is understood that the employer will exercise no control over the cooking.” Similarly, a corporate executive is an employee despite enjoying substantial control over the manner in which he does his job. Conversely, a lawn-care provider who periodically services each of several sites is an independent contractor regardless how closely his clients supervise and control his work. The full-time cook and the executive are employees and the lawn-care provider is an independent contractor not because of the degree of supervision under which each labors but because of the degree to which each functions as an entrepreneur—that is, takes economic risk and has the corresponding opportunity to profit from working smarter, not just harder.

In FedEx Home Delivery v. NLRB, the circuit confirmed this new “entrepreneurial opportunities” test as the proper standard for evaluating employee status. The majority retained the common law agency test as the proper standard, but argued that entrepreneurial opportunity was “an important animating principle by which to evaluate [the common law agency] factors.” The court explicitly rejected control

148 See Davidov, supra note 19, at 371.
149 292 F.3d 777 (D.C. Cir. 2002).
150 Id. at 780 (internal quotation marks omitted).
151 Id. (second alteration in original) (quoting Restatement (Second) of Agency § 202(1) cmt. d (1958)).
152 563 F.3d 492 (D.C. Cir. 2009).
153 Id. at 497.
as the primary factor, citing its indefiniteness as well as its failure to capture the essence of employee status.\textsuperscript{154} The dissent found that the majority’s “entrepreneurial opportunities” test failed to follow the Supreme Court-approved common law test,\textsuperscript{155} a contention supported by other commentators.\textsuperscript{156}

4. The “Entrepreneurial Control” Test

The Restatement (Third) of Employment Law has adopted a variation of the “entrepreneurial opportunities” test by defining “employee” as one who works in the interests of the employer when “the employer’s relationship with the individual effectively prevents the individual from rendering the services as part of an independent business.”\textsuperscript{157} The Restatement further refines this as follows: “An individual renders services as part of an independent business when the individual in his or her own interest exercises entrepreneurial control over the manner and means by which the services are performed.”\textsuperscript{158} The Restatement commentary agrees with the FedEx court that the common law right-to-control test “looks not only to the principal’s control of the physical details of how the service provider performs the work but also to other factors relevant to whether the service provider has entrepreneurial control over the manner and means by which the services are performed.”\textsuperscript{159} Thus, while both the D.C. Circuit and the Restatement focus on entrepreneurialism, the court’s “entrepreneurial opportunities” test focuses on whether employees have a legal right to pursue

\textsuperscript{154} Id. (“It was as if the sheet music just didn’t quite match the tune.”).

\textsuperscript{155} Id. at 510 (Garland, J., dissenting in part).

\textsuperscript{156} See, e.g., Jeffrey M. Hirsch, Employee or Entrepreneur?, 68 WASH. & LEE L. REV. 353, 357 (2011) (arguing that the D.C. Circuit’s new test “directly contradicts Supreme Court precedent”).

\textsuperscript{157} Restatement (Third) of Employment Law, § 1.01(1) (Tentative Draft No. 2, 2009), available at http://www.ali.org/00021333/Employment%20Law%20TD%20No%202%20Revised%20September%202009.pdf. The full definition is:

Unless otherwise provided by law or by § 1.02 or § 1.03, an individual renders services as an employee of an employer if (a) the individual acts, at least in part, to serve the interests of the employer, (b) the employer consents to receive the individual’s services, and (c) the employer’s relationship with the individual effectively prevents the individual from rendering the services as part of an independent business.

\textsuperscript{158} Id. § 1.01(2). Entrepreneurial control is further defined as “control over important business decisions, including whether to hire and where to assign assistants, whether to purchase and where to deploy equipment, and whether and when to service other customers.” Id. § 1.01(3).

\textsuperscript{159} Id. § 1.01 cmt. a.
economic gain outside of the relationship. The Restatement’s test, on the other hand, looks at the degree of entrepreneurial control exercised by the parties within the relationship.\footnote{As the Restatement frames it: “Employees do not provide their services as an independent business.” \textit{Id.}; see \textit{id.}, § 1.01 cmt. d (“The key question is whether a service provider functions as an independent business while performing services on the principal’s behalf.”).}

5. The Purpose Test

Finally, one definition of employment has sought to look past the category itself and instead focus on the underlying purpose of the statutory or common law scheme at issue. As one commentator has asked: “[W]hy should employee status matter at all?”\footnote{Carlson, \textit{supra} note 11, at 299.} Instead of creating a category of “employee” that applies in a variety of different situations, critics contend that courts, regulators, and legislators should focus on the particular purpose of a particular legal regime and should tailor coverage to meet that purpose. In discussing the statutory definition of employee within the FLSA, Judge Easterbrook argued that the statutory purposes of that statute were quite different from the common law concerns at issue in the control test.\footnote{See Sec’y of Labor v. Lauritzen, 835 F.2d 1529, 1543–45 (7th Cir. 1987) (Easterbrook, J., concurring). Judge Easterbrook described the three purposes of the FLSA as preventing workers from working abnormally long hours, spreading work and thereby reducing unemployment, and protecting the overtime workers from themselves. \textit{Id.} In contrast, he described the purpose of vicarious liability as creating proper incentives to take care against harm and to potentially spread the risk of loss. \textit{Id.} He argued: “The reasons for blocking vicarious liability at a particular point have nothing to do with the functions of the FLSA.” \textit{Id.} at 1544.} Instead of having a uniform definition across legal regimes, it would be more appropriate, argued the judge, to develop definitions based on the functions of the particular law.

Although the functional approach has intuitive appeal, it has not gained a foothold in the law. In its initial interpretations of “employee” under the New Deal statutes, the Supreme Court began by using the functional approach.\footnote{See United States v. Silk, 331 U.S. 704, 711–12 (1947) (“The very specificity of the exemptions, however, and the generality of the employment definitions indicates that the terms ‘employment’ and ‘employee,’ are to be construed to accomplish the purposes of the legislation.” (footnote omitted)), \textit{abrogation recognized by} Nationwide Mut. Ins. Co. v. Darden, 503 U.S. 318 (1992); NLRB v. Hearst Publ’ns, Inc., 322 U.S. 111, 124 (1944) (stating that the definition of “employee” under the NLRA “‘must be read in light of the mischief to be corrected and the end to be attained’” (quoting S. Chi. Coal & Dock Co. v. Bassett, 309 U.S. 251, 259 (1940))).} However, Congress soon moved to amend both the NLRA and the Social Security Act to reinstate the
common law control test. The deeper theoretical problem for the functional or purpose test is its abandonment of any common notion of employment. If certain regimes are based on the notion of “employee” to determine the extent of coverage, then arguably the concept of employment is part of the overall system of regulation. The purpose-oriented approach seeks to deny, to a greater or lesser extent, the theoretical basis for this commonality. And yet the concept of employment retains rhetorical and policy force. Indeed, even proponents of the function or purpose test concede that Congress has continually gone back to the “employee” category to shape the contours for various areas of the law. Accordingly, the biggest problem for a truly purpose-oriented theory of employment is that it has no theory of employment at all.

One variation on the purpose test is to construct a hybrid version in which a core notion of employment is matched with various additions to the definition depending on the context. The United States has a limited version of this approach, as the common law definition is widely used, but the FLSA and FMLA expand to protect a wider range of workers based on the notion of dependency. But even such flexible approaches need a core vision of employment to provide consistency amidst the permutations. As such, it relies on the notion of employment to provide a category, even if some variations on that category are permitted in individualized instances.


165 See Carlson, supra note 11, at 300 (“The courts, of course, cannot abandon employee status as a test as long as Congress and state legislatures continue to make employee status the clearly stated basis of statutory coverage.”).

166 See, e.g., Guy Davidov, The Reports of My Death Are Greatly Exaggerated: ‘Employee’ as a Viable (Though Over-used) Legal Concept, in Boundaries and Frontiers of Labour Law 133, 151 (Guy Davidov & Brian Langille eds., 2006) (“An appropriate balance is to separate protective labour and employment regulations from other areas of law in which the concept of employee is used, such as tort law and taxation; and maintain a unified definition of ‘employee’ for protective labour and employment regulations, based on their common goals, while allowing room for extensions or exceptions in particular instances.”).

167 See id. (“While I wholeheartedly share the view that the concept of employee should be interpreted purposively, and that the concept can have different meanings in different contexts, dismantling the concept altogether takes this approach too far.” (footnote omitted)).
B. Defining “Scope of Employment”

Unlike the competing definitions for the term “employee,” the term “scope of employment” has not been the subject of various theoretical approaches. The term is not generally used in labor and employment statutes, as in most cases the nature of the rights provided to employees guarantees that those rights concern activities within the scope of employment. The one primary exception is workers’ compensation, which only provides protections against injuries incurred within the scope of employment. Outside of labor and employment law, employers are only liable for the torts and crimes of their employees in such actions as are taken within the scope of employment. And intellectual property protections generally only apply to works made within the scope of employment.

Scope of employment is defined as that zone of conduct in which the employee is performing her job duties. The doctrinal definition for “scope of employment” can be quite detailed. For example, the Restatement (Second) of Agency has two provisions devoted to defining scope of employment, both with lengthy lists of factors. See Restatement (Second) of Agency § 228(1) (1958) (defining conduct as within the scope of employment “if, but only if: (a) it is of the kind he is employed to perform; (b) it occurs substantially within the authorized time and space limits; (c) it is actuated, at least in part, by a purpose to serve the master, and (d) if force is intentionally used by the servant against another, the use of force is not unexpectable by the master”); id. § 229(2) (“In determining whether or not the conduct, although not authorized, is nevertheless so similar to or incidental to the conduct authorized as to be within the scope of
employees’ duties as excluding all torts, statutory violations, or criminal activity have generally been unavailing. Under the doctrine of respondeat superior, if the employee is on the job or within a zone of activity related to the employment duties, the employer will generally be liable for the employee’s tort, regardless of the employer’s efforts to define such conduct as outside of the employee’s duties or authority. Instead, courts have adopted something along the lines of a foreseeability test, in which the employer is liable if the employee’s actions are in some way foreseeable. In two famous cases involving drunken sailors, both Judge Hand and Judge Friendly found employers liable for acts of violence to person and property taken by intoxicated employees. In both cases, however, the courts found that the actions were taken within the sailors’ overall context of employment and that therefore the employer was liable. Moreover, an employer may be liable for employee actions taken outside of the scope of employment if the master retains some level of responsibility (through intent, recklessness, or non-delegable duty) or if the employee was aided in some way by apparent authority or the agency relationship itself. Given “the proclivity of seamen to find solace

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175 Ira S. Bushey & Sons, 398 F.2d at 172; Nelson, 86 F.2d at 732.

176 RESTATEMENT (SECOND) OF AGENCY § 219(2) (1958) (“A master is not subject to liability for the torts of his servants acting outside the scope of their employment, unless: (a) the master intended the conduct or the consequences, or (b) the master was negligent or reckless, or (c) the conduct violated a non-delegable duty of the
for solitude by copious resort to the bottle while ashore,” their acts of violence—while regrettable and unauthorized—were sufficiently foreseeable to be part of the costs of doing such business.\textsuperscript{177}

As a result, “scope of employment” categorization questions have usually concerned not whether the particular employee is following the script of her particular contractual relationship with the employer, but rather whether the activity is part and parcel of the overall employment relationship.\textsuperscript{178} The employer is expected to absorb the costs of doing business as a firm, which includes a certain level of employee activity that may not directly inure to the employer’s benefit. As the Restatement (Second) of Agency put it, the “ultimate question” in determining the scope of employment is “whether or not it is just that the loss resulting from the servant’s acts should be considered as one of the normal risks to be borne by the business in which the servant is employed.”\textsuperscript{179} Or, as then-Judge Cardozo put it, \begin{quote}
The risks of injury incurred in the crowded contacts of the factory through the acts of fellow workmen are not measured by the tendency of such acts to serve the master’s business. Many things that have no such tendency are done by workmen every day. . . . The test of liability is the relation of the service to the injury, of the employment to the risk. \textsuperscript{180}
\end{quote}

\begin{footnotes}
\item \textsuperscript{177} Ira S. Bushey & Sons, 398 F.2d at 172. The Restatement (Second) of Agency has a complex set of interrelated provisions attempting to define scope of employment. Along with a ten-factor test for determining whether certain kinds of unauthorized acts may fall within the scope of employment, Restatement (Second) of Agency § 229(2) (1958), the Restatement has separate provisions on criminal or tortious conduct, id. § 231, failures to act, id. § 232, conduct not for the purpose of serving the master, id. § 235, and instrumentalities of employment used outside of the relationship, id. § 238. Another instance along this boundary is whether the employer is liable to an unauthorized passenger. See Rahman v. State, 246 P.3d 182, 189 (Wash. 2011) (finding employer liable for injury to unauthorized passenger), superseded by statute, 2011 Wash. Sess. Laws, ch. 82, 754–55 (codified at Wash. Rev. Code Ann. § 4.92.180 (West 2011)) (absolving employer of liability for unauthorized passenger).
\item \textsuperscript{178} See Alan O. Sykes, The Boundaries of Vicarious Liability: An Economic Analysis of the Scope of Employment Rule and Related Legal Doctrines, 101 Harv. L. Rev. 563, 609 (1988) (“The scope of employment limitation upon respondeat superior liability may be understood in many instances as a way to limit the employer’s liability to torts that are ‘caused’ by the business enterprise.”).
\item \textsuperscript{179} Restatement (Second) of Agency § 229 cmt. a (1958).
\item \textsuperscript{180} Leonbruno v. Champlain Silk Mills, 128 N.E. 711, 712 (N.Y. 1920).
\end{footnotes}
III. EMPLOYEES AND THE THEORY OF THE FIRM

Although we think of employees as defined by their work or labor, the legal definitions of “employee” have much more to do with the relationship between the individual worker and the person or entity for whom she works. Employment is not simply labor; it is labor within a particular context. In the modern economy, employees always work within the context of an economic firm. In fact, it is my contention that the firm itself creates the employment relationship. This Part examines how the theory of the firm in economic and organizational literature has focused on the employment relationship, and how being an “employee” really means providing one’s labor within the context of a firm.

Employees have been central to our conception of the firm from the start. In early neoclassical economics, the theory of firm was quite rudimentary; it simply saw the firm as a black box which took in inputs and produced outputs. No further dissection was undertaken. However, this theory did differentiate between what was inside the firm and what was outside: employees and capital assets were inside, while customers and suppliers were outside.\textsuperscript{181} Although this conception of the firm was useful in early economic modeling and retains that purpose even today, it was ripe for a reinvestigation that endeavored to give it substance.

Ronald Coase kicked off the exploration of the internal workings and purpose of the firm in \textit{The Nature of the Firm}.\textsuperscript{182} In an oft-quoted passage, Coase framed the issue this way:

\begin{quote}
Outside the firm, price movements direct production, which is co-ordinated through a series of exchange transactions on the market. Within a firm, these market transactions are eliminated and in place of the complicated market structure with exchange transactions is substituted the entrepreneur-co-ordinator, who directs production. It is clear that these are alternative methods of co-ordinating production. Yet, having regard to the fact that if production is regulated by price movements, production could be carried on without any organisation at all, well we might ask, why is there any organisation?\textsuperscript{183}
\end{quote}

Coase’s answer was that the price mechanism can be costly.\textsuperscript{184} For certain transactions, it is cheaper to simply direct the production to

\begin{footnotesize}
\begin{itemize}
  \item Coase, supra note 12.
  \item Id. at 388 (footnote omitted).
  \item Id. at 390–92.
\end{itemize}
\end{footnotesize}
occur rather than contracting separately for it. In order to avoid the transaction costs of contracting, such transactions will occur within a firm rather than on an open market.\footnote{185}

Of course, the firm-based transactions described by Coase involve the purchase of labor for a particular endeavor. In explaining these transactions, Coase stated: “If a workman moves from department Y to department X, he does not go because of a change in relative prices, but because he is ordered to do so.”\footnote{186} The relationship between the entrepreneur-coordinator and the employee is the primary distinction between the firm and the market. It is the reason for the firm’s existence. Coase seemed to be arguing that firms would be unnecessary but for the need to remove the employment relationship from the vagaries of market transactions.

This conclusion is cemented when Coase considered “whether the concept of a firm which has been developed fits in with that existing in the real world.”\footnote{187} His answer? “We can best approach the question of what constitutes a firm in practice by considering the legal relationship normally called that of ‘master and servant’ or ‘employer and employee.’”\footnote{188} He then quoted at length from a treatise concerning the common law “control” test, which provided that “‘[t]he master must have the right to control the servant’s work, either personally or by another servant or agent.’”\footnote{189} Coase concluded: “We thus see that it is the fact of direction which is the essence of the legal concept of ‘employer and employee,’ just as it was in the economic concept which was developed above.”\footnote{190} For Coase, the firm was defined by the employer-employee relationship.\footnote{191}

In an important response to Coase’s work, Armen Alchian and Harold Demsetz also focused on the relationship of employees with other participants within the structure of the firm.\footnote{192} However, they

\footnote{185} Id.
\footnote{186} Id. at 387.
\footnote{187} Id. at 403.
\footnote{188} Id.
\footnote{189} Id. at 404 (quoting Frances Raleigh Batt, The Law of Master and Servant 6 (1933)).
\footnote{190} Id.
\footnote{191} See Orts, supra note 18, at 296–97.
\footnote{192} Alchian & Demsetz, supra note 17, at 777 (“When a lumber mill employs a cabinetmaker, cooperation between specialists is achieved within a firm, and when a cabinetmaker purchases wood from a lumberman, the cooperation takes place across markets (or between firms).”).}
argued that Coase’s focus on control, authority, and direction was misleading. Instead, they framed their argument in these terms:

Telling an employee to type this letter rather than to file that document is like my telling a grocer to sell me this brand of tuna rather than that brand of bread. I have no contract to continue to purchase from the grocer and neither the employer nor the employee is bound by any contractual obligations to continue their relationship. Long-term contracts between employer and employee are not the essence of the organization we call a firm.

Alchian and Demsetz’s critique of Coase’s theory does not mean that employees are no longer central to the idea of the firm. Instead, they argue that the importance of the firm (as separate from the market) stems from the need to coordinate production in the midst of a variety of inputs. The need for a system of team production is what separates firms from markets. Alchian and Demsetz defined team production as “production in which 1) several types of resources are used and 2) the product is not a sum of separable outputs of each cooperating resource.” As a result, team production is used when the coordinated effort increases productivity, after factoring out the costs associated with monitoring and disciplining the team.

Although Alchian and Demsetz did not endorse Coase’s model of the firm, their model also revolves around the role of the employee within the firm. The primary concern of the team production model is making sure that the team members do not shirk their responsibilities to the team. The inability to measure individual contributions to productivity is what makes the firm an efficient alternative to markets, but it is also the firm’s central governance problem. Alchian and Demsetz argued that a specialized, independent monitor may be the best way of insuring that the team members all contribute appropriately and are rewarded appropriately. That central monitor—the recipient of the residual profits—would be the firm. Although Coase as well as Alchian and Demsetz personified this monitor in the role of an entrepreneur-coordinator, such a collapse of powers into one human being is only possible in the smallest of firms. In order to

193 “To speak of managing, directing, or assigning workers to various tasks is a deceptive way of noting that the employer continually is involved in renegotiation of contracts on terms that must be acceptable to both parties.”

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195 Id. at 777–78.

196 Id. at 779.

197 Id. at 780.

198 Id. at 782–83.
meet the criteria set down by the model, the central component of team production is the firm itself: a “person” who contracts for all other team inputs.

It could be argued that Alchian and Demsetz conceived of a firm detached from employees, since the Alchian-Demsetz monitor must be outside the production process while being able to negotiate with all team members for their input and compensation. However, unless the “firm” is a sole proprietor, that monitor is merely a mechanism for providing coordination of inputs. And employees are the primary source of the inputs. Thus, the Alchian-Demsetz team production model does not exclude employees from the definition of the firm. Although their model, with its focus on “inputs,” broadens the scope of the firm to include investors as well as employees, the purpose of the Alchian-Demsetz firm remains the management of employees through the coordination of team production.

As theorists moved beyond these foundational works and into empirical research, the identification of transaction costs, monitoring costs, and team production have remained central concepts. Using the transaction-costs model, Oliver Williamson and others have identified the types of contractual difficulties that are likely to lead to firm governance, rather than market solutions. In situations where contributions and compensation can be harder to define, the parties will

199 Alchian and Demsetz set forth the following characteristics of the firm: “(a) joint input production, (b) several input owners, (c) one party who is common to all the contracts of the joint inputs, (d) who has rights to renegotiate any input’s contract independently of contracts with other input owners, (e) who holds the residual claim, and (f) who has the right to sell his central contractual residual status.” Id. at 783.

200 Alchian and Demsetz seem to believe that the firm will be represented by a central figure who has claim to the entire residual, and thus an interest in coordinating the firm most efficiently. But they say nothing about who can appoint such a central figure, and they express skepticism about the ability of shareholders to perform the monitoring function. Rather than characterize shareholders as owners, they argue that shareholders should be viewed merely as investors, like bondholders, albeit “more optimistic” ones. They ask:

In sum, is it the case that the stockholder-investor relationship is one emanating from the division of ownership among several people, or is it that the collection of investment funds from people of varying anticipations is the underlying factor? If the latter, why should any of them be thought of as the owners in whom voting rights, whatever they may signify or however exercisable, should reside in order to enhance efficiency? Why voting rights in any of the outside, participating investors?

Id. at 789 n.14.

201 Oliver E. Williamson, The Economic Institutions of Capitalism (1985) (discussing transaction costs economics); Jeffrey T. Macher & Barak D. Richman,
be left with incomplete contracts that require a governance structure to prevent opportunism. This opportunism will be particularly problematic where one or both of the parties must invest significant resources in assets specific to the particular firm, project, or transaction. This asset specificity makes the parties susceptible to hold-ups from their contractual partners in the absence of a system of governance. Firms can be useful in providing the structures that deter opportunism.202

The focus on assets has carried over into the “property rights” theory of the firm. This theory, developed in a series of articles by Grossman, Hart, and Moore, argues that firms are necessary as a repository of property rights for assets used in joint production.203 By owning the property outright, the firm prevents the problem of the commons (in which no one holds property rights over valuable assets) as well as the problem of the anticommons (in which property rights are divvied up amongst too many disparate actors). The Grossman-Hart-Moore model dictates that the firm should be owned by those who contribute the most valuable and most asset-specific property to the joint enterprise. They are not only most necessary to the firm’s success; they are also the most vulnerable to hold-up problems as the joint enterprise moves forward in time.

These theories have not focused on the role of the employee in the firm, instead focusing on contracts and property rights. But the role of the employee in these models still remains critical. Although the property rights discussed in the model are generally nonhuman assets, the assets are “the glue that keeps the firm together”204 and thus keep employees within the firm. Hart poses the following hypothetical: if firm 1 acquires firm 2, what is to stop workers at former firm 2 from quitting and forming a new entity?

For firm 1’s acquisition of firm 2 to make any economic sense, there must be some source of firm 2 value over and above the workers’ human capital, i.e. some ‘glue’ holding firm 2’s workers in place. This source of value may consist of as little as a place to meet; the
firm’s name, reputation, or distribution network; the firm’s files, containing important information about its operations or its customers; or a contract that prohibits firm 2’s workers from working for competitors or from taking existing clients with them when they quit. . . . [W]ithout something holding the firm together, the firm is just a phantom. 205

Thus, the property-rights theory of the firm is designed in part to explain why the firm’s employees remain within the firm. 206

In the transaction costs model, employees’ contributions must be recognized as assets of both the firm and the employee—often described as “human capital.” Some types of human capital are transferable, such as education or general skills, but other types are specific to the firm and generally worthless outside it. To the extent an employee has invested in firm-specific skills, she is subject to opportunist behavior by the firm, since she cannot credibly threaten to depart and take those skills to a different firm. In the transaction-cost model, employees may be precisely the vulnerable yet valuable contributors to the joint enterprise who are most vulnerable to opportunist behavior. 207

Along these lines, Rajan and Zingales have proposed an “access” model of power within the firm. 208 The model defines a firm “both in terms of unique assets (which may be physical or human) and in terms of the people who have access to these assets.” 209 Access to the unique assets is what defines the power of the individuals within and outside of the firm. Rajan and Zingales define access as “the ability to use, or work with, a critical resource.” 210 Examples of critical resources include machines, ideas, and people. 211 As Rajan and Zingales make clear, “The agent who is given privileged access to the

205 Id. (footnotes omitted).
206 But cf. Raghuram G. Rajan & Luigi Zingales, Power in a Theory of the Firm, 113 Q.J. ECON. 387, 388 (1998) (“The property rights view does not consider employees part of the firm because, given that employees cannot be owned, there is no sense in which they are any different from agents who contract with the firm at arm’s length.”).
207 Indeed, Margaret Blair offers the following critique: “The tendency in the transactions cost literature has been to recognize that firm-specific human capital raises similar questions, but then to sidestep the implications of these questions for corporate governance.” Margaret M. Blair, Firm-Specific Human Capital and Theories of the Firm, in EMPLOYEES AND CORPORATE GOVERNANCE 58, 66 (Margaret M. Blair & Mark J. Roe eds., 2000).
208 Rajan & Zingales, supra note 206.
209 Id. at 390.
210 Id. at 388.
211 Id.
resource gets no new residual rights of control. All she gets is the opportunity to specialize her human capital to the resource and make herself valuable.”\[212\] Combined with her right to leave the firm, access gives the employee the ability “to create a critical resource that she controls: her specialized human capital.”\[213\] Control over this critical resource is a source of power. Rajan and Zingales argue that “[s]ince the amount of surplus that she gets from this power is often more contingent on her making the right specific investment than the surplus that comes from ownership, access can be a better mechanism to provide incentives than ownership.”\[214\] Given the importance of access, the role of the firm is to allocate access efficiently amongst the firm’s agents.\[215\]

Recent scholarship has taken the role of human capital even further. One aspect of this capital—knowledge—has served as the basis for a new set of approaches to the firm.\[216\] Knowledge is defined both as explicit sets of formal information as well as the ability to apply a repository of unspecified information in developing an answer or approach to a particular problem.\[217\] As one set of knowledge-based theorists explains, “The way a firm develops the knowledge it will use in its production process and the extent that the firm can bind this knowledge to its structure will influence its organizational structure.”\[218\] Rather than emphasize the ownership of physical assets,

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\[212\] Id.
\[213\] Id.
\[214\] Id.
\[215\] Id. at 391.

\[217\] For a discussion of explicit versus tacit knowledge, see Ikuiro Nonaka et al., A Theory of Organizational Knowledge Creation: Understanding the Dynamic Process of Creating Knowledge, in HANDBOOK OF ORGANIZATIONAL LEARNING & KNOWLEDGE 491, 494 (Meinolf Dierkes et al. eds., 2001). Gorga and Halberstam classify knowledge into three types: “knowledge embedded in physical assets,” “knowledge embedded in the organizational structure or the group of individuals that constitute the firm[,]” and “specialized knowledge embedded in the individual.” Gorga & Halberstam, supra note 216, at 1141–42.

\[218\] Gorga & Halberstam, supra note 216, at 1140.
which can be fungible and nonspecific, the knowledge-based theory focuses on the need to produce, distribute, and ultimately retain valuable knowledge-based assets within the firm.\textsuperscript{219} Choices between centralized and multi-divisional organizational structures,\textsuperscript{220} or between covenants not to compete and employee stock options,\textsuperscript{221} are based on the management of knowledge within the firm. Along the same lines, a capability-based theory of the firm focuses on firm-specific knowledge and learning that can be translated into joint production.\textsuperscript{222} This theory also emphasizes the role of employees as holders of the firm’s capabilities.\textsuperscript{223}

Knowledge-based theories of the firm serve as something of a bridge between the economic, organizational, and sociological theories as to the nature of the firm.\textsuperscript{224} Management historians such as Alfred Chandler have long considered the actual roles of employees within the firm to be the centerpiece of firm dynamics.\textsuperscript{225} Organizational theory has built upon these insights and carried them over to today’s firms, which generally offer flatter hierarchical structures and more work in teams. In fact, one set of scholars examined the role of the firm as a “collaborative community” in which employees work together toward common goals.\textsuperscript{226} Such a firm must have a shared ethos of contribution to a collective purpose and the success of others;\textsuperscript{227} it must be structured so as to allow for flexible organiza-

\textsuperscript{219} Id. at 1137 (criticizing the property rights theory for failing to account for the importance of employees as assets).

\textsuperscript{220} Id. at 1173–83.

\textsuperscript{221} Id. at 1183–92; cf. Oren Bar-Gill & Gideon Parchomovsky, Law and the Boundaries of Technology-Intensive Firms, 157 U. PA. L. Rev. 1649, 1686–88 (2009) (discussing the role of covenants not to compete in managing innovation within the firm).


\textsuperscript{223} Id. at 139.

\textsuperscript{224} See, e.g., Rajan & Zingales, supra note 206, at 424–25 (arguing that there is “ample opportunity for gains from trade” between economics and sociology, as sociologists have studied the role of power within organizations “in some detail”); D. Gordon Smith & Brayden G. King, Contracts as Organizations, 51 Ariz. L. Rev. 1, 1 (2009) (comparing organizational theories to the traditional legal and economic theories of contract and firm).

\textsuperscript{225} See, e.g., Alfred D. Chandler, Jr., The Visible Hand 1–12 (1977) (discussing the role of middle- and upper-management in coordinating large firms and their employees).


\textsuperscript{227} Id. at 39–43.
tional boundaries but highly specialized knowledge;\textsuperscript{228} it must base status on knowledge and expertise, rather than hierarchy;\textsuperscript{229} and it must create an identity of independence and personal consistency.\textsuperscript{230} Such collaborative-community firms are contrasted with hierarchical firms, which manage employees with a traditional command-and-control structure,\textsuperscript{231} as well as market-based firms, which break down traditional firm barriers through outsourcing and contingent workers.\textsuperscript{232} This vision of the future of the firm seeks to develop the optimal approach to the relationship between a firm and its employees. Indeed, the driving consideration seems to be managing employees in a knowledge-based economy in the most efficient and productive way possible.\textsuperscript{233}

There are theories of the firm, such as the “nexus of contracts” approach, that do not single out employees for special primacy of place.\textsuperscript{234} On the whole, however, approaches to the nature of the

\begin{footnotesize}
\begin{enumerate}
\item[228] Id. at 44.
\item[229] Id.
\item[230] Id. at 54–59.
\item[231] Id. at 64–65 (discussing the Wal-Mart approach).
\item[232] Id.
\item[233] See, e.g., id. at 74 (“One major danger [to our economic future] is the hardening of the current dualistic structures: strong mechanisms of collaboration and community for high-end 'knowledge workers' alongside coercive hierarchical and market control over the lower tier of the workforce.”).
\item[234] Tellingly, perhaps, the theory of the firm which has had the most purchase on corporate law cares least about the role of employees within the firm. The “nexus of contracts” theory argues that the firm is merely a central hub for a series of contractual relationships. See Michael C. Jensen & William H. Meckling, \textit{Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure}, 3 J. FIN. ECON. 305, 310 (1976). Jensen and Meckling emphasize that the firm is a “legal fiction[ ]”; it is “not an individual” and has no real independent existence. Id. at 310–11. Although Jensen and Meckling’s model focuses on agency costs, it largely ignores employees as a whole. The agents in question are the upper-level managers who are tasked to do the bidding of principals. Their theory defines agency costs as the costs associated with “the monitoring expenditures by the principal,” “bonding expenditures by the agent,” and “the residual loss.” Id. at 308. The monitoring they describe does look a lot like the “control” that Coase focused on as the key element in defining the firm. However, Jensen and Meckling turn their attention to the relationship between shareholders (principals) and management (agents), rather than the relationship of employees to the firm. Id. at 310. Their model seeks to describe the finance structure of the firm in conjunction with the management structure of corporate governance. The nexus of contract theory is thus not really a theory of the firm at all, but rather a theory of agency costs within a certain type of firm. See, e.g., Oliver Hart, \textit{An Economist’s Perspective on the Theory of the Firm}, 89 COLUM. L. REV. 1757, 1759 (1989) (“Principal-agent theory . . . fails to answer the vital questions of what defines a firm and where the boundaries of its structure are located.”); McInerney, supra note 222, at 137–38 (“Scholars working in this paradigm do not offer theories of the firm so much
firm within a market economy have developed the role of employees and employment within the firm, as opposed to "independent" contracting parties outside of the firm. This insight has been recognized from Coase up through the knowledge-based theories of the present. As such, theories of the firm can serve as an intellectual foundation for the concept of "employee" and "employment" within the law. The following Part is an initial effort at building this foundation.

IV. Employment as Participation in a Firm

A. Participation as Theory

Coase recognized that in looking for the theory of the firm out in the real world, one should look not at the law of entities, but rather the law of employment. Although business organizations are the "firms" considered in Coase's musings, business organizations themselves did not represent the natural boundaries of a firm for economics purposes. Rather, firms were represented by the relationship between the legal entity and its employees. The relationship between employer and employee was the nonmarket interaction that justified the creation of the firm in the first place.

The weakness in Coase's analysis, however, was his overemphasis on the concept of "control" within the firm. Yes, an employee can be directed to work on one task rather than another, and an employer can dictate the details of that work in a very close manner. But the nature of the supervision need not be significantly different than the close oversight a general contractor provides to a subcontractor. Moreover, given that most employment contracts are at-will, both the employer and the employee are free to walk away from the relationship at any time. Employees cannot be controlled, at least over any duration, if they are free to walk away at any time. A business with a supplier under a long-term contract has more extensive legal control than an employer does over an at-will employee.

And so it is with the "control" test used in the common law definition of employment. The concept of "control" seems to overstate the power exercised by the employer within the relationship, at least with

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235 Coase, supra note 12, at 388 (discussing the firm in the context of employer-employee relationships).
236 Id. at 405.
237 Id. at 393.
238 See supra note 31 and accompanying text.
respect to supervision. An employee can be given a relative degree of freedom on the job but still be considered an employee, while an independent contractor can be given exacting specifications and still be outside the firm. Even the Restatement (Second) of Agency recognizes that the degree of actual supervisory control is a poor proxy for employment.\textsuperscript{239} Moreover, the issue of “control” implies that those employees with more power within the organization are less like other employees, as they are less controlled than they are controlling. However, when it comes to traditional agency doctrine, the power of the employee within the organization is irrelevant to their status as an employee. As the Restatement confirms, “ship captains and managers of great corporations are normally superior servants, differing only in the dignity and importance of their positions from those working under them.”\textsuperscript{240}

So if the concept of control is not the best proxy for the employment relationship, what provides a better touchstone? We can look to the Alchian-Demsetz critique of Coase for some answers. Alchian and Demsetz took on Coase’s notion of control by arguing that employees received market direction just as other economic participants did. They argued that the critical purpose behind the firm is the coordination of joint production.\textsuperscript{241} In their model, team production is defined as “production in which 1) several types of resources are used and 2) the product is not a sum of separable outputs of each cooperating resource.”\textsuperscript{242} Firms are used when the team method increases productivity, after factoring out the costs associated with monitoring and disciplining the team.\textsuperscript{243}

The critical insight is that employment is defined not by control, but by participation—participation in team production. It is not that employees are controlled by the firm that makes them employees. It is rather that they are part of a process of joint production, acting together within one unit. The participants in this unit—the firm—

\textsuperscript{239} Restatement (Second) of Agency § 220(1) cmt. d (1958) (“[T]he full-time cook is regarded as a servant [rather than as an independent contractor] although it is understood that the employer will exercise no control over the cooking.”).

\textsuperscript{240} Id. § 220 cmt. a. The Restatement (Third) of Agency seems to recognize this problem more overtly: “In some employment relationships, an employer’s right of control may be attenuated. For example, senior corporate officers, like captains of ships, may exercise great discretion in operating the enterprises entrusted to them, just as skilled professionals exercise discretion in performing their work. Nonetheless, all employers retain a right of control, however infrequently exercised.” Restatement (Third) of Agency § 7.07 cmt. f (2006).

\textsuperscript{241} Alchian & Demsetz, supra note 17, at 777–79.

\textsuperscript{242} Id. at 779.

\textsuperscript{243} Id. at 780.
have cast their lots together to engage in economic activity that would otherwise be extremely difficult to tease out into separate contracts. Because these players are all working together, they are treated as a unit for certain purposes.\textsuperscript{244} The firm is responsible for the actions of its members, and it has responsibility to those members vis-à-vis the fruits of its production process.

This insight is borne out in subsequent theories of the firm. Both the transaction costs model of the firm and the property rights model of the firm focus on the assets of the firm, but these assets can include human capital.\textsuperscript{245} One of the primary functions of the firm under these theories is to organize assets such that employees continue to work at and invest their human capital in the firm.\textsuperscript{246} Thus, the point is to manage employee participation, rather than to control employee conduct. Similarly, the “power” model of the firm developed by Rajan and Zingales revolves around the power of access to critical resources. Both the critical resources and the access provided to them involve the participation of various players within the process.\textsuperscript{247} Finally, knowledge-based theories of the firm look to understand how firms manage the production and utilization of knowledge within the firm.\textsuperscript{248} Such processes are best understood through the lens of joint production and employee participation.

Thus, employment is not about the employer’s control over a particular worker; control is not necessary or sufficient to the employment relationship. Instead, what is needed is placement of the worker within the boundaries of the firm. Such a worker is an employee; one who works outside those boundaries is an independent contractor. Going forward, then, we should look to participation, not control, for our touchstone in the legal doctrine of employment.

\textsuperscript{244} Guy Davidov has recognized that the concept of employee requires a governance structure (such as a firm) outside of the market. He argues that structure is necessary as “a direct result of two combined factors: first, our inclination to join forces and work together with others; and, second, the need to coordinate production to an extent that the market cannot satisfy.” Davidov, supra note 19, at 377–78.

\textsuperscript{245} See supra Part III.

\textsuperscript{246} See supra Part III.

\textsuperscript{247} See Rajan & Zingales, supra note 206, at 388.

\textsuperscript{248} See, e.g., Gorga & Halberstam, supra note 216, at 1128 (“We show how the management of knowledge resources required in mass production and high-tech firms differentially affects their decisional hierarchies, and in certain instances also their compensation and ownership structure.”).
If the key to our understandings of employment is participation—participation, that is, in an ongoing economic enterprise as organized into a firm—then how do we operationalize this as legal doctrine? What would a “participation” test look like? As it turns out, much of the doctrine has already moved in the direction of participation; it just has not been recognized as such. Although the notion of control has dominated the common law test, most of the other factors in that test reflect the degree of participation in the enterprise. Look at these factors in the *Restatement (Second) of Agency*’s test other than control:

(b) whether or not the one employed is engaged in a distinct occupation or business;

(c) the kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of the employer or by a specialist without supervision;

(d) the skill required in the particular occupation;

(e) whether the employer or the workman supplies the instrumentalities, tools, and the place of work for the person doing the work;

(f) the length of time for which the person is employed;

(g) the method of payment, whether by the time or by the job;

(h) whether or not the work is a part of the regular business of the employer;

(i) whether or not the parties believe they are creating the relation of master and servant; and

(j) whether the principal is or is not in business.  

These elements, particularly (b), (e), (f), (h), (i), and (j), examine whether the worker at issue is a participant in a continuing enterprise or an independent actor that works outside of the firm. They are about firm boundaries. Employees are those inside the firm, while independent contractors are outside. Participation, not control, is the common theme.

The “participation” standard also synchronizes better with the modern movement toward an “entrepreneurial opportunities/control” test for employee status. The *Restatement (Third) of Employment Law* describes employees as those who work in the interests of the employer when “the employer’s relationship with the individual effectively prevents the individual from rendering the services as part of an
independent business."250 Nonemployees, on the other hand, exercise "entrepreneurial control over the manner and means by which the services are performed."251 This test may at first seem related to the degree of control exercised by the employer over the details of work, since it discusses control over the manner and means of performance. However, the overall test seems designed to capture whether the worker is engaged with the firm’s business or rather operating independently of the firm. In other words, is the worker part of the firm or part of an independent business? The D.C. Circuit’s description of its “entrepreneurial opportunities” test is similarly firm-oriented: it counsels that the determination of employee status should “focus not upon the employer’s control of the means and manner of the work but instead upon whether the putative independent contractors have a significant entrepreneurial opportunity for gain or loss.”252

Participation within a firm should not be confused with formalistic determinations such as whether the employee is on the payroll or is categorized as an employee by the firm itself. These labels are obviously useful but do not tell the whole story. After all, some firms will use disingenuous labeling with the purpose of avoiding the legal consequences of employment.253 On the other hand, participation must not be defined to include all those who play a role in the firm’s economic life. A too-broad definition of participation will engulf a variety of nonemployees, including members of another firm that is engaging in a joint venture or even a simple contractual relationship with the “employer” firm. For example, a painting company with its own painter-employees is arguably “participating” in the economic enterprise of the firm that hires the company, even if no one would consider its employees to be employees of the hiring firm. A critical component of the participation standard is that an employee must be participating in the ongoing economic enterprise as organized into a particular firm. A painter hired to work at the firm through an independent company may be doing the same painting as an employee

251 Id. § 1.01(2).
252 Corporate Express Delivery Sys. v. NLRB, 292 F.3d 777, 780 (D.C. Cir. 2002) (internal quotation marks omitted).
253 See Carlson, supra note 11, at 298 (”[T]he advantages (to employers) of employing workers who are plausibly not employees motivate a good deal of arbitrary and questionable ‘non-employee’ classification.”); Davidov, supra note 19, at 363 (“Deliberate misclassification is becoming more and more common as a result of an increased emphasis on flexibility and the new pressures of globalization.”).
hired by the firm itself. But the first painter is an employee of the independent painting firm, while the second is part of the ongoing enterprise of the firm itself. Factors in the common law test such as the length of the engagement, the parties named to the contract, the method of payment, and the parties’ beliefs about the relationship all point to the differences between an employee and an independent contracting party, because they show whether the employee is actually an ongoing participant in the enterprise.\textsuperscript{254} Of course, line-drawing problems remain. In particular, workers who would generally be seen as part of the employer’s regular business but have been outsourced to a clearly separate firm would pose tough questions about the meaning of “participation.” However, the participation standard would not override existing boundaries to include workers who were clearly outside the firm, even if the outsourcing were done for purposes of escaping legal ramifications of employment.\textsuperscript{255}

Looking at the areas of law in which employment plays a role, the concept of “participation” arguably does a better job of defining employee status than does control. The doctrine of respondeat superior dictates when a firm is liable for the actions of one of its participants. If control were the touchstone, then liability issues would focus on the extent to which the employees’ actions were controlled by the firm in carrying out the tortious act. Instead, courts have generally provided broad berth to employee actions in finding that they were taken within the scope of employment. Firms are liable for the actions of their employees not because the employees were being controlled, but because the employees were part of a joint enterprise, and that enterprise should bear the costs created by its participants. This justification matches up with the standard theoretical defenses for respondeat superior, which justify the doctrine based on risk-allocative

\textsuperscript{254} See Restatement (Second) of Agency $\S\ 220(2)(b), (f), (g), (i), (j)$ (1958).

\textsuperscript{255} For an argument that an employer’s decision to shift work from employees to outside independent contractors should in some cases constitute a violation of the underlying labor and employment law regime, see Noah D. Zatz, Beyond Misclassification: Tackling the Independent Contractor Problem Without Redefining Employment, 26 A.B.A. J. Lab. & Emp. L. 279, 289 (2011) (“If I am correct, then the right question to ask is not who is an employee, but instead to what extent should firms be able to choose organizational structures that preclude unionization by avoiding having employer-employee relationships at all.”); see also Davidov, supra note 19, at 395–98 (discussing “dependent contractors” as a classification of workers that are not employees but deserve some labor-and-employment-type protections); Brian A. Langille & Guy Davidov, Beyond Employees and Independent Contractors: A View from Canada, 21 Comp. Lab. L. & Pol’y J. 7, 22–29 (1999) (discussing the category of dependent contractors in Canadian law).
or retributivist theories. As argued in the Prosser and Keeton treatise:

A multitude of very ingenious reasons have been offered for the vicarious liability of a master: he has a more or less fictitious “control” over the behavior of the servant; he has “set the whole thing in motion,” and is therefore responsible for what has happened; he has selected the servant and trusted him, and so should suffer for his wrongs, rather than an innocent stranger who has had no opportunity to protect himself; it is a great concession that any man should be permitted to employ another at all, and there should be a corresponding responsibility as the price to be paid for it—or, more frankly and cynically, “In hard fact, the reason for the employers’ liability is the damages are taken from a deep pocket.” None of these reasons is so self-sufficient as to carry conviction, although they are all in accord with the general common law notion that one who is in a position to exercise some general control over the situation must exercise it or bear the loss. . . .

What has emerged as the modern justification for vicarious liability is a rule of policy, a deliberate allocation of a risk. The losses caused by the torts of employees, which as a practical matter are sure to occur in the conduct of the employer’s enterprise, are placed upon that enterprise itself, as a required cost of doing business. They are placed upon the employer because, having engaged in an enterprise, which will on the basis of all past experience involve harm to others through the torts of employees, and sought to profit by it, it is just that he, rather than the innocent injured plaintiff, should bear them; and because he is better able to absorb them, and to distribute them, through prices, rates or liability insurance, to the public, and so to shift them to society, to the community at large.

In other words, because the firm is the locus of joint production, and the employee is engaged in that joint production, the firm should bear the risk. This theory better explains such seemingly strange results as the drunken-sailor cases; even though these employees were acting utterly outside of the control of their firms, they were nev-

256 See T. Batty, Vicarious Liability 100 (1916); Richard A. Posner, Economic Analysis of Law 188 (7th ed. 2007).
257 Keeton et al., supra note 36, at 500–01 (footnotes omitted).
258 See Ira S. Bushey & Sons, Inc. v. United States, 398 F.2d 167, 171–72 (2d Cir. 1968) (“The proper test here bears far more resemblance to that which limits liability for workmen’s compensation than to the test for negligence. The employer should be held to expect risks, to the public also, which arise ‘out of and in the course of’ his employment of labor.” (citation omitted) (internal quotation marks omitted)).
259 See supra Section II.B.
ertheless participants in the firm, and the firm needed to bear the costs of their actions within the scope of employment. A similar theory applies to criminal enterprise liability: the firm is blamed if one of its participating employees engaged in the criminal activity within the scope of employment and with the intent to benefit the firm.\textsuperscript{260} It does not matter whether the employee was “controlled” by the firm in his or her criminal activity; it only matters that the employee was participating in the work of the firm when committing the crime.

The role of employment in intellectual property doctrine also accords more closely to a participation theory than a control theory. Under the work-for-hire doctrine, the employee marks the boundaries of the firm; works made by employees within the scope of their employment are considered property of the firm, while works made by independent contractors are not (by default).\textsuperscript{261} Under the shop-right doctrine, employers enjoy a non-exclusive right to use a patent created by an employee without having to compensate the employee.\textsuperscript{262} A shop right arises when the employee has created the invention on the job using the employer’s materials.\textsuperscript{263} Once again, the firm provides the context: if the employee creates the invention at work while using the employer’s tools, the employer has a right to use that invention without cost.\textsuperscript{264} Because the employee has been engaged in the process of joint production, under circumstances where it may be difficult to separate out each individual contributor’s contributions, the employee has (impliedly) agreed that all joint property belongs to the firm. It is the employees’ participation within the firm—not their control by the firm—that justifies the transfer of property rights from individual to group.

The participation approach matches up with other recent scholarship considering IP rights from the perspective of the theory of the firm.\textsuperscript{265} This scholarship uses both the transaction-costs model and

\textsuperscript{260} See, e.g., United States v. Singh, 518 F.3d 236, 249 (4th Cir. 2008) (“We have recognized that ‘a corporation is liable for the criminal acts of its employees and agents done within the scope of their employment with the intent to benefit the corporation’” (quoting Mylan Labs., Inc. v. Akzo, N.V., 2 F.3d 56, 63 (4th Cir. 1993))).


\textsuperscript{262} Id.

\textsuperscript{263} Fisk, supra note 54, at 118.

\textsuperscript{264} Id.

the property-rights model in demonstrating the connections between intellectual property, employees, and the firm. Using the transaction-costs model, Robert Merges pointed to the concern about employee opportunism and holdups to explain why employers generally hold intellectual property rights over employee inventions.266 Comparing a system of registered patents to a system based on contract and trade secret protections, Paul Heald argued that patent law makes it easier to buy and sell the information at issue.267 The patent buyer need not enter into a costly array of contractual protections in order to keep others (especially the sellers) from using the information and thereby saves on transaction costs.268 Heald also argued that patents facilitate the creation of technical information and the use of that information in team production.269 Patents enable the critical information to be used within the team without fear that one of the team members will defect.270 The alternative would again be costly contracts with all employees in the team.271 Without the need to monitor these contracts, the firm can facilitate team production more efficiently.272

The property-rights theory of the firm explicitly alludes to the importance of intellectual property. In describing the theory, Oliver Hart uses forms of intellectual property as examples of the “glue” that binds employees to the firm.273 The protections for this type of property are designed to manage not only the interactions between firms, but also between the firm and its employees. Dan Burk and Brett McDonnell similarly highlight the way that intellectual property rights balance property interests between firms as well as within firms.274 Employees have an interest in exploiting information they have created on the job, both within the firm and outside the firm when on the job market.275 Patent, copyright, and trade secrets each balance


267 Heald, *supra* note 265, at 476.
268 *Id.* Such contractual efforts would likely encounter difficulties, for example, if one of the seller’s former employees sought to use the information.
269 *Id.* at 487–88.
270 *Id.*
271 *Id.*
272 *Id.* at 480–84. Heald also notes that some companies use patent applications, which must be filed by individuals, as a way of monitoring employee performance. *Id.* at 492–93.
275 *Id.* at 592.
the firm’s needs and the individual employee’s needs in separating employee information “assets” from firm assets. Burk and McDonnell point out that this division mirrors that of agency law and the corporate opportunity doctrine, in that the critical factors are whether the information/opportunity arose in the context of employment with the use of firm resources. Moreover, they point out that the weakest form of intellectual property protection—trade secret doctrine—applies to the type of information most likely to overlap with an employee’s own information capital. This balancing of rights within firms and between firms leads to their “Goldilocks” hypothesis: the level of legal protection of intellectual property rights that minimizes transaction costs will be somewhere between a system that provides strong rights to firms and a system of weak rights for firms. And this calibration of legal rights is necessary to balance individual participation with group production; the degree of control over the individual participants is largely irrelevant.

Finally, the participation theory of employment has explanatory power in areas of labor and employment law. The ability of the firm’s supervisory authorities to control the minute details of work, as opposed to the overall scope of a project, does not explain why employees should be singled out for protection. An employee can still be given largely free reign to create and produce within the firm, and an independent contractor’s work can still be closely supervised and monitored. However, the notion that employees are participating in a common enterprise explains why that enterprise would have certain obligations to those employees within that relationship. The firm is not only responsible for the actions of its employees; it is also responsible to those employees. Employment laws are designed to

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276 Id. at 593.
277 Id. at 595–97.
278 Id. at 609. Employee covenants not to compete are also included, since their impact intersects with intellectual property, particularly trade secrets. See id. at 628–33; see also Bar-Gill & Parchomovsky, supra note 221, at 1686–88 (explaining that covenants not to compete provide indirect protection of innovation).
279 Burk and McDonnell would calculate the level for interfirm transactions independently from the level for intrafirm transactions, although these levels could overlap or even be identical once calculated. Burk & McDonnell, The Goldilocks Hypothesis, supra note 265, at 620–21. Moreover, they indicate that employees are critical not only to intrafirm analysis, but also to interfirm analysis. Id. at 632.
force upon employers certain types of responsibility for their participants. Within the common boundaries of the firm, employers have an obligation to pay minimum wage and overtime; provide family and medical leave; avoid discrimination; bargain with collective representatives; adhere to certain requirements as to retirement and health care benefits; and provide insurance in case of unemployment.281 Employers have the responsibility to provide these things because employees are participants in the employer’s common enterprise.282 Team production justifies obligations from the team to the individual members.283

At the same time, participation theory might help us articulate why our definition of “employee” seems too crabbed or limiting when it comes to certain types of labor and employment protections. For example, employers at the fringes of the labor market have used the structure of the firm to regulate their exposure to wage and hour protections.284 Because the FLSA uses a definition of “employ” that includes “to suffer or permit to work,”285 courts have expanded its definition of “employee” to include workers with some degree of independence from a traditional firm relationship.286 This exception to the general dominance of the “control” test may signal that different definitions of employment are appropriate. However, it may instead be that certain wage and hour regulations should protect workers beyond the employment relationship. Other countries have taken the approach of expanding wage and hour protections to include so-called “dependent contractors,” who may have independence from the firm but not true independence from the economic relation-

281 See Davidov, supra note 19, at 386.
282 Cf. id. at 375–76 (arguing that “labour and employment laws are generally designed to protect workers who appear to require this protection in their relationship with an identifiable employer”).
283 Cf. id. at 394 (“[P]rotective labour and employment laws can be understood to share a basic purpose . . . to minimize the extent of democratic deficits and dependency in work relations and to correct unwanted outcomes of these phenomena.”).
284 For an extensive discussion of this phenomenon, see Glynn, supra note 19, at 207–15.
286 See Nationwide Mut. Ins. Co. v. Darden, 503 U.S. 318, 326 (1992) (noting that the FLSA ‘stretch[es] the meaning of ‘employee’ to cover some parties who might not qualify as such under a strict application of traditional agency law principles’); see also Nichols v. All Points Transp. Corp. of Mich., 364 F. Supp. 2d 621, 630 (E.D. Mich. 2005) (“Because the statutory definition of FMLA, unlike the definition found in ERISA, incorporates the FLSA’s broader definition of ‘employee’ and ‘employ,’ the court will continue to apply the ‘economic realities’ test as described by the Sixth Circuit . . . .”).
ship. Rather than lumping these dependent contractors into the employment relationship, it may make more sense to recognize that wage and hour protections should run to contractual as well as firm relationships. Similarly, employees as well as partners deserve protection against race and sex discrimination, although Title VII only applies to the former. Labor and employment laws provide a diversity of regulatory schemes, and there may be good reasons to extend some of those schemes beyond the common definition of employment. However, it is important first to establish a common notion of employment, in order to give meaning to the category beyond a chameleon-esque placeholder. Participation theory provides the best common definition for the category.

In addition, participation explains why employees themselves have a duty to the firm. The fiduciary obligations of corporate directors are well established: directors owe duties of loyalty, care, and good faith in the exercise of their responsibilities. Delaware recently extended these obligations to corporate officers as well. However, the common law has long maintained that even lower-level employees owe fiduciary obligations to their employer. These obli-

287 See Davidov, supra note 19, at 395–98 (discussing “dependent contractors” as a classification of workers that are not employees but deserve some labor-and-employment-type protections); Langille & Davidov, supra note 255, at 22–29 (discussing dependent contractors in Canadian law).

288 See Glynn, supra note 19, at 227–35.


290 Davidov has arrayed the justifications for workplace regulatory regimes along a spectrum from selective (as to employees) to universalist (as to society as a whole). He cautions that while universalist justifications have a broad appeal, they are insufficiently tethered to the employment relationship to justify workplace regulation. Guy Davidov, The Goals of Regulating Work: Between Universalism and Selectivity, U. TORONTO L.J. (forthcoming 2013) (manuscript at 30–31), available at http://ssrn.com/abstract=2205000.


292 Gandler v. Stephens, 965 A.2d 695, 708–09 (Del. 2009) (“In the past, we have implied that officers of Delaware corporations, like directors, owe fiduciary duties of care and loyalty, and that the fiduciary duties of officers are the same as those of directors. We now explicitly so hold.” (footnotes omitted)); Glynn, supra note 280, at 326 (“[O]fficers and other high-level employees owe fiduciary duties—including a duty of care—to the firm.”).

293 Restatement (Second) of Agency § 387 (1958) (“Unless otherwise agreed, an agent is subject to the duty to his principal to act solely for the benefit of the principal in all matters connected with his agency.”); O’Neill, supra note 32, at 685 (“All employees owe a fiduciary duty of loyalty to their employer—be the employer a sole proprietor, a partnership, a close corporation, or a large, publicly traded corporation.”).
gations are explored in the *Restatement (Third) of Employment Law*, which provides that “[e]mployees owe a duty of loyalty to their employer in matters related to the employment relationship.”294 Employees breach the duty of loyalty by disclosing or using the employer’s confidential information, competing with the employer, or appropriating the property of the employer or engaging in self-dealing.295 Under a control theory of employment, these obligations do not really make any sense—why should those who are more controlled by the firm have an obligation of loyalty to the firm? But the participation theory nicely explains why individual firm members would owe duties to the ongoing enterprise of which they are a part.296

Admittedly, participation theory does not solve a number of extant issues with the definitions of employee and employment. It does not explain why some participants in a common enterprise—family members, for example, or prisoners—are not considered to be employees despite their compensated labor.297 It also does not differentiate between employees who are simply employees and those who are labeled as supervisors, managers, or officers and thus are excluded from the definition of “employee” for certain purposes.298 “Control” is sometimes used as a distinguishing factor in this context: those who are controlled by the firm are employees, while those who control the firm (and/or their coworkers) are not.299 But employees from the

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295 *Id.* § 8.01(b).
296 But cf. Davidov, *supra* note 19, at 386 (arguing that the employee’s duty to “obey” makes the employment relationship “one-sided”).
297 See Noah D. Zatz, *Prison Labor and the Paradox of Paid Nonmarket Work*, in *Economic Sociology of Work*, in 18 RESEARCH IN THE SOCIOLOGY OF WORK 369, 369–70 (Nina Bandelj ed., 2009) (discussing the determination that prison labor is “noneconomic” in nature and is thus not employment); Zatz, *supra* note 6, at 884–92 (discussing the determination by courts that prison labor is not employment because it is “noneconomic” in nature). However, one answer might be that these workers are “participants” in different enterprises: namely, the family and the prison.
298 See, e.g., 29 U.S.C. § 152(3) (2006) (excluding supervisors from the definition of employee); *id.* § 2614(b)(2) (providing an exception to certain FMLA requirements for salaried employees who are “among the highest paid 10 percent of the employees employed by the employer within 75 miles of the facility at which the employee is employed”).
299 See, e.g., Clackamas Gastroenterology Assocs., P.C. v. Wells, 538 U.S. 440, 449–51 (2003) (using the control test to determine whether doctors who were shareholders in a professional corporation counted as employees or were instead employers and thus not categorized as employees).
bottom to the top of the firm’s hierarchy are all participants in the
ongoing economic enterprise; those who have more power within the
firm may, in fact, be even more closely associated with it. The purpose
of the participation standard for employment is to distinguish
between employees and independent contractors—between those
who are inside and outside of the firm. It does not distinguish
between employees as to their roles within the firm; it does not say
which employees can be considered the “employer” for purposes of
certain labor and employment law regimes. In those cases, control
may be a more appropriate guide. However, the fact that courts
have used the control test to distinguish both between employees and
independent contractors, as well as between employees and employ-
ers, provides some indication of the inherent incoherence of the test
as currently constituted.

Control is not necessary in finding a worker to be part of an
organization. Although commentators have included the notion
of being controlled as critical to the concept of employment, such a
requirement (in my view) is unnecessary and limiting. An employee
remains an employee whether in an extremely hierarchical workplace
or in a more collaborative and democratic environment. In fact,
the notion that employees must be controlled—must be deprived of
power within the firm—has perhaps been a self-fulfilling prophecy.
Viewing employees as participants rather than pawns will not only
accord better with the economic reality of the modern workplace.

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300 Davidov, supra note 19, at 381 (“Control is the concept most central to
understanding the organizational aspect of employment relationships.”).

301 Davidov has argued that the lack of participation in the control of the enter-
prise—which he terms “democratic deficits”—is one of the three “axes” of the
employment relationship, along with dependency on the relationship for the fulfill-
ment of certain social and psychological needs and economic dependency that ren-
ders it difficult to spread risks. Id. at 394. However, he specifies that control “does
not necessarily mean control of the employer over every aspect of the production
process.” Id. at 381. Instead, control means “the superior power of the employer vis-
a-vis the employee within their relationship and the resulting inability of the
employee to control her own (working) life.” Id. Although Davidov acknowledges
that these democratic deficits cannot be justified on the grounds of efficiency or
expertise, he nevertheless believes that “democratic deficits exist (to different
extents) in any employment relationship.” Id. at 380.

302 See Adler & Heckscher, supra note 226, at 59–63 (discussing the existence of
collaborative workplace communities within certain firms).

303 Cf. Zatz, supra note 255, at 288 (discussing the role of law in how firms shape
their organizational structures); Zatz, supra note 6, at 866 (discussing the “constitutive
role for employment law with respect to the boundaries of economic life”).

304 See Adler & Heckscher, supra note 226, at 12–13.
but will also send a signal about the proper role of employees within the organization.

C. Participation as Doctrine: Two Examples

An explanation of the “participation” test cannot hope to exhaust the myriad situations in which the test will be called upon to differentiate independent contractor from employee. But applying the test to particular examples may better demonstrate how the test would actually work in practice. This Section examines how the concept of participation might be usefully deployed to categorize two different types of workers: delivery truck drivers and migrant agricultural workers.

The status of delivery truck drivers has arisen in a variety of contexts. The National Labor Relations Board tackled their status in a set of cases, and has gone both ways on employee status depending on variations between the structures of the jobs. In *Roadway Package System, Inc.*, the NLRB found delivery truck drivers working for a nationwide package delivery company to be employees, based on their lack of prior experience, their (de facto) exclusive arrangements with the company, and the uniformity of their operating procedures.305 However, in a companion case, *Dial-A-Mattress Operating Corp.*, the NLRB found the drivers to be independent contractors.306 The Dial-A-Mattress drivers had much more flexibility in choosing and outfitting their trucks, and their trucks displayed the name of each individual trucker’s company.307 The NLRB has used these two cases as lodestars in more recent analyses.308 Rather than focusing simply on the question of control, the NLRB has considered the variety of factors listed in section 220 of the *Restatement (Second) of Agency*.309 And although it

307 Id. at 886–87.
308 See, e.g., St. Joseph News-Press, 345 N.L.R.B. 474, 478 (2005) (“In determining the status of the carriers in this case, we rely on the Board’s analysis in *Roadway and Dial-A-Mattress*.”).
309 The NLRB in *Roadway Package System, Inc.* stated:

While we recognize that the common-law agency test described by the Restatement ultimately assesses the amount or degree of control exercised by an employing entity over an individual, we find insufficient basis for the proposition that those factors which do not include the concept of “control” are insignificant when compared to those that do. Section 220(2) of the Restatement refers to 10 pertinent factors as “among others,” thereby specifically permitting the consideration of other relevant factors as well, depending on the factual circumstances presented. . . . Thus, the common-law agency test encompasses a careful examination of all factors and not just those that involve a right of control.
is not specifically part of the list of factors in section 220, the NLRB has used the presence of entrepreneurial opportunities as another factor in evaluating the independence of the workers. As noted earlier, the D.C. Circuit has focused in on this factor as being determinative. According to the court, the emphasis of the common law test has shifted “away from the unwieldy control inquiry in favor of a more accurate proxy: whether the putative independent contractors have significant entrepreneurial opportunity for gain or loss.” Using this standard, the circuit has found delivery drivers to be independent contractors. The IRS followed this approach in a set of published guidelines on van operators; the agency found that the critical factor is whether the drivers have the potential to realize profit or loss. However, the results have largely been different in respondeat superior cases involving drivers. In those cases, injuries caused by delivery drivers were to be considered part of the costs of doing business for the hiring company. In a recent Eighth Circuit decision, the court held that a tractor-trailer driver may have been a FedEx employee under vicarious liability despite having a separate contractor agreement.

326 N.L.R.B. at 850.
311 See FedEx Home Delivery v. NLRB, 563 F.3d 492, 497 (D.C. Cir. 2009) (“An important animating principle by which to evaluate [the common law] factors . . . is whether the positing presents the opportunities and risks inherent in entrepreneurialism.”); Corporate Express Delivery Sys. v. NLRB, 292 F.3d 777, 780 (D.C. Cir. 2002) (“The full-time cook and the executive are employees and the lawn-care provider is an independent contractor not because of the degree of supervision under which each labors but because of the degree to which each functions as an entrepreneur—that is, takes economic risk and has the corresponding opportunity to profit from working smarter, not just harder.”).
312 FedEx Home Delivery, 563 F.3d at 497 (citation omitted) (internal quotation marks omitted).
315 See id. at 28 (“[W]hen an entity engaged in a commercial activity on its own initiative places a fleet of drivers and automobiles on the public roads to accomplish a part of its core business activity, it is at the least a reasonable inference that accountability and responsibility for the injurious results of negligence in the operation of those automobiles should be borne by the entity engaging in the commercial activity.”).
driver was required “to look and act like [a] FedEx employee[ ] while [he] performed FedEx services, and we believe that these provisions show the extent of FedEx’s control over some details of [the driver’s] work.”317

A participation approach to determining these drivers’ employment status would focus on those factors relevant to their level of participation in the firm. Thus, the most important Restatement factors would be: “(b) whether or not the one employed is engaged in a distinct occupation or business,”318 “(e) whether the employer or the workman supplies the instrumentalities, tools, and the place of work for the person doing the work,”319 “(f) the length of time for which the person is employed;”320 and particularly “(h) whether or not the work is a part of the regular business of the employer.”321 The goal is to look at the shape of the firm and determine whether the workers at issue are properly a part of it. Thus, additional factors would be the extent of work that the worker did for that particular firm over time, as well as the degree to which the firm has “branded” the employee or her equipment for public purposes. In the case of the FedEx drivers before the D.C. Circuit, the delivery drivers wore FedEx uniforms and had FedEx logos on their trucks when making deliveries.322 As the FedEx majority admitted, “once a driver wears FedEx’s logo, FedEx has an interest in making sure her conduct reflects favorably on that logo.”323 As the dissent noted, the drivers “perform a function that is a regular and essential part of FedEx Home’s normal operations,” a factor that other courts had repeatedly cited in their analyses.324

Similarly, migrant agricultural workers are often critical to the operations of the farms on which they work, and thus perform a role that is part of the normal business of the farm company. In other respects, however, certain arrangements can render them independent of the firm that owns the farm itself. As Judge Easterbrook argued in his concurrence in Secretary of Labor v. Lauritzen, the migrant workers in that case more closely resembled independent contractors under the traditional test.325 The farm owner contracted with various migrant worker families to pick cucumbers, generally from July

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317 Id. at 859.
318 Restatement (Second) of Agency § 220(2)(b) (1958).
319 Id. § 220(2)(e).
320 Id. § 220(2)(f).
321 Id. § 220(2)(h).
322 FedEx Home Delivery v. NLRB, 563 F.3d 492, 500 (D.C. Cir. 2009).
323 Id. at 501.
324 Id. at 512 (Garland, J., dissenting) (quoting majority).
325 835 F.2d 1529, 1540 (7th Cir. 1987) (Easterbrook, J., concurring).
through September, paying them a piece rate of one-half of the proceeds that the farm realized on their harvest.\textsuperscript{326} Going through the factors in the “economic realities” test, Judge Easterbrook pointed out the ways in which the migrant workers failed to meet the test.\textsuperscript{327} The methods the workers used in their harvesting were not monitored; the farm only measured the output.\textsuperscript{328} The pickers received a fifty-percent share in that output, and they therefore had what looked like a significant entrepreneurial opportunity at stake.\textsuperscript{329} The length of the engagement was brief, and the workers presumably traveled extensively working with a variety of different farms across the year.\textsuperscript{330} They were not even really dependent on this particular farm, Judge Easterbrook contended, because they were free to pick up and move elsewhere—to a different farm or even an entirely different kind of agricultural product.\textsuperscript{331} Nevertheless, he concurred in the case because he concluded that the purposes of the statutory scheme at issue (the FLSA) called for the workers to be protected.\textsuperscript{332}

The participation test would likely find the workers in \textit{Lauritzen} to be independent contractors. One could argue that their role in the core of the operations, along with the lack of a business entity intermediary (other than a loosely defined “family”), would make them participants in the firm that owned and managed the farm. However, the families did in fact appear to serve as mini-“firms,” with their own structure and process for distributing the gains.\textsuperscript{333} And as Judge Easterbrook found, these families seemed to exist independently of the farm in many important respects.\textsuperscript{334} There is also no “dependency” factor in the participation test. Yes, participation is about the “economic realities” of whether a set of workers is actually participating in a firm, despite how their legal relationship may be structured. But in this case, the realities pointed in many ways toward independence.

While I am arguing that the participation test is the best way to define employees, that does not mean I would not want the \textit{Lauritzen} workers to be excluded from the FLSA. “Suffer or permit to work” means something more expansive than the traditional notion of employment, and therefore the definition should go beyond the con-

\textsuperscript{326} \textit{Id.} at 1532 (majority opinion).
\textsuperscript{327} \textit{Id.} at 1540–43 (Easterbrook, J., concurring).
\textsuperscript{328} \textit{Id.} at 1540 & n.2.
\textsuperscript{329} \textit{Id.} at 1540.
\textsuperscript{330} \textit{Id.} at 1541.
\textsuperscript{331} \textit{Id.}
\textsuperscript{332} \textit{Id.} at 1544 (“The functions of the FLSA call for coverage.”).
\textsuperscript{333} \textit{Id.} at 1532–33 (majority opinion).
\textsuperscript{334} \textit{Id.} at 1540–41 (Easterbrook, J., concurring).
cept of employment itself. Other countries have endeavored to cover this pool of workers who are outside of employment but deserve protection through a category called “workers” or “dependent contractors.”\textsuperscript{335} These laborers do not meet our traditional standards of participation within the firm, but they are sufficiently dependent and vulnerable that they should be encompassed within certain types of protections targeted to vulnerable workers. Guy Davidov has described these workers as meeting the economic axes of dependency and an inability to spread risks, but not the organizational axis of having a democratic deficit.\textsuperscript{336} Because he describes employment as “a structure of governance with democratic deficits,”\textsuperscript{337} Davidov acknowledges that dependent contractors do not meet that definition.\textsuperscript{338} He nevertheless argues that labor and employment law protections should extend to these workers because of the purpose of these protections \textit{vis-à-vis} vulnerable workers.\textsuperscript{339} I agree with Davidov’s result. Employees should be limited to those who participate in firms, but some employment protections (such as the FLSA) should extend to workers like \textit{Lauritzen}’s migrant farm harvesters who, because of their dependency and market-devalued personal capital, risk getting less than the minimum wage or putting their children to work.\textsuperscript{340} But rather than morphing our definition of “employee” to fit the needs of the particu-

\textsuperscript{335} See Davidov, supra note 10, at 57, 61 (discussing the United Kingdom’s “worker” category and Canada’s “dependent contractor” category).

\textsuperscript{336} Davidov, supra note 19, at 395.

\textsuperscript{337} Id. at 377.

\textsuperscript{338} Davidov, supra note 10, at 61–62.

\textsuperscript{339} Davidov, supra note 166, at 151.

lar statutory scheme, we should keep the definition constant and add other categories, such as “dependent contractors,” when appropriate.\footnote{Cf. Davidov, supra note 166, at 151 (arguing for “a unified definition of ‘employee’ for protective labour and employment regulations, based on their common goals, while allowing room for extensions or exceptions in particular instances”). I disagree with Davidov to the extent that I believe the definition of “employee” should be held constant across the law as a whole, and should be based on our conception of employment, rather than the goals of labor and employment regimes.}

\section{The Future of Employment in the Law}

The preceding discussion assumes the continuing vitality of the concept of employment within the law. However, both the employment relationship and the firm itself—at least, in its most common legal persona of the corporation—have questionable long-term prospects. The corporation is under siege by a plethora of new organizational structures, most notably the limited liability company (LLC). When the Treasury moved to “check-the-box” taxation for these new entities, they became viable alternatives to the corporation in a variety of different fields.\footnote{See Treas. Reg. § 301.7701-3 (2004); Larry E. Ribstein, The Rise of the Uncorporation 121 (2010).} The flexibility of the LLC form is in contrast to many of the requirements, state and federal, placed upon the corporation.\footnote{Moreover, when it comes to the public corporation, commentators have suggested that more firms have gone private because of the regulatory requirements layered upon the public corporation. William J. Carney, The Costs of Being Public After Sarbanes-Oxley: The Irony of “Going Private,” 55 Emory L.J. 141, 143 (2006) (discussing evidence that smaller issuers are being forced out of public markets). But see Robert P. Bartlett III, Going Private but Staying Public: Rerexamining the Effect of Sarbanes-Oxley on Firms’ Going-Private Decisions, 76 U. Chi. L. Rev. 7, 10 (2009) (arguing that Sarbanes-Oxley is not to blame for the high-profile “going private” transactions of the last decade).} It seems, perhaps, as if Jensen and Meckling’s “nexus of contracts” model\footnote{Coase, supra note 12, at 388 (discussing the firm in the context of employer-employee relationships).} is coming to life in the LLC, and the corporation’s failure to live up to their model is bringing it down.\footnote{Ribstein, supra note 342, at 119–35.}

The employment relationship is moving from firm to market as well. In the mid-twentieth century, labor economists identified the internal labor market as a deviation from neoclassical labor market theory.\footnote{Stone, supra note 48, at 51–63.} These economists found that employees largely stayed within one firm for their lifetime of employment, and that firms gen-
erally used internal promotion to fill vacancies.347 These findings established an empirical basis for Coase’s notion of the importance of employment to the firm.348 Moreover, internal labor markets are an instantiation of the separateness of the firm from the market; they demonstrate that the firm is truly a different set of economic relationships.349 However, economists are finding that the importance of internal labor markets has been dwindling.350 Beginning in the 1970s, firms began to hire more temporary and contingent workers.351 This trend accelerated through the 1990s, and continues apace.352 Recent reports indicate that the 2008 recession has turned many employees into “permanent” temporary workers; even in 2005, as much as twenty-six percent of the workforce reportedly had “nonstandard” jobs.353 And the effects go beyond low-skill and low-wage employment; executive officers, lawyers, and scientists are all among the temporarily employed.354 Moreover, “outsourcing”—a word of relatively recent vintage—continues to break down relationships that were traditionally within the firm.355 What Alan Hyde said in 1998 continues to be true today: “Increasingly, labor is hired through short-term, market-mediated arrangements that may not be ‘employment’ relations in any legal or technical sense of that word.”356

If the corporation is giving way to a more contractually oriented form of business enterprise, and the employment relationship is dissolving back into the market, then perhaps corporations (or their successor organizational forms) will exist only to structure financial relationships and confer limited liability. There is reason to believe, however, that the firm and the corporation will remain relevant to our economic system. From the organizational perspective, the role of the “uncorporation” remains limited under current law.357 It seems likely

347 Id. at 51–52.
349 STONE, supra note 48, at 52–56.
350 Id. at 67–72.
351 Id. at 68–70.
352 Id. at 74–83.
353 Coy et al., supra note 21, at 35.
354 STEVEN GREENHOUSE, THE BIG SQUEEZE xi–xiii (2008); Coy et al., supra note 21, at 36.
356 Hyde, supra note 23, at 99.
357 RIBSTEIN, supra note 342, at 119.
that not only will the public corporation survive, but it will be made even less contractual after the passage of finance reform legislation.\textsuperscript{358} And in the employment context, the flight from employment seems driven by an effort to avoid employment-related regulations and restrictions, rather than the disappearance of the firm itself.\textsuperscript{359} In fact, many employers are looking to tie their employees even more closely to the firm and its image.\textsuperscript{360} The importance of “brand” for businesses means that employees are critical to reifying and promoting the brand, especially in service industries.\textsuperscript{361} Firms have used branding to draw out psychological commitments from employees that are not reciprocal on the part of the employer.\textsuperscript{362} Participation by enthusiastic employees is becoming more important to the role of the firm, not less.

In fact, it may be that the tide is turning back to a more employee-oriented workplace. Popular management literature emphasizes the importance of the employee.\textsuperscript{363} Small startups, particularly in the tech industry, are once again blurring the line between entrepreneur and employee.\textsuperscript{364} Academia is evolving as well. As discussed earlier, recent research into the theory of the firm has focused on the importance of knowledge-based assets and the distribution of access to those assets within the firm.\textsuperscript{365} As we learn more about the importance of trust, norms, and procedural justice within the corporation, employees will grow even more in importance.\textsuperscript{366}


\textsuperscript{359} See Coy et al., supra note 21, at 35.


\textsuperscript{361} Id.

\textsuperscript{362} Scholars have criticized this branding as too invasive, as it dictates what employees wear, what they say, and what they do when not on the job. See id.; Crain, supra note 22, at 1179–80.

\textsuperscript{363} See, e.g., Tony Hsieh, Delivering Happiness (2010) (discussing Zappos’s approach to employee service).


\textsuperscript{365} See Gorga & Halberstam, supra note 216; Rajan & Zingales, supra note 206.

\textsuperscript{366} See generally Tom R. Tyler & Steven L. Blader, Cooperation in Groups (2000) (discussing the importance of cooperation and procedural justice in groups); Margaret M. Blair & Lynn A. Stout, Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law, 149 U. PA. L. REV. 1735 (2001) (discussing the role of internalized trust in discouraging opportunistic behavior among corporate participants).
It is possible to envision a radically individualized future, in which each worker is a “corporation” unto herself and firms are merely temporary agglomerations within the global market. It is also possible to envision a future in which employees participate at the highest levels of governance, and corporations are tools of team production rather than investor enrichment. Perhaps both of these futures are in store, to varying degrees within different industries. Further exploration into the role of the firm will enable us to better understand these changes and manage them efficiently through the legal system.

CONCLUSION

To better understand the meaning of employment, we need to look to the organizational structures that create the employment relationship. We recognize a category of “employees” because we recognize the employers that harness their collective labor in pursuit of a common economic enterprise. By looking to the literature on the theory of the firm, we can better understand the importance of “employment” as an economic and legal concept, and we can better define that role to meet the definitional needs of various doctrines. At this point in our history, it makes sense to consider an employee to be one who participates in joint production within the context of a firm, rather than one who is controlled by an employer. Such a conception of employment as participation will enable us to better understand the reasons why we have a common conception of employment that ribbons throughout our law. Because employees participate within a firm, they are responsible to the firm, and the firm is responsible both to and for them.

We currently are a nation largely of employees. But that could change. In the end, it will be our approach to the concept of firms that will dictate whether the employment relationship—as defined in law—is a historical anachronism or a basis for continued common production. By better understanding the nature of employment and better framing it as a legal concept, we can understand its strengths and limitations as a legal tool and employ that tool properly in the future.

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