Research

The NLRB's New Joint Employer Standard, Unions, and the Franchise Business Model

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EXECUTIVE SUMMARY

In this paper, we examine the implications of the National Labor Relations Board's (NLRB) new joint employer standard for unions membership and franchise employment. In August 2015, the NLRB made headlines when in an effort to empower collective bargaining it fundamentally altered the legal definition of "joint employer" so that it applies to a broader array of business arrangements. The NLRB asserted that the previous joint employer standard, established in 1984, eroded collective bargaining and that the broader standard would help reverse the long-term decline in private sector union membership. The last several decades of union trends, however, indicate that the previous joint employer standard was unrelated to union membership, suggesting the new standard is unlikely to achieve the NLRB's goal of increasing union membership. In particular,

- The long-term decline in private sector union membership pre-dates the previous joint employer standard; and
- The decline in the private sector union membership rate was quicker before the NLRB established the previous joint employer standard (0.7 percentage points annually) than after (0.3 points).

Meanwhile, the new standard could completely upend the franchise business model, one of most dependable sources of job creation in the United States. Since 2012,

- In the private sector, franchise employment has increased by 3.4 percent and non-franchise employment has only risen by 2 percent annually; and
- Employment in the leisure and hospitality industry has increased by 3.5 percent in franchise businesses and only 2.8 percent in non-franchise businesses.

The new joint employer standard is a radical change for franchising and may slow job growth in franchise companies. We project that the slowdown could result in,

- 1.7 million fewer jobs in the entire private sector; and
- 500,000 fewer jobs in the leisure and hospitality industry.

While the new joint employer standard appears unlikely to achieve the NLRB's goals of strengthening collective bargaining, it poses a major risk to franchise businesses and the US labor market.

INTRODUCTION

In recent years, the legal definition of “joint employer” has been among the most contentious labor policy issues in the United States. When a firm is considered a joint employer, the federal government holds it responsible for the labor practices of a separate independent business. In August 2015, the National Labor Relations Board (NLRB) broadened the definition of joint employer and reversed decades old precedent. This change is particularly significant for the franchise business model, as a franchisor is now more likely to be held jointly accountable for employment and pay in independent franchisees.

With the backdrop of a decades long decline in union membership, the NLRB made this change to empower collective bargaining. Advocates for the change believe that the previous standard, set in 1984, and the ensuing growth in franchises was a factor that led to the long-term decline in union membership. This viewpoint, however, ignores two key facts about the U.S. labor market. First, the decline in union membership pre-dates the previous joint employer standard, and union membership fell more rapidly before the 1984 NLRB decision than after. Second, the franchise business model is one the most significant sources of job creation in the United States. Any efforts to undermine the model and threaten its growth could end up costing millions of jobs. These two facts suggest that the new joint employer standard not only is unlikely to achieve its intended goals, but also poses a major risk to the US labor market.

THE HISTORY OF “JOINT EMPLOYER” AND WHAT IT MEANS FOR FRANCHISES

The legal definition of joint employer comes down to how a firm impacts the employees of a separate business. In 1984, the NLRB ruled in two cases, *TLI, Inc.* and *Laerco Transportation*, that a firm is a joint employer only if it exercised direct control of the employees in another business. For example, hiring, firing, and supervision constituted direct control. These decisions overturned the previous standard, which held a firm as a joint employer if it had had any direct or *indirect* control of another business’s workers.[1]

The NLRB’s August 2015 ruling on *Browning-Ferris Industries (BFI)*,[2] however, reversed the 1984 decisions and broadened the joint employer standard by returning it to its pre-1984 definition. BFI, a waste management company, contracted with Leadpoint Business Services, a staffing firm, to provide temporary employees to a California recycling facility. In 2013, Leadpoint workers at the BFI facility sought to collectively bargain with BFI, asserting that BFI and Leadpoint are joint employers. In its August 2015 decision, the NLRB broadened the standard of joint employer when it ruled that BFI is a joint employer for collective bargaining purposes.[3] In its decision, the NLRB asserted that a firm could be considered a joint employer if it directly or indirectly impacts the employment or pay of another business’s workers, effectively returning to the pre-1984 standard.[4]

Although it has been roughly a year and a half since the NLRB broadened the definition of joint employer, the new standard still faces major hurdles. In particular, the United States Appeals Court is reviewing the legality of the NLRB's *BFI* ruling. The new joint employer standard appears to be on shaky legal ground, as Judge Patricia Millett noted that the NLRB "dropped the ball" in its legal analysis.[5] Meanwhile, under the Trump Administration, the NLRB will soon be run by a conservative majority and the board will be able to revisit the *BFI* ruling, potentially reversing it. The extent to which they are able to alter the *BFI* ruling, however, depends on the outcome of the current Appeals Court case. A conservative-majority NLRB would be able to overturn *BFI* if the Appeals Court rules against the NLRB or says the new standard is permissible. On the other hand, if the Appeals Court rules that the new joint employer standard is the correct one, then a conservative NLRB will be less able to change it. Outside the Courts, Congress can also pass a new law returning the definition of joint employer to the 1984 standard.[6]

If the Appeals Court upholds the NLRB decision and Congress fails to repeal it, the outcome would have widespread ramifications. The *BFI* ruling greatly expands the joint employer standard, as the vague nature of "indirect" control means that the NLRB can begin holding firms as joint employers for any number of business relationships. As is clear in the *BFI* case, under the new standard a firm that hires contractors or staffing firms are now much more likely to be considered jointly liable for the labor conditions of workers in those firms. But of all the business relationships subject to the new joint-employer standard, none appear to be more targeted than the franchisor-franchisee relationship. In the franchise business model, a franchisor neither pays franchisee worker wages and salaries nor does it direct a franchisee how to compensate its employees. Rather all influence exerted by the franchisor is to impose quality standards and ensure uniformity in goods, services, and operations, all of which is required by the Lanham Trademark Act of 1946.[7]

Under the new joint employer standard, however, the NLRB's General Counsel issued complaints against McDonald's USA for labor violations in independent franchisees, asserting that they are joint employers. The NLRB's application of the joint employer label on the franchise business model is a major shift from all previous standards.[8] Indeed, the NLRB General Counsel's claim that McDonald's is a joint employer directly contradicts the vast majority of judicial decisions over the last five decades that found franchisors and franchisees are not joint employers.[9] Even before 1984, the NLRB itself had long established that franchisors are not joint employers because all interactions with franchisees are aimed to preserve the franchise brand, not order franchisees how to manage their workers.[10]

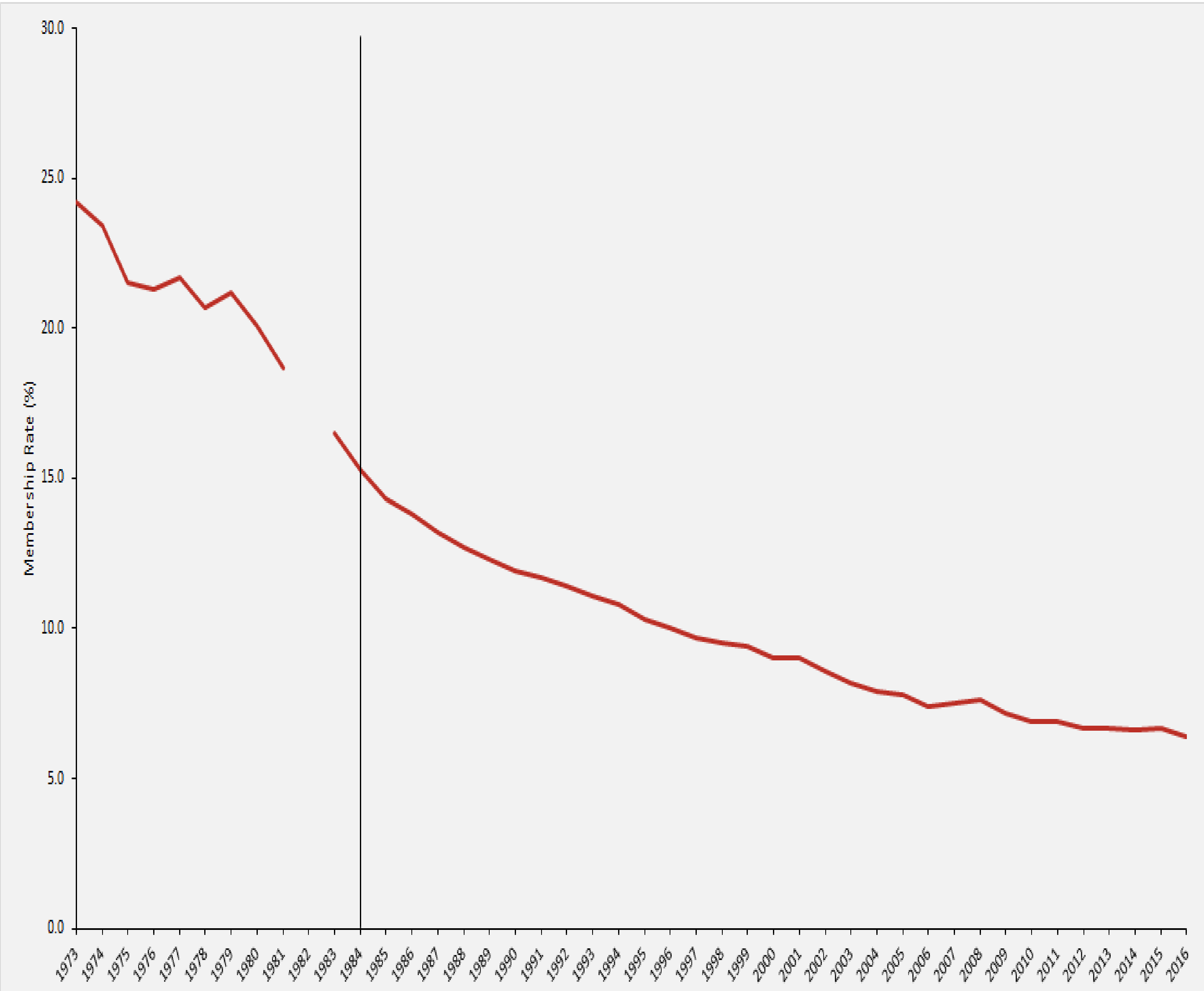
With the NLRB believing that the previous standard weakened collective bargaining and the Board's focus on franchises, these events raise two important policy questions. First, how much does the definition of joint employer impact collective bargaining? And second, by holding franchises as joint-employers, the NLRB essentially eliminates a key element that makes franchising unique and profitable. What could the new joint employer standard mean for employment in franchises?

UNION MEMBERSHIP AND THE JOINT EMPLOYER STANDARD

The NLRB is straight forward about why it believes the broadened joint employer standard is necessary. The NLRB's General Counsel put it bluntly: the 1984 joint-employer standard "inhibits meaningful collective bargaining."[11] In other words, the NRLB believes that the previous standard established in 1984 weakened collective bargaining, implying that it is a reason that the US labor market has featured a long-term decline in union membership. By reversing the 1984 decisions, the NLRB hopes that the broadened standard will empower collective bargaining in franchises and lead to a higher rate of union membership.

But, does changing the joint employer standard have any effect on union membership in the first place? Examining how union membership related to the NLRB's standard set in 1984 suggests the answer is no. Using the Current Population Survey, economists Barry Hirsch and David Macpherson have estimated the private sector union membership rate from 1973 to 2016,[12], [13] illustrated in Chart 1.

Chart 1: Private Sector Union Membership Rate



Clearly, there has been a long-term decline in private sector union membership. That decline, however, predates the 1984 joint employer standard, as the percent of workers who are union members has been falling at least since the early 1970s. In 1973, the first year for which we have data, 24.2 percent of private sector workers were union members. Fast forward to 2016 and only 6.4 percent private sector workers were union members. This suggests that the decline in union membership is mainly driven by forces unrelated to the joint employer standard.

Moreover, if the previous joint employer standard did impact union membership by preventing "meaningful collective bargaining," one would expect the long-term decline to have accelerated after the NLRB's 1984 rulings. In reality, however, the exact opposite happened: after the NLRB established the previous joint employer standard in 1984, union membership began declining at a slower rate.

Table 1 contains the average annual percentage point change in the private sector union membership rate and the annualized percent change in the number of union members before and after the NLRB introduced the previous joint employer standard in 1984.

Table 1: Change in Private Sector Union Membership Before and After 1984

Year	Membership Rate	Members
1973-1984	-0.7 pt	-2.2%
1985-2016	-0.3 pt	-1.4%

From 1973 to 1984, the union membership rate declined an average 0.7 percentage points each year. After the NLRB established the previous joint employer standard, the average annual decline dropped to only 0.3 percentage points per year. In addition, the number of private sector workers belonging to unions fell by 2.2 percent annually before the previous joint employer standard. From 1985 to 2016, the rate of decline in the number of union members decreased to 1.4 percent per year.

In recent years, the private sector union membership rate had been relatively stable and then began to decline again in 2016, the year after the NLRB adopted the new joint employer standard. From 2012 to 2015, the membership rate bounced between 6.6 percent and 6.7 percent. After the NLRB ruled on *BFI* at the end of 2015, however, the private sector union membership dropped to 6.4 percent in 2016.

So, there is no obvious evidence that changing the joint employer standard makes any impact on union membership or that the previous standard facilitated the decline union membership in the first place. Consequently, it is very likely that the new standard will not empower unions to gain more members, failing to achieve the NLRB's principle goal.

HOW THE NEW JOINT EMPLOYER STANDARD IMPACTS FRANCHISES

As previously mentioned, the new joint employer standard is being used to directly target franchises. Franchises have been among the most dependable sources of job creation in the United States. The new joint employer standard, however, could upend the franchise model and poses a major risk to the US labor market.

Franchise Job Growth

Franchises are networks of small business establishments that operate under the same brand to sell goods and services in a uniform way. Under the franchise model, a franchisor develops a product and a brand. While the franchisor generally establishes a few company-owned locations, most establishments are franchisees, independent businesses that pay the franchisor a fee to utilize its brand and sell its goods and services. After paying the fee, the franchisee bares all responsibilities and costs of doing business, including labor, as it keeps any profits for itself and absorbs any losses on its own. As a result, a franchisee hires, fires, and pays workers all on its own.[14]

Franchises make it easy for individuals to become small business owners, leading to rapid job growth. The franchisor develops the product or service and the brand, saving franchisees substantial startup costs. Moreover, as a franchisee, a small business operates under a brand that has regional, national, or even global recognition and a loyal customer base.[15] With clear advantages to franchising, franchised businesses have grown rapidly and have become major sources of job creation.

According to the payroll processing firm ADP, in 2016 franchises employed roughly 8.4 million workers, 6.9 percent of private sector employees in the United States. 5.1 million (61 percent) of those workers were in the leisure and hospitality industry. Using ADP's historical private sector[16] and franchise data,[17] we examine the growth in franchise and non-franchise firms since 2012, the first full year of franchise employment data available. Table 2 compares franchise to non-franchise employment growth in the entire private sector and in leisure and hospitality.

Table 2: Franchise vs. Non-Franchise Employment Growth Rates, 2012 to 2016

Biz Model	All Industries	L & H
Franchise	3.4%	3.5%
Non-Franchise	2.0%	2.8%
Difference	1.4 pt	0.7 pt

Since 2012, employment in franchises has grown 3.4 percent annually, 1.4 percentage points faster than the 2 percent growth rate in non-franchise businesses. In leisure and hospitality, franchise jobs grew at a similar rate of 3.5 percent, 0.7 percentage points quicker than the non-franchise job growth rate of 2.8 percent.

With franchise jobs growing more rapidly than non-franchise jobs, the business model has been punching well above its weight. Table 3 shows that since 2012, the portion of new jobs in the private sector created by franchises is disproportionately large.

Table 3: Portion of Workers in and Jobs Created by Franchises

Jobs	All Industries	L & H
All Jobs	6.9%	33.0%

Jobs Added Since 2012	10.9%	37.6%

In both the entire private sector and in the leisure and hospitality industry, franchises have been outperforming other businesses. While franchises employed 6.9 percent of private industry workers in 2016, since 2012 they have created 10.9 percent of new private sector jobs. In the leisure and hospitality industry, 33 percent of workers were employed by franchises in 2016. But, since 2012, franchises created 37.6 percent of new jobs in the industry. Franchises have indeed been a bright spot in the United States' anemic economic recovery from the Great Recession.

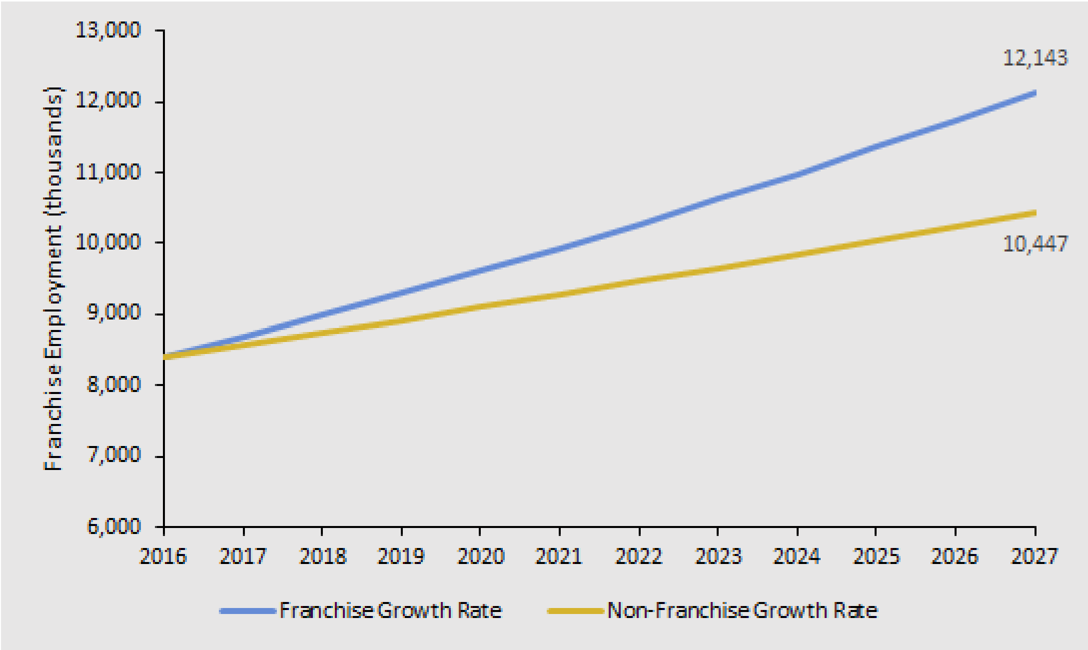
The Risk Franchises and the US Labor Market Face Under the New Joint Employer Standard

The NLRB's new joint employer standard could effectively change franchising as we know it. Under the new standard, franchisors may become responsible for the employment and pay of workers in each independent business unit. As a result, the franchisors would likely take a much more active role in day-to-day operations and bear much of the labor costs. When facing these costs, companies would likely cease franchising and may even seek to end current franchise agreements, opting instead to build a network of company-owned establishments.[18] With fewer individuals opening small businesses at low startup costs, franchises would lose what has made them such a successful source of job creation in the United States.

Lacking the dynamic that makes franchising unique and profitable, it is likely that franchises would begin to act more like regular businesses. One potential outcome of this is that franchise jobs would begin to grow at the same rate as jobs in non-franchise businesses, greatly slowing private sector job creation. To gauge the magnitude of the slowdown in job growth, we project future franchise employment levels under two scenarios. In the first scenario, we assume that the current franchise annual job growth rate (3.4 percent in the private sector and 3.5 percent in leisure and hospitality) continues over the next ten years. In the second scenario, we assume that over the next ten years the annual franchise job growth rate drops to the non-franchise employment growth rate (2 percent in the private sector and 2.8 percent in leisure and hospitality).

Chart 2 contains private sector franchise employment projections under each scenario.

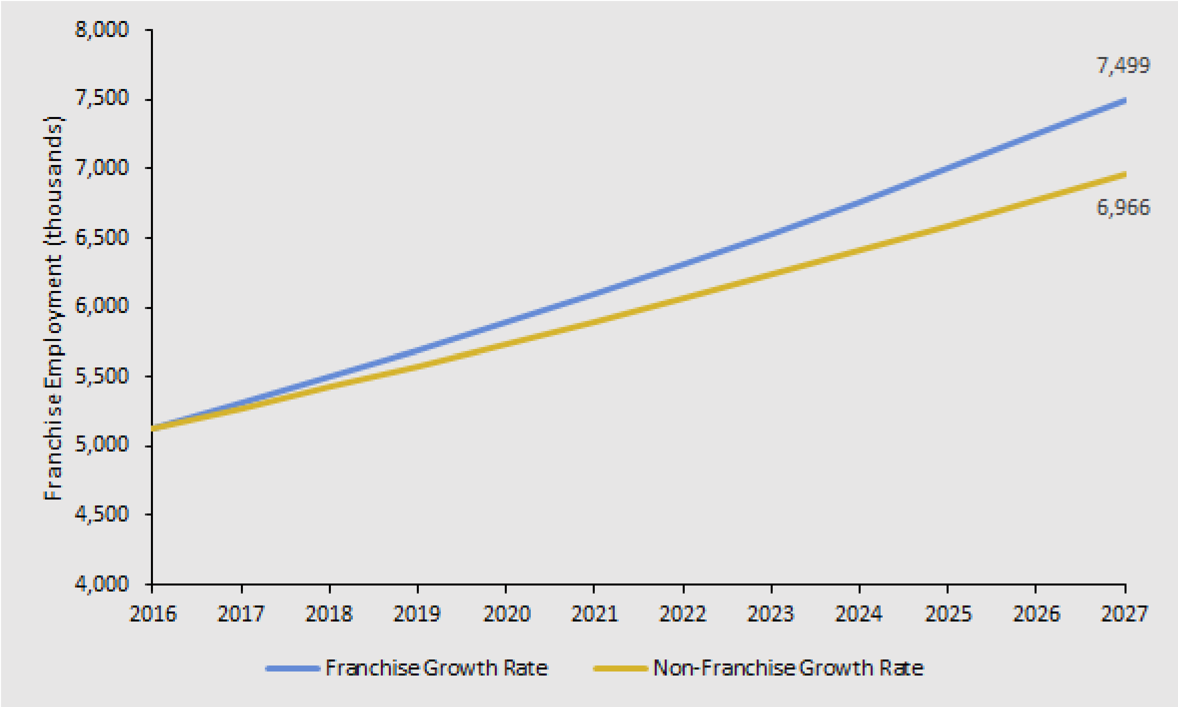
Chart 2: Private Sector Franchise Employment Growth Projections



If franchise job growth in the private sector were to continue at its current 3.4 percent rate, then franchise employment will increase to 12.1 million jobs by 2027. If franchise job growth, however, dropped to the 2 percent annual rate experienced in the rest of the private sector, then in 2027 franchise employment will only increase to 10.4 million jobs. This translates to a loss of 1.7 million jobs.

As illustrated in Chart 3, employment in leisure and hospitality franchises would also suffer from slower growth.

Chart 3: Leisure and Hospitality Franchise Employment Growth Projections



At the current franchise job growth rate of 3.5 percent in leisure and hospitality, employment in the industry will increase to 7.5 million jobs by 2027. Yet, under the slower 2.8 percent non-franchise job growth rate, leisure and hospitality employment will only increase to 7 million jobs, translating to a loss of 500,000 jobs.

It is still unclear how franchise businesses will react to the NLRB's new joint employer standard, but, these projections illustrate the magnitude of the risk that the new standard imposes on the labor market.

CONCLUSION

While there is no indication that the new joint employer standard will achieve the NLRB's collective bargaining objectives, it could upend a successful business model and over a million of jobs. There is no evidence that the previous joint employer standard established in 1984 weakened collective bargaining. In particular, union membership declined quicker before the 1984 standard took effect than it did after the standard was in place. This suggests that the NLRB's new standard will provide little, if any, help in efforts to increase collective bargaining. Meanwhile, no businesses appear to be more targeted by the NLRB than franchises. Yet, efforts to label franchisors as joint employers with franchisees would completely undermine the very aspect of franchising that has allowed it to create millions of jobs in the United States. Consequently, the new standard could cost up to 1.7 million jobs in the private sector and 500,000 jobs in leisure and hospitality. With weak legal and economic justifications, the NLRB's new joint employer standard is a misguided policy that now poses a major risk to the US labor market.

[1] Daniel B. Pasternak & Naomi Y. Perera, "The NLRB's Evolving Joint-Employer Standard: Browning-Ferris Industries of California, Inc.," ABA Journal of Labor and Employment Law, 295, 2016, pgs. 296-297, http://www.americanbar.org/content/dam/aba/publishing/aba_journal_labor_employment_law/v31n2/abajlel31-2_04pasternak.authcheckdam.pdf

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[3] Daniel B. Pasternak & Naomi Y. Perera, "The NLRB's Evolving Joint-Employer Standard: Browning-Ferris Industries of California, Inc.," ABA Journal of Labor and Employment Law, 295, 2016, pgs. 297-302, http://www.americanbar.org/content/dam/aba/publishing/aba_journal_labor_employment_law/v31n2/abajlel31-2_04pasternak.authcheckdam.pdf

[4] "Browning-Ferris Industries of California, Inc., d/b/a BFI Newby Island Recyclery, and FPR-II, LLC, d/b/a Leadpoint Business Services, and Sanitary Truck Drivers and Helpers Local 350, International Brotherhood of Teamsters, Petitioner," National Labor Relations Board, Decision, Case 32-RC-109684, 2015, pg. 2, https://www.nlrb.gov/case/32-RC-109684

[5] Robert Iafolla, "U.S. Appeals court grapples with labor board 'joint employment' test," Reuters, March 9, 2017, http://www.reuters.com/article/us-usa-employment-republic-servs-idUSKBN16G2WQ

[6] Chris Opfer, "New Joint Employer Liability Test Tough to Undo, NLRB Counsel Says," Bloomberg BNA, March 29, 2017, https://www.bna.com/new-joint-employer-n57982085895/

[7] David J. Kaufman, Felicia N. Soler, Breton H. Permesly, and Dale A. Cohen, "A Franchisor is Not the

Employer of Its Franchisees or Their Employees," Franchise Law Journal, Vol. 34, No. 4, Spring 2015, pgs. 455-456, http://www.americanbar.org/content/dam/aba/publications/franchising_law_journal/Spring_2015/FLJ%2034-4_01Kaufmann.authcheckdam.pdf

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[9] David J. Kaufman, Felicia N. Soler, Breton H. Permesly, and Dale A. Cohen, "A Franchisor is Not the Employer of Its Franchisees or Their Employees," Franchise Law Journal, Vol. 34, No. 4, Spring 2015, pg. 473, http://www.americanbar.org/content/dam/aba/publications/franchising_law_journal/Spring_2015/FLJ%2034-4_01Kaufmann.authcheckdam.pdf

[10] Meghan B. Phillips, "Amicus Brief of the General Counsel," Case 32-RC-109684, National Labor Relations Board, pgs. 15-16, https://www.nlrb.gov/case/32-RC-109684

[11] Ibid., pg. 11

[12] "Union Membership, Coverage, Density, and Employment Among Private Sector Workers, 1973-2016," Union Membership and Coverage Database from the CPS, http://www.unionstats.com/

[13] For information on database methodology see: Barry T. Hirsch & David A. Macpherson, "Union Membership and Coverage Database from the Current Population Survey: Note," Industrial and Labor Relations Review, Vol. 56, No. 2, January 2003, http://www.unionstats.com/

[14] David J. Kaufman, Felicia N. Soler, Breton H. Permesly, and Dale A. Cohen, "A Franchisor is Not the Employer of Its Franchisees or Their Employees," Franchise Law Journal, Vol. 34, No. 4, Spring 2015, pg. 453-455, http://www.americanbar.org/content/dam/aba/publications/franchising_law_journal/Spring_2015/FLJ%2034-4_01Kaufmann.authcheckdam.pdf

[15] Ibid.

[16] "ADP National Employment Report: March 2017," Historical Data, https://www.adpemploymentreport.com/2017/March/NER/NER-March-2017.aspx

[17] "ADP National Franchise Report: March 2017," Historical Data, https://www.adpemploymentreport.com/2017/March/NFR/NFR-March-2017.aspx

[18] David J. Kaufman, Felicia N. Soler, Breton H. Permesly, and Dale A. Cohen, "A Franchisor is Not the Employer of Its Franchisees or Their Employees," Franchise Law Journal, Vol. 34, No. 4, Spring 2015, pg. 441, http://www.americanbar.org/content/dam/aba/publications/franchising_law_journal/Spring_2015/FLJ%2034-4_01Kaufmann.authcheckdam.pdf