Insight

Economic Costs of the PRO Act: Update

ISABELLA HINDLEY | MARCH 7, 2023

Executive Summary

- A bipartisan group of House and Senate members has reintroduced the Protecting the Right to Organize (PRO) Act (H.R. 20), which seeks to strengthen labor unions and increase their leverage in collective bargaining negotiations by reclassifying independent contractors, broadening the joint employer standard, repealing right-to-work laws, and eliminating employers' ability to replace striking workers.
- While the intent of the bill is to increase worker protections, many of the provisions ignore stated worker preferences and have the potential to harm the labor market through increased costs that small businesses, franchisees, and entrepreneurs likely cannot afford.
- This paper updates previous American Action Forum research assessing the macroeconomic costs of the PRO Act and estimates that the bill could increase employment costs by anywhere from $18 – $61 billion and put up to $2.3 trillion of gross domestic product at risk.

Introduction

A bipartisan group of House and Senate members recently reintroduced the Protecting the Right to Organize (PRO) Act (H.R. 20). The bill is intended to be "pro-worker" legislation, as it seeks to strengthen labor unions and increase their collective bargaining power. Many of the provisions in the bill, however, do not align with the majority of workers' stated preferences and have the potential to harm employers, freelancers, and consumers across a wide array of industries. Among other things, the provisions of the PRO Act would narrow the classification criteria for independent contractors (ICs), expand the number of businesses subject to joint-employer liability, repeal all right-to-work laws, and restrict employers from replacing strikers.

The PRO Act would have dramatic implications for the labor market and the U.S. economy. The legislation would impose significant costs on employers, particularly small business owners such as franchisees and entrepreneurs, who would be subject to higher costs that they would likely be unable to absorb. Higher employer costs would result in higher prices for consumers and lost growth opportunities for businesses and their workers. This research provides an update to previous American Action Forum (AAF) research and estimates that the PRO Act could increase employment costs by approximately $18–$61 billion and put up to $2.3 trillion in gross domestic product (GDP) at risk.

Provisions

This research focuses on those provisions of the PRO Act with the greatest economic impact. The following provisions are likely to produce the greatest economic costs. The combined impact of the PRO Act's provisions would put approximately $2.3 trillion of GDP at risk: $2.2 trillion from the bill's IC reclassification provisions, $20–$38.7 billion from broadening the joint employer standard, and $16.1 billion from eliminating employers' ability to replace striking workers.

Reclassification of Workers

The PRO Act would narrow the definition of ICs in the National Labor Relations Act (NLRA) for the purposes of classification with the intent of reclassifying most independent contractors as employees. Yet reclassification is generally against the wishes of many independent contractors, with only about 9 percent of the 73.3 million American freelancers reporting that they prefer a traditional employee status to their status as ICs. ICs cite flexibility, entrepreneurial opportunity, and autonomy in choosing work hours and location as their chief considerations for pursuing freelancing.

The PRO Act would limit workers' ability to choose freelancing by narrowing the NLRA's definition of who can qualify as an independent contractor. Reclassification would jeopardize ICs' ability to set their own schedules, prices, and gigs. The bill would do this by inserting what is typically called the "ABC test," – a rule used to determine worker classification – into the NLRA. The ABC test holds that an individual is an employee, and not an independent contractor, unless:-

> (A) The individual is free from the employer's control and direction in connection with the performance of the service, both under the contract for the performance of service and in fact;
>
> (B) The service is performed outside the usual course of the business of the employer; and
>
> (C) The individual is customarily engaged in an independently established trade, occupation, profession, or business of the same nature as that involved in the service performed.

To be considered an IC, the employer must prove that the worker meets all of these criteria. If an employer is found to have misclassified employees as ICs, they may be subject to additional costs such as tax and payroll fines, back payments to reclassified workers, and legal damages.

Imposing the ABC test would significantly disrupt the labor market through mass reclassification of workers. Workers would face a reduction in autonomy, flexibility, and in some cases wages. Businesses, many of which rely on the work of independent contractors, would likely need to adjust their business models and adapt to higher costs. This study used recent Credit Summit research and the Bureau of Labor Statistics' (BLS) September 2022 Employer Costs for Employee Compensation data to estimate the additional costs associated with worker reclassification. Assuming a conservative 15–50 percent of ICs would be reclassified as employees under the ABC test, this could produce between $18.4–$61.4 billion in additional weekly employment costs for businesses.[i] California implemented the ABC test in January 2020 through the passage of Assembly Bill 5 (AB 5) into California labor law. Previous AAF research found that a national version of AB 5 could risk up to 8.5 percent ($2.2 trillion) of U.S. GDP.

The economic impact could be more substantial if, as the California courts have asserted, the ABC test were interpreted to apply to franchise relationships as well. Previous AAF research estimated that franchisors across the country would likely face an additional $4.9 million per hour in employment costs due to worker reclassification under the Biden Administration's proposed independent contractor rule, which would narrow the classification criteria for independent contractors in a way similar to the PRO Act. Thus, implementation of the ABC rule under the PRO Act would likely result in similar costs. Under the PRO Act, franchisees would likely not meet the criteria of the ABC test, potentially replacing the franchise model entirely with one of traditional employment. Such an arrangement would require the franchisor to assume joint responsibility for employment decisions, collective bargaining negotiations, and unfair labor practice claims, which would disincentivize the franchise model.

Broadening the Joint Employer Standard

The PRO Act would significantly alter the joint-employer standard under the NLRA. "Joint employment" describes a situation in which two or more distinct entities share responsibility in the terms and conditions of employment including hiring, disciplinary action, and supervision of employees. When labeled as a joint employer, an entity may be responsible for participating in union negotiations and responding to unfair labor practice claims on behalf of the other employers. It may also be subject to accretion, the addition of employees to existing bargaining unions without an election, and a greater likelihood that employee complaints be lawfully upheld. Under a broad joint employer standard, such as that in the PRO Act, a company is considered a joint employer if it has indirect or potential control over a group of employees. This vague definition of the standard would make it easier for companies to be labeled as joint employers. (See additional information on the joint employer standard here.)

Franchises would be hit especially hard by a broader joint employer standard. Under the model, the franchisor provides support for franchisees through brand recognition and corporate procedures. Under the PRO Act, it is likely that the support given by franchisors could be enough for the NLRB to classify them as joint employers. The prospect of reclassification would make these companies less likely to provide the brand support they can offer under a narrow joint employer definition or to disengage from the franchise model. (See additional information on the impacts of the joint employer standard on franchises here.)

Research in 2018 found that the broadened joint employer standard would lead to an estimated lost potential output for franchisees of 2.55–4.93 percent. If the recently introduced PRO Act were to pass, the annual loss of economic output for franchises would range between $20–$38.7 billion.

Repealing Right-to-work

The PRO Act would repeal right-to-work (RTW) laws, which protect workers' right to refrain from joining a union as a condition of employment, across the country. If employment offers were to become contingent on union membership, many workers could be required to pay union fees, lose employment opportunities, or risk job loss.

A 2021 Harvard University Study found that those who live in RTW states have 1.6 percentage points higher employment and 1.4 percentage points higher labor force participation than those who live in non-RTW states.

Replacing Striking Workers

Under the NLRA, unions and employers are allowed to use economic tools, such as strikes and lockouts, respectively, to settle disagreements. The law limits reliance on these tools, however, to reduce the economic harm these tools produce. Under the PRO Act, employers would be stripped of their ability to replace striking workers, regardless of the circumstances. This would tip the bargaining power balance in favor of unions, leaving employers with little option but to accept union demands or operate without staff. Under these provisions, strikes would likely become more common, consumer prices would increase, and businesses with little resource capacity would be unable to operate.

According to BLS, there were 23 major strikes and lockouts in 2022. These work stoppages involved 120,600 workers. Assuming these workers usually operated at peak productivity, the loss in productive output alone was approximately $16.1 billion for the year. That said, BLS considers a major strike to include at least 1,000 workers and to last at least one shift during the work week. Therefore, the estimate is likely a conservative one as it does not account for strikes that involved fewer workers.

Broad Impacts

The PRO Act is, among other things, designed to improve union leverage in collective bargaining negotiations. This will likely increase union density which itself has negative economic consequences. Previous AAF research found statistically significant evidence that an increase of 1 percentage point in union membership rates correlates with a reduction of 0.25 percentage points in a state's real GDP growth rate. The study also reported that declines in union density in a state led to more jobs and increased weekly earnings.

Conclusion

The PRO Act's provisions to increase union membership would be detrimental to the economy. Businesses would face higher costs and increased union activity, consumers would see higher prices, and GDP growth would suffer. The most harmful provisions could increase employment costs by anywhere from $18–$61 billion and put up to $2.3 trillion of GDP at risk. Lawmakers should consider the negative impacts of the PRO Act before approving such a drastic change to U.S. labor law.

[i] The reclassification estimate is the same as that used in previous AAF research.