LABOUR LAW AND TRIANGULAR EMPLOYMENT GROWTH

Timothy J. Bartkiw

Associate Professor
Ryerson University, Toronto, ON, Canada

Labour Law and Triangular Employment Growth

Timothy J. Bartkiw, Associate Professor
Ryerson University, Toronto, ON, Canada
tbartkiw@ryerson.ca

Paper for presentation at the inaugural Labour Law Research Network Conference,

Pompeu Fabra University, Barcelona, Spain, June 13-15, 2013.

I. Introduction

By various accounts, "triangular employment," in which "employees find themselves interacting with two (or more) interlocutors, each of whom assumes certain functions of a traditional employer,"[1] has grown in many countries in recent decades.[2] Triangular employment growth has in many cases coincided with a general neoliberal[3] trend in labour market regulation in the past few decades, which involved a mix of deregulatory and re-regulatory[4] shifts in labour policy. In the U.S. for example, it has been argued that the growth of "temporary help services", an important variant of triangular employment, has substantially contributed to labour market deregulation, through a general undermining and deregulation of the employment relationship itself.[5]

However, triangular employment growth has been embodied not only in the expansion of so-called "temporary help", but also within certain other "services"[6] provided by the proliferating, and increasingly global, staffing industry. This growth has been quite uneven across jurisdictions.[7] By exploring the relationship between triangular employment growth and labour law, this paper contributes to our understanding of triangular employment growth, and of its globally uneven expansion.

Part II of the paper provides a brief review of the meaning of "triangular employment" and a discussion of why it is often understood in normative terms as a potential policy "problem". This is followed in Part III by a discussion of some of the competing normative theoretical claims made about triangular employment. I argue that despite claims about potential benefits arising from staffing services based on triangular employment, at a minimum there remains substantial space for the concern that triangular employment raises significant labour policy problems. Part IV outlines the theoretical concept of a "regulatory differential". These are understood as differences in regulatory effect occurring under triangular employment than under "direct" employment, from the ultimate perspective of the "user" of the worker, stimulating triangular employment growth. Further, a taxonomy of different forms these

---

[1] International Labour Conference, Report V(1): Scope of the Employment Relationship, International Labour Conference, 95th Session, 2006, p. 13.

[2] DONALD STORRIE, TEMPORARY AGENCY WORK IN THE EUROPEAN UNION (European Foundation for the Improvement of Living and Working Conditions, Luxembourg: Office for the Publications of the European Communities, 2002).; Jamie Peck and Nik Theodore, *Flexible Recession: The Temporary Staffing Industry and Mediated Work in the United States,* 31(2) CAMBRIDGE JOURNAL OF ECONOMICS 171. (2007); Jamie Peck and Nik Theodore, *Temped Out? Industry Rhetoric, Labour Regulation, and Economic Restructuring in the Temporary Staffing Business*, 23(2) ECONOMIC AND INDUSTRIAL DEMOCRACY 143 **(**May 2002); Jamie Peck, Nik Theodore and Kevin Ward, *Constructing Markets for Temporary Labour: Employment Liberalization and the Internationalization of the Staffing Industry*, GLOBAL NETWORKS 5, 1 (2005), 3-26. LEAH F. VOSKO, TEMPORARY WORK: THE GENDERED RISE OF A PRECARIOUS EMPLOYMENT RELATIONSHIP (2000); Timothy J. Bartkiw, *Baby Steps? Towards the Regulation of Temporary Help Agency Employment in Canada*, 31(1) COMPARATIVE LABOR LAW AND POLICY JOURNAL 163 (Fall 2009); and Britton Lombardi and Yukako Ono, *Professional Employer Organizations: What are they, who uses them, and why should we care?,* ECONOMIC PERSPECTIVES (4th quarter, 2008).

[3] DAVID HARVEY, A BRIEF HISTORY OF NEOLIBERALISM (2005); Greg Albo, *The 'New Economy' and Capitalism Today* in INTERROGATING THE NEW ECONOMY: RESTRUCTURING WORK IN THE 21ST CENTURY (Norene Pupo, ed., 2009).

[4] See Guy Standing, *Globalization, Labour Flexibility and Insecurity: The Era of Market Regulation*, 3(EUROPEAN JOURNAL OF INDUSTRIAL RELATIONS 7 (1997).

[5] Peck and Theodore, *Flexible Recession*, *supra* note 2.

[6] The use of the term "services" is not meant to attribute any particular degree of legitimacy to such business transactions.

[7] Peck, Theodore, and Ward, *Constructing Markets, supra* note 2; See also Storrie, *supra*, note 2.

regulatory differentials take, and the ways in which they operate, is provided. The paper then employs this concept of a regulatory differential to examine diverging patterns in triangular employment growth in Canada and the U.S. over recent decades. To this end, Part V reviews the data illustrating that triangular employment growth in the U.S. has in fact significantly outpaced developments in Canada. This analysis reveals that the greater growth of triangular employment in the U.S. may be largely explained, in an accounting sense, by both the size and growth of a certain variant of triangular employment that seemingly only exists on a large scale in the U.S., namely "professional employer" services, provided by "professional employer organizations" or "PEOs".

Part VI of the paper undertakes comparative legal analysis to assess the degree to which the theoretical framework is consistent with the observed patterns of triangular employment growth. U.S. and Canadian labour laws are examined to assess the comparable degree to which each country's labour laws (broadly defined) embody regulatory differentials capable of stimulating triangular employment growth. To this end, shifts in the law creating these differentials, and the timing of these shifts, are also assessed. Analysis is limited to two sub-fields among many: the regulation of retirement benefit plans and the regulation of employer-sponsored healthcare benefits. Overall, I argue that regulatory differentials favouring triangular employment growth are more prevalent in the U.S., and that the timing of the construction of these regulatory differentials in U.S. law is largely consistent with observed patterns in triangular employment growth, confirming potentially causal relations. Part VII provides some concluding thoughts about the findings overall and their consequences.

II. What is Triangular Employment?

In a recent report summarizing deliberations of the 95th Session of the international Labour Conference, triangular employment is summarized as comprising two main scenarios in contractual relationships: 1) contracts for the performance of work and services, and 2) contracts for the supply of labour services.[8] In scenario 1, a so-called "provider" organization[9] contracts with a "third party" organization, referred to as the "user", to produce and supply some form of work or service.[10] The "provider" then uses its own equipment and/or personnel to supply this work or service to the user, for use within the user's production process. In scenario 2, the "supply of labour services" scenario, the commodity supplied under contract by the "provider" is ostensibly "labour" itself – work performed by personnel "employed" by the provider. Here, the classical distinction between "labour" and "labour power" is informative. It should be recognized that in an employment contract, the hiring organization is actually hiring "labour power", as opposed to "labour", and this labour power must then be *managed* within a "labour process", towards the production of some commodity. Thus, in scenario 1, the provider firm manages the worker in its own labour process, and subsequently provides a commodity to the user firm.

---

[8] Report V(1), *supra*, note 1, p. 42.

[9] Throughout this paper, the words "organization", and "firm" are used interchangeably and ought to be understood broadly to include both public and private sector organizations.

[10] Consistent with ILO terminology, this paper uses the terms "user" and "provider" to identify the 2 organizational parties within a triangular employment relationship. See *Report V(1),* Supra, note 1, page 42. However, the phrase "third party" is not employed in a similar fashion, since it may be taken as implying a particular normative view of these relationships. See Jan Theron, *Intermediary or Employer? Labour Brokers and the Triangular Employment Relationship*, 26 INDUS. L.J. JUTA 618 (2005). Theron argues that it is inappropriate for the ILO to refer to the client user as a "3rd party" in its terminology, given that the user is the actual and underlying source of demand for the labour without which there would be no employment of the worker at all. Referring to the user as a 3rd party in relation to the provider and worker risks attributing an inappropriate degree of normalcy and/or legitimacy to the contested view of the provider as the "employer".

In scenario 2, the ultimate utilization of labour power occurs only within the user firm's labour process. Despite this intuition, distinguishing between these different types of contractual relationships may at times be difficult, given the nature of "services" ostensibly provided.

As noted, these two scenarios encompass a broad category of commercial relations. In fact, some further crucial details are also relevant in establishing a definition of triangular employment. As stated in the ILO Report V on the Scope of the Employment Relationship:

> "…such contracts may present a technical difficulty as the employees concerned may find themselves interacting with two (or more) interlocutors, each of whom assumes certain functions of a traditional employer. The term 'triangular' employment relationship is used in this report to describe employment situations of this kind".[11]

This close interaction between the worker and more than one interlocutor assuming functions of a traditional "employer" may arise under *both* scenarios 1 and 2 (Ie. both the service and labour supply scenarios), although with arguably greater likelihood under scenario 2. In scenario 2, the user is ostensibly only a party to a commercial contracting arrangement with the provider, and not to any formal "employment" relationship with the worker. The provider is the ostensible employer of the worker. Thus, for the user, the arrangement serves to some extent as a *substitute* for directly "employing" its own workers. Despite the importance of recent trends in related "subcontracting" arrangements, this paper is focused on expansion in those triangular relations found in scenario 2, of a "labour supply" nature. Specifically, the paper focuses on growth in related services supplied by the expanding "staffing services" industry. Over the past few decades, this industry has provided an increasingly diverse bundle of services referred to alternatively as "staffing", "personnel", "employment", "human resources", or "human capital" services.[12]

According to the ILO, these various triangular relationships raise policy concern insofar as they represent either "disguised employment" or "objectively ambiguous employment". A disguised employment relationship is:

> "one which is lent an appearance that is different from the underlying reality, with the intention of nullifying or attenuating the protection afforded by the law. It is thus an attempt to conceal or distort the employment relationship, either by cloaking it in another legal guise or by giving it another form in which the worker enjoys less protection."[13]

Parties may "disguise" employment relations by masking the identity of the "true" or *de jure* employer; by giving the relationship the appearance of a different legal nature (eg. civil, commercial contract, etc.);

---

[11] Report V(1): Scope of the Employment Relationship, International Labour Conference, 95th Session, 2006, p. 13.

[12] The American Staffing Association website contains a list of staffing service categories for prospective organizational members to use to self-identify the kinds of services focused upon by their organization. These include the following categories: direct placement services; human resources consulting; long term and contract help; managed service provider; managed services; outplacement; payrolling; professional employer organization or employee leasing; recruitment process outsourcing; retained search services; temporary help; temporary to hire; vendor management systems. See https://americanstaffing.net/commerce/memberJoin.cfm.

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

or by attempting to alter the "form" of employment (eg. repeated usage of formally short term contracts in an otherwise long term "employment" relationship".)[14]

Alternatively, in the case of "objectively ambiguous employment", there may actually be no intention to alter the appearance of the underlying relationship. However, the specifics of the relationship are such that it raises serious questions about the proper allocation of *de jure* employer status and ensuing rights and responsibilities.

In both of these situations involving potentially disguised employment, the determination and allocation of *de jure* employer status is a function typically reserved to relevant local authorities of various sorts, empowered to determine the existence of employment relationships as a part of the regulatory function they perform. Adjudicative determinations are made in accordance with the meaning and content of the concept of "employer" (and/or "employee", "employment" etc.) institutionalized within the given jurisdiction, either through statute or case law. Here the ILO advocates adherence to the principle of the "primacy of fact", meaning simply that the true factual nature of the relationship, and not the description or labels assigned to it by the parties themselves, be determinative. Practices in the allocation of employer status as between user and provider vary, along with different regulatory models, across jurisdictions.[15]

Triangular employment is generally not a *de jure* category *per se*. Rather, it is a peculiar employment arrangement involving a provider and user, where *one* of the provider or user purports *not* to be the (or a)[16] *de jure* employer of the worker, but the factual situation objectively raises a question as to *de jure* employer status. Importantly, in triangular employment the parties acknowledge that there *is* a *de jure* "employment" relationship in place, along at least one[17] of the sides of the triangle.

Growth of the global "staffing" industry has generated triangular employment growth insofar as some of its services either depend upon the creation of triangular employment relations explicitly, or may create triangular employment as a by-product. A common model that has attracted much academic attention has been temporary help services, where the provider ostensibly employs a worker and then assigns the worker to a client user, to work for (purportedly) temporary work assignments, commonly under the direction and control of the user. Gonos argues that underpinning the "temporary help formula" and the massive growth in these arrangements in the U.S., was the gradual recognition of the provider as the *de jure* employer of the worker in these triangular arrangements in the 1960's and 70's.[18]

The various service bundles provided by the staffing industry may be differentiated in two main ways. First, there are *qualitatively* different staffing functions provided in different situations. For example, in North America, while employee "screening" and "recruitment" functions are generally included as part

---

[14] Ibid, pp. 24-26.

[15] Storrie, Supra, note 2; Guy Davidov, *Joint Employer Status in Triangular Employment Relationships*, 42 BRITISH JOURNAL OF INDUSTRIAL RELATIONS 727 (2004).

[16] In other words, under triangular employment, one party may purport not to be the sole employer, nor one of the multiple employers of the worker. Various alternative terms are applied to describe multiple employer contexts: joint employers, common employers, related employers, and co-employers.

[17] In more rare cases, parties could sometimes purport to be *de jure* "joint employers", or some other similar concept employed in the jurisdiction, mentioned in the preceding footnote.

[18] George Gonos, *The Contest over 'Employer' Status in the Postwar United States: The Case of Temporary Help Firms*, 31 LAW AND SOCIETY REVIEW 81 (1997). George Gonos, *The Interaction Between Market Incentives and Government Actions*, in CONTINGENT WORK: AMERICAN EMPLOYMENT RELATIONS IN TRANSITION, (K. BARKER AND K. CHRISTENSEN, EDS., 1998), pp. 170-191; and Vosko, *supra*, note 2.

of the bundle of services commonly identified as the "temporary help" service, these functions are less likely included in so-called "employee leasing" or "professional employer" services arrangments. Specific services may either supplement or displace pre-existing functions performed by the user, with the total bundle varying in intensity of substitution of functions previously or potentially performed by the user. Certainly, not all of the qualitatively different staffing services should be understood as generating triangular employment. Many such services would have little impact on the logic of *de jure* employer status, in which case parties will generally not make any such claims. For example, in the Canadian system, it is fairly well established that the mere provision of so-called "payroll services" by a staffing firm will not cause a shift in *de jure* employer status. Where there *is* a goal of affecting *de jure* employer status, a more intensive substitution in favour of staffing services is generally required, with the specific degree and character of these being highly affected by prevailing rules and tests for determining the *de jure* employer.

Secondly, there are important *temporal* distinctions embodied in different service bundles provided by the staffing industry. Although there is conflicting use of terminology, examples of staffing services embodying an important short term *temporal* component include: "day labour" (very short term), "temporary help" (short to medium term), and "temp to perm" (short to medium term). Other services such as "employee leasing",[19] or "professional employer services" are generally conceived as being non-temporary, or for an indeterminate time period.[20] Of course, in practice the label used to describe a particular staffing service bundle may be factually inaccurate, particularly with respect to temporality. For example, much attention has been drawn to the "perma-temps" phenomena, in which so-called "temporary help" arrangements are in fact not temporary.[21] Similarly, "employee leasing" has in practice been used to label arrangements more closely resembling classic temporary help services.[22] In general, firms may also hold themselves out as providers of a specific type of staffing service, while actually providing others.

This heterogeneity of staffing services may have constrained prior analysis of some of these triangular relationships to some extent.[23] In North America, official statistical categories have been adjusted over time to attempt to distinguish between the different service models produced by the industry overall.[24] However, the degree to which official categorization of service models is followed and understood in

---

[19] See the discussion in EDWARD A. LENZ, CO-EMPLOYMENT: EMPLOYER LIABILITY ISSUES IN THIRD-PARTY STAFFING ARRANGEMENTS, 7TH ED. (2011). As Lenz points out, the term "employee leasing" is sometimes used as a generic term to refer to all forms of staffing services. However, it is more often (and here) understood to refer to an intricate human resource outsourcing arrangement that purports to transfer employer status to the employee leasing firm, which in more recent years have become increasingly referred to as "professional employer organizations".

[20] See Lenz, *supra*, note 19. The fact that employee leasing services themselves are not in general based on short a term basis, needs to be understood as separate from the fact that the definition of the *de jure* concept of a "leased employee", which is used in U.S. tax law and is discussed in significant detail in Part VI below, is partly based on the duration of services provided by the worker in question. See Internal Revenue Code, s. 414(n).

[21] ERIN HATTON, THE TEMP ECONOMY: FROM KELLY GIRL TO PERMATEMPS IN POSTWAR AMERICA, 2011. Other evidence of increasing duration of assignments in so-called temporary help arrangements is also provided in Vosko, Temporary Work, *supra*, note 2. See also Matt Vidal and Leann M. Tigges, *Temporary Employment and Strategic Staffing in the Manufacturing Sector,* 48 INDUSTRIAL RELATIONS 55 (2009).

[22] Lenz, Supra note 19.

[23] For example, Lombardi and Ono, *supra*, note 2, cite a lack of prior analysis of PEO growth.

[24] Canada, the U.S. and Mexico have since at least 1997 used the North American Industrial Classification System for classifying official statistics. In certain instances, efforts have been made to "recode" some earlier data based on NAICS, to create longer time series for comparisons.

practice in industry is not clear, and likely has certain limits.[25] Nevertheless, as different service models have evolved and become more prevalent over time, certain observable patterns have emerged. An important example to which this paper will return in Part V has been the very rapid expansion in the subcategory of "professional employer" services in the U.S.A. over the past few decades, which are based on the construction of non-temporary triangular employment relations.[26] Indeed, the National Association of Professional Employer Organizations ("NAPEO"), the key industry association for PEOs, openly and explicitly embraces triangularity, as it claims the somewhat ambiguous concept of "co-employment" as being at the heart of the services provided by its member firms.[27]

"Co-employment" is a term created by the PEO industry, it is not a juridical category, and *de jure* employer status of firms providing these services would still be determined by application of legal tests and the primacy of fact. As well, the industry itself does not seemingly define "co-employment" based on a specific bundle of services. Rather, co-employment is established by contract between a PEO and a client, and the contract defines the relationship, from among a fairly large set of potential (re)allocations of various sorts of human resources related functions and responsibilities.[28] Although the use of professional employer service arrangements would not necessarily alter *de jure* employer status in every circumstance, given the continuum of employment related services provided under the various labels[29] the concern is clearly raised that a significant proportion of PEO arrangements would raise a serious question as to *de jure* employer status, in various factual and legal contexts, and thus would fall under our working definition of triangular employment.

Analytical focus emphasizing the specifically *triangular* component of the various staffing arrangements, abstracting away from temporal differences, is necessary and feasible. Some academic commentators similarly argue that insufficient attention has been paid to the triangular (as opposed to the temporal) dimension of temporary help services by policy makers.[30] The recent ILO Convention No. 181, Private

---

[25] In an interview, a president of a large Canadian staffing firm stated that there is not a strong understanding of the concept of "PEO" services in Canada, despite this being an official category used by Statistics Canada. Official statistics, reviewed in Part V of the paper, suggest that there is (at most) a very small volume of such services supplied in Canada.

[26] Lombardi and Ono, *supra*, note 2. See also Lenz, Supra, note 19.

[27] See NAPEO website description of co-employment at http://www.napeo.org/peoindustry/coemployers.cfm.

[28] In a page containing a list of typical questions and answers about PEO relationships, the website of the National Association of Professional Employer Associations in the U.S. provides the following answer to the question "How does a PEO arrangement work?": "Once a client company contracts with a PEO, the PEO will then co-employ the client's worksite employees. In the arrangement among a PEO, a worksite employee and a client company, there exists a co-employment relationship in which both the PEO and client company have an employment relationship with the worker. The PEO and client company share and allocate responsibilities and liabilities. The PEO assumes much of the responsibility and liability for the business of employment, such as risk management, human resource management, and payroll and employee tax compliance. The client company retains responsibility for and manages product development and production, business operations, marketing, sales, and service. The PEO and the client will share certain responsibilities for employment law compliance. As a co-employer, the PEO will often provide a complete human resource and benefit package for worksite employees."

[29] See for example the list of employee management services offered by the firm XCELHR listed at http://www.xcelhr.com/BundledServices/ServiceGrid.aspx.

[30] For example, Vosko argued that the province of Ontario's recently adopted "Bill 139" legislation addressing temporary help arrangements – a regulatory breakthrough to a small extent given the dearth of regulation of temporary help in Canada – focuses too much on the temporary, rather than the triangular dimension of these relations. See Leah Vosko, *A New Approach to Regulating Temporary Agency Work in Ontario or Back to the Future?,* 65(4) RELATIONS INDUSTRIELLES 632 (2010), For a review of the prior regulatory environment of temporary help in Canada, see Bartkiw, *Baby Steps*, *supra*, note 2.

Employment Agencies Convention, 1997[31] purports to aim at remedying this lack of state regulation of the triangular dimension insofar as it calls upon states to specifically clarify and assign responsibilities within these relationships.[32] Abstraction of this sort, emphasizing triangularity *per se*, underpins analysis in this paper, which now turns to reviewing normative theoretical claims about staffing services and public policy.

III. Triangular Employment and Public Policy: Normative Concerns?

The importance of the relationship between public policy and triangular employment growth is caught up with the question of the degree to which triangular employment represents a labour policy "problem". Academic literature has provided a range of explanations for growth in triangular employment, in its particular forms. While some explanations suggest a desire on the part of employers to "avoid" the effects of labour law,[33] other explanations raise the possibility of more "benign" behavior towards "legitimate" purposes.[34] This paper adopts, *inter alia*, the simple normative assumption that where either status quo labour policy or the degree of social protection is undermined by triangular employment, this is a *prima facie* problem. While it is a conceptual possibility that by some normative measure the "benefits" of triangular employment may "outweigh" the problem of labour policy being undermined, there can be no *prima facie* acceptance of this. This is because labour policy determining the degree of social protection for workers may be understood as already being the product of *competing* social concerns, including efficiency.[35] Leaving aside crucial questions about the nature of democratic policy-making, a basic necessary (albeit arguably insufficient) condition for the acceptability of any such tradeoff of "social protection" would be evidence of an explicit, informed, democratic policy choice.[36]

Potential explanations of triangular employment growth based on the pursuit of "legitimate" purposes emerge from explanations for growth in the types of related staffing services themselves. These explanations of staffing services growth based on "legitimate" purposes appear to be largely based in literature embracing the neoclassical economic paradigm,[37] and in particular, the neoclassical "theory of

---

[31] *Available at* http://www.ilo.org/ilolex/cgi-lex/convde.pl?C181.

[32] For an argument emphasizing the limits of this Convention, Leah F. Vosko, *Legitimizing the Triangular Employment Relationship: Emerging International Labour Standards from a Comparative Perspective*, 19 COMPARATIVE LABOR LAW AND POLICY JOURNAL 43 (1997).

[33] See Gonos, *The Contest over Employer Status, supra*, note 18; Peck and Theodore, Flexible Recession, Supra, note 2; David Autor, *Outsourcing at Will: Unjust Dismissal Doctrine and the Growth of Temporary Help Employment*, 23 JOURNAL OF LABOR ECONOMICS 1 (2003); Houseman, Susan, *Why Employers Use Flexible Staffing Arrangements: Evidence from an Establishment Survey*, 55 INDUSTRIAL & LABOR RELATIONS REVIEW 105 (2001); L. Mitlacher , *The Role of Temporary Agency Work in Different Industrial Relations Systems — a Comparison between Germany and the USA*, 45 BRITISH JOURNAL OF INDUSTRIAL RELATIONS, 581 (2007).

[34] See Gregory Hammond, *Flexible Staffing Trends and Legal Issues in the emerging Workplace*, 10 THE LABOR LAWYER 161 (1994).

[35] Leaving aside the question of the highly contested meaning of "efficiency", particularly as it is commonly employed in neoclassical economic analysis.

[36] This of course implicitly assumes significant rationality and benevolence of policy makers, and does not at all address the vast range of models of state behavior and democratic decision-making.

[37] Bruce Kaufman, *Labor Law and Employment Regulation: Neoclassical and Institutionalist Perspectives*, in LABOR AND EMPLOYMENT LAW AND ECONOMICS (Kenneth Dau-Schmidt, Orley Lobel and Seth Harris (eds.), 2009).

the firm."[38] Using this literature, Storrie provides a helpful summary of the legitimate benefits potentially generated from the use of *temporary help* services:[39]

a) *Economies of scale and an improved "division of labour"*. Economies of scale in the provision of certain functions may be provided by a staffing firm, where it carries out such functions across multiple firms, improving cost/quality tradeoffs. Commonly cited examples of such economies of scale that may flow, particularly to smaller users, include improved recruitment and screening functions, and improved regulatory compliance capacity.[40] Similar cost or risk pooling effects may enable efficiencies in the purchase or provision of insurance-like worker benefits relating to health, welfare, injury compensation, and/or retirement.[41]
b) *Diversification of employment risk*. This benefit may also be conceived of as being essentially a specific example of the economies of scale benefit in (a) above. Firms all face both firm-specific and market risks of hiring workers. Staffing firms may face lower risks, given their employment portfolios across multiple firms, of investing in employment.
c) *Increased "flexibility"*: Two main forms of flexibility enhancements have been identified. "Numerical" flexibility refers to firms' ability to adjust the number of workers utilized quickly. "Functional" flexibility, on the other hand, refers to the ability to adjust the configuration of different types of human resource skills available to the firm over time.[42]
d) *"Matching" improvements*: Through using short term placements, the worker and user are able to exchange information prior to committing to a longer term employment relationship.[43]

While there arguably remains significant space for normative concerns about the *effects* of triangular employment despite explanations for its growth based in neoclassical theory, some important points may also be made about interpreting these claims. First, it is important to remember that these claims have generally been raised within the analysis of one specific variant of triangularity, namely temporary help services. Given this paper's focus upon triangularity itself, it is important to note that some of the potential economic benefits produced by temporary help services are rooted in its temporal dimension, and not in its triangularity. This would appear to apply to the various notions of "flexibility" in (c) above as well as to potential "matching" efficiencies in (d), both of which have been repeatedly invoked in the literature. These benefits relate to a firm's ability to adjust either the numerical quantity, or qualitative nature, of the labour power it requires *over time*. Thus, it is somewhat imprecise to speak of temporary help services – comprising as it does both a triangular and temporal dimension – as being a bearer of these forms of flexibility. Rather, flexibility is embedded in the increased capacity for temporal adjustment, and the necessity of a triangular employment relationship in order to capture that

[38] Frank Knight, RISK, UNCERTAINTY AND PROFIT (1921); Storrie, *supra*, note 2; and L.I. Smirnykh, LABOUR LEASING: ECONOMIC THEORY, EU AND RUSSIA EXPERIENCE (Moscow: Russian-European Centre for Economic Policy, 2005).

[39] Storrie, *supra*, note2, at 33-35.
[40] Hammond, *supra*, note 34.
[41] Storrie, *supra*, note 2; and Willborn, *supra*, note 45. In the USA, the National Association of Professional Employer Organizations ("NAPEO") cites these sorts of benefits flowing from its services. See list of "frequently asked questions" at NAPEO website at http://www.napeo.org/peoindustry/faq.cfm
[42] Storrie, *supra*, note 2.
[43] Storrie, *supra*, note 2, at 34.

efficiency is a separate question for further analysis.[44] Of course, it is also true that there are also various other staffing service models that are explicitly *not* based on a temporal dimension. For example, employee leasing or PEO services arrangements in the U.S. do not normally include the provision of matching (Ie. recruitment, dispatch) functions. Here it all the more clear that any triangular employment thereby generated cannot be justified by reference to these particular conceptions of "flexibility", and their justification needs to be based on the remaining ground of economies of scale (including risk diversification, which, as noted, is a specific form of this).

At a more fundamental theoretical level, in considering the question of efficiencies generated by staffing services that appears to emerge from some neoclassical analysis, it is crucial to take seriously the nature of the service itself in an ontological sense. That is, we need to be able to analytically isolate an actually-existing or "concrete" staffing service supplied, from the law's response to such services, if any, and to clarify what exactly *is* the source of the efficiency. Here, it is possible that in certain actually-existing contexts, the imposition of *de jure* employer status may be (or appear to be) *legally* (as opposed to *actually*) required in order to enable the staffing firm to deliver the efficiency in question.[45] However, this may also be the product of prior policy choices and existing legal arrangements, which are adjustable. Arguably a true efficiency gain ought to be traceable to an underlying quality of the service itself, without entirely depending upon either prior policy choices, or potential legal responses to the arrangement, for its *prima facie* justification. Thus, the question of how *de jure* employer status is constructed and applied in triangular arrangements, and the consequences of this, should be conceived of as occupying a separate space, not necessarily implicated in (or constituting) the neoclassical conception of efficiency inherent in particular service arrangements. Arguments about efficiency gains that do necessarily depend upon either the maintenance of prior policy choices or a specific accommodation of the law to the service, are thus of a less fundamental, or "second-order" nature, since the extra constraints on socially-protective policy choices that these alleged efficiencies require for their realization must be taken into account.[46]

This also raises the question of the proper analytical counterfactual to be used in assessing efficiency claims about triangular employment arrangements. Wilborn describes this as considering how the workers would be treated, *ceteris peribus*, in the absence of the triangular arrangement.[47] However, this might be taken to imply that in the counter-factual scenario employed in analysis, the remainder of

---

[44] This analysis of flexibility here does not include the concept of "regulatory flexibility", or the evasion of regulation, a third form of flexibility identified in critical scholarship, since here I am attempting to address the more mainstream neoclassical arguments about flexibility. See Peck and Theodore, Temped Out?, *Supra*, note 2.

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

[46] Theron makes an intuitively similar argument in discussing the consequences of the "fiction" enshrined in South African legislation of the temporary employment service as the *de jure* employer. While he admits possible theoretical support for temporary employment service arrangements generally, noting for example that some workers prefer temporary work, he grasps the leap in logic, stating "there is no apparent gain for them [those who prefer temporary work] in designating the TES as employer". See Theron, *supra*, note 10.

[47] Steven Willborn, *Leased Workers: Vulnerability and the Need for Special Legislation*, 19. COMP. LAB. L.J. 85, (1997). While Willborn used the term "leased worker", his analysis suggests that he was essentially concerned with what are now more commonly referred to as temporary help arrangements. The same logic would seem to apply in either case.

the larger status quo context is held constant. This is a helpful but somewhat limited analytical approach. A more extensive analysis requires consideration of potential alternative legal/institutional arrangements. For example, in Part V of this paper, the potential for U.S. staffing firms to provide other firms with improved economies of scale in the provision of health insurance benefits is reviewed and accepted as a potential *bona fide* service provided by staffing firms. However, the analysis also shows that the market for this service is rooted in various prior policy choices in the regulation of health care in that country.[48] Employing a more thorough counterfactual, one might ask whether the particular efficiencies provided (here, economies of scale) might also be produced under alternative organizational forms and/or contracting arrangements that do not involve generating triangular employment. Alternative arrangements may not exist because of prior barriers imposed by the law, and thus existing law/policy may favour the use of triangular employment over other alternatives. Given the need to isolate concrete services from legal responses to such, analysis should also consider whether the alleged efficiency assumes particular legal responses/consequences, and considers competing alternative arrangements that do not depend on such "triangular employment" construction.[49] An example of this kind of analysis is found in Freeman and Gonos' exploration of the case for regulating temporary help firms despite the flexibility efficiencies they create, based on the greater regulatory burden imposed on union hiring halls, a key rival institutional arrangement.[50]

Further, alleged benefits that emerge from neoclassical theory of the employment relationship may be challenged on the same grounds that the neoclassical model is critiqued in general.[51] Indeed, the rationale for much of modern labour regulation may be understood as being anchored in institutionalist conceptions of the labour market and its critique of the various flaws in (or limits to) the neoclassical labour market model.[52] This institutionalist intuition, with its emphasis on so-called "market failures" such as imperfections in mobility, competition, information, and rationality may be understood as forming the basis for some of the critiques of triangular employment arrangements, and may also provide theoretical support for some alternative, and more critical explanations for the growth in staffing services.[53] For example, it could be argued that triangular employment relations exacerbate

---

[48] In other words, given the nature of other institutional arrangements, the triangular employment relations constructed may be understood an example of what the Varieties of Capitalism literature refers to as a "complementary" institutional arrangement, forming a complementary component of the particular cluster of inter-firm coordinating mechanisms in that economy. PETER HALL AND DAVID SOSKICE, VARIETIES OF CAPITALISM: THE INSTITUTIONAL FOUNDATIONS OF COMPARATIVE ADVANTAGE (2001).

[49] For example, some firms in the U.S. staffing industry are known as Administrative Services Organizations ("ASO"s). These firms provide many of the same services provided by Professional Employer Organizations ("PEO"s), by contract. The key distinction seems to be that under ASO contracting arrangements, the parties do not explicitly purport to contract for "co-employment". In other words, they don't claim any alteration in employer status as part of the bundle of services.

[50] Harris Freeman and George Gonos, *Taming the Employment Sharks: The Case for Regulating Profit-Driven Labor Market intermediaries in High Mobility Labor Markets*, 13 EMPLOYEE RIGHTS AND EMPLOYMENT POLICY JOURNAL 285 (2009).

[51] Kaufman, *supra*, note 37. .

[52] There is substantial recent literature on the search for a new normative paradigm to guide the ongoing development of labour and employment law. See Davidov and Langille, eds., THE IDEA OF LABOUR LAW, 2011. For the argument that much of this literature implies an acceptance of the dominant neoclassical paradigm to varying degrees, ironically while promoting the concept of "market failure" as labour law's *raison d'etre*, see Judy Fudge, *Labour as a 'Fictive Commodity': Radically Reconceptualizing Labour Law*, in THE IDEA OF LABOUR LAW, (DAVIDOV AND LANGILLE, EDS. 2009) 120-136.

[53] The definitional boundary between the neoclassical and institutionalist paradigms are somewhat unclear in that some ostensibly neoclassical analysis at times seeks to incorporate institutionalist critique into its domain.

existing informational asymmetries in employment, as the true state of authority, capacity, and responsibility allocation between the two "employing" entities becomes increasingly unclear to the worker, reducing his/her bargaining capacity (or increasing his/her bargaining "costs"), with potentially similar effects on his/her ability to *enforce* the bargain.[54]

Yet further alternative conceptualizations of triangular employment as a labour policy "problem" may exist, drawing from more critical literature. Although there is somewhat of a shared emphasis (with institutionalists) on the role of information, through the lens of critical theory, triangular employment relations may be seen as potentially affecting the nature of worker identities, interactions and solidarities. These dynamics factor in the overall construction of the balance of class forces and corresponding prevailing ideological conceptions. Extending Marx' classic notion of the fetish (the concealment from view of the true nature of social relations) produced by the commodity form and the false conception of labour (as opposed to labour power) as a commodity,[55] triangular employment relations may be understood as performing a complementary obfuscation function, both at the level of the firm, and cumulatively at a broader socio-political level, each of which factors into the balance of class forces. A related branch of critical theory similarly extends Marx' concept of a "character mask"[56], a social role that an actor (or group, class, institution, etc.) performs in which it falsely presents (or is the "bearer" of) the characteristics of somebody and/or something else. The mask performs a concrete function, with real effects, which assists in preserving the functionality and/or legitimacy of existing relations of production and social power.[57] An example of a critical analysis of triangular employment in this vein is Gonos' account of how trianguarity contributes to the concealment of surplus value and its appropriation, in part through the fiction of there being no fees for certain staffing firm services.[58]

Overall, this review of alternative perspectives on triangular employment suggests that there remains significant space for the claim that triangular employment represents a policy "problem", even if we accept the potential efficiencies like economies of scale generated by some services provided in some of these arrangements. As my review of (neoclassical) attribution of efficiency in these services suggests, it remains conceivable that a large part of the true benefit of services flows not only from efficiency

---

Examples are neoclassical references to "market failure", and so-called neoclassical analysis based on the work of Coase, which has elsewhere been cited as supporting the impossibility of fundamental tenets of neoclassical analysis. See Bruce Kaufman, *The Impossibility of a Perfectly Competitive Labour Market*, 31 CAMBRIDGE JOURNAL OF ECONOMICS 775. In a related critique of recent literature, Judy Fudge points out some of the logical contradictions in the use of the concept of "market failure" as a normative justification for labour law. See Judy Fudge, *Labour as Fictive Commodity*, *supra*, note 52.

[54] Here, we could conceive of the bargain as including legislated terms, since exacerbated informational problems could extend to these.

[55] See KARL MARX, CAPITAL, VOLUME 1 (1867), chapters 1-3. Marx argues repeatedly throughout CAPITAL and other writings that the true essence of economic transactions and relations between social actors, are not apparent.

[56] A Wikipedia page on this topic notes that "English translators of other writings by Marx & Engels, or of classical Marxist texts, quite often deleted *Charaktermaske* as well, and often substituted other words such as "mask", "role", "appearance", "puppet", "guise" and "persona"." See discussion at http://en.wikipedia.org/wiki/Character_mask#cite_ref-99, downloaded on May 1, 2013.

[57] See Max Horkheimer, *Montaigne and the Function of Skepticism* in MAX HORKHEIMER, BETWEEN PHILOSOPHY AND SOCIAL SCIENCE : SELECTED EARLY WRITINGS STUDIES IN CONTEMPORARY GERMAN SOCIAL THOUGHT (1993); Eduard Urbánek, *Roles, Masks and Characters: a Contribution to Marx's Idea of the Social Role*, 34 SOCIAL RESEARCH 529 (1967).

[58] George Gonos, *Never a Fee! The Miracle of Postmodern Temporary Help and Staffing Agency*, WORKING USA: THE JOURNAL OF LABOR AND SOCIETY (2000-01).

embodied in concrete functions, but rather from favorable legal consequences of revised arrangements, such as a shift in *de jure* employer status and/or corresponding erosion in the effect of labour law/policy on the user. In the real world of limited and imperfect legal/policy instruments, the possibility of benefits flowing from what might be termed a "regulatory gap" entering into the mix of benefits facing the user firm is quite feasible. Indeed, there is fairly substantial empirical evidence in the literature that triangular employment may lead to various effects of this sort,[59] raising the possibility that firms may obtain such gains as *byproducts* of service arrangements, intentionally or not. This reinforces the importance of examining the potential relationship between law/policy and triangular employment growth.

IV. "Regulatory Differentials" Across Alterative Employment Forms

As noted in the prior section, the claim that triangular employment relations may undermine the function of labour/employment law is not a new one. Both ILO reports and academic literature contain various references to triangular employment having such effects. Indeed, much analysis implies that triangular employment enables firms to "avoid" or "escape" the law or its effects, and it is also suggested that as the burden of employment regulation grows, firms increasingly use triangular employment relations in response, to avoid the growing burden.[60] But arguably, our understanding of how triangular employment enables this alleged avoidance is incomplete. Indeed, in some accounts, the process of "shifting" employer status onto a 3rd party staffing firm seems to be improperly understood as being *synonymous* with regulatory avoidance.

Here the U.S. case is informative. One of the most important explanations for the historical expansion in temporary help services in the U.S., and how this process is rooted in struggles over legal regulation, is found in the work of Gonos.[61] Gonos traces how temporary help firms were successful in a lengthy lobbying campaign throughout the 1960's and 1970's over constructing[62] its status as a new type of labour market intermediary. On the one hand, the industry was able to distinguish itself from the historical legal category of "employment agency", largely winning for itself exemptions from pre-existing regulations on these sorts of firms. Moreover, the industry gradually also succeeded in obtaining recognition of its member firms as the *de jure* "employers" of the workers they assign to client users for temporary work. As an early step, the industry convinced levels of government to accept unemployment insurance and payroll tax remittances concerning "its" employees, establishing the staffing firm as the *de jure* employer for such purposes. The staffing industry was then successful in gradually extending the domain within which its status as *de jure* employer was recognized over time. Gonos argues that user firms' increasing ability to count on the staffing firm's *de jure* employer status became a crucial factor in stimulating demand for these services. He argues that the construction of this temporary help formula, which then became embedded in the employment law landscape into subsequent decades, was itself a major deregulatory shift that coincided with and reinforced other, more well-known macro-level deregulatory shifts in industrial relations in the U.S. beginning in the 1970's.

---

[59] See for example the summaries of labour policy problems arising from temporary help agency employment provided in Vosko, Temporary Work, *supra*, note 2; Peck and Theodore, Temped Out?, *supra*, note 2; Bartkiw, Baby Steps, *supra*, note 2.

[60] Autor, *supra*, note 33.

[61] See Gonos, *The Contest Over Employer Status*, *supra*, note 18.

[62] Gonos' work is an excellent example of literature emphasizing the importance of strategic choices by actors, towards transforming the industrial relations system.

While Gonos' contribution is extremely important, his argument about the nature of deregulatory shift ends with the construction of the temporary help formula and the shift in *de jure* employer status to the agency/staffing firm. The more specific details about *how* this shift in *de jure* employer status achieves such a deep deregulatory effect, and the scope or limits of this shift, are not articulated. Indeed, much subsequent literature cites Gonos' seminal work on this deregulatory shift as seemingly confirming the benefit of regulatory avoidance via the shift in *de jure* employer status.[63]

Other analysis also seemingly adopts this rather simplistic assumption that the shift in *de jure* employer status creates the benefit of avoidance of the effects of the law for user firms. This intuition seems also to underlay comparative analysis of triangular growth across jurisdictions. In some studies, it is posited that the greater the regulatory burden imposed by the labour/employment policy regime in a given jurisdiction, the greater will be the use of triangular employment, as firms seek to avoid the regulatory burdens of the regime.[64] Again, neither the precise mechanisms nor the limits of this avoidance are clear.

In fact, the victory of the temporary help industry (and the entire staffing industry overall) in achieving *de jure* employer status – and the regulatory avoidance this engenders - is neither as simple nor as complete as some of the post-Gonos claims about regulatory avoidance suggest. Employer status in these contexts is generally determined on an *ad hoc* basis. Legal tests for determining the *de jure* employer continue to be based on the primacy of fact, and the tests in the U.S. have in most recent years depended substantially upon indicators of "control" (this is discussed in more detail in Part VI, *infra*.) Thus, in those cases where control over assigned workers by the staffing firm is severely lacking, *de jure* employer status of supplied workers may instead be reserved to the user. Further, *de jure* employer status is not necessarily robust across policy sub-fields or regimes, meaning that status may be allocated differently by adjudicators in different regimes or contexts. For example, the capture of *de jure* employer status for staffing firms under payroll tax rules does not guarantee a similar outcome for the purposes of minimum employment standards, labour relations, or workers compensation regimes, since there may remain some variation among the application of the common law tests across adjudicators within the specific regimes.[65]

Moreover, even where *de jure* employer status does shift to the "provider" (staffing firm), actual and complete avoidance of the effects of law is neither an obvious nor universal consequence. Where the staffing firm becomes the *de jure* employer, it then becomes subject to the full range of employer obligations in law, such as they are, within the jurisdiction. Here, the question remains why regulatory effect imposed on the staffing firm would not hold, and/or why its effects would not be internalized within the staffing service contractual arrangement? In other words, why would the effect of the law not simply be transferred back to the user as part of a rational contracting exercise? As a very simple

---

[63] See for example the references to Gonos' work in Peck and Theodore, *Temped Out*, *supra*, note 2.

[64] See Autor, *supra*, note 33; Mitlacher, *supra*, note 33.

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

example, suppose that employment law universally requires a minimum wage of $10 per hour. This same rule would apply regardless of whether the user or provider is the *de jure* employer. In the latter case, the provider would be required to pay the minimum wage, and we would expect it to charge the user for this mandated labour cost, plus markup. From the user's perspective here, regulation is formally equivalent across employment forms; there is no regulatory gap as between the employment forms. Note that the same outcome would seem to hold regardless of the size of the minimum wage imposed, so that either a $10 or $15 minimum wage would be similarly equivalent in effect across employment forms, there being no obvious regulatory gap to exploit from the triangular employment form in either case.

Overall then, despite fairly widespread acceptance of the basic intuition that a shift in *de jure* employer status enables user firms to *avoid* regulatory effects,[66] these effects are neither universal nor boundless, and thus these claims require some further articulation of how this process occurs, and the mechanisms at work in this process.

To this end, a more helpful concept in grasping the relationship between regulation and triangular employment growth is the concept referred to throughout the rest of the paper as a *regulatory differential*. Here, a differential effect of regulation occurs across employment forms. These regulatory differentials alter the effects of law upon actors, creating incentives for users to shift to triangular employment in certain contexts. It follows that in theorizing the effects of law on triangular employment growth, what is required is an extensive analysis of law with a view to deconstructing regulatory differentials embedded within the law, in one form or another, creating an ultimate potential benefit for the user.[67] This required analytical approach applies both in the analysis of a single jurisdiction, and in the comparative context. Here, a broad conception of the nature of law is necessary, recognizing the importance not only of explicit rules but of implied ones as well, establishing not only formal "rights" of parties, but also the various privileges, powers and immunities (as articulated in Hohfeld's famous typology),[68] shaped by the overall configuration and interaction of explicit and implicit rules, and patterns of enforcement.

Thus, I argue that certain differences in the way that law either formally applies to, or effects, triangular versus direct employment, which I call *regulatory differentials*, form a key determinant of triangular employment growth. There are multiple ways in which some component(s) of the law might constitute

---

[66] Similarly, in more recent literature examining the importance of the boundaries of the employment relationship, it is argued that through vertical disintegration and the use of various forms of external intermediaries, firms are not only able to "externalize their responsibility for employing labour", but the current basis for ascribing employment related obligations operates as an incentive to firms" to do so. See Judy Fudge, "The Legal Boundaries of Labour Protection", in Guy Davidov and Brian Langille, *Boundaries and Frontiers of Labour Law: Goals and Means in the Regulation of Work* (Oxford: Hart Publishing, 2006), at 314.

[67] Somewhat similar understanding of this more complex relationship between law and triangular employment growth is illustrated in the work of Peck and Theodore, who in their comparative analysis of staffing industry growth across jurisdictions point out that the industry is highly active in *both* less and more regulated countries. They argue therefore that the true domain of the temporary staffing industry lies in what they call the murky "shadow" of regulation. Here, the industry seeks to function as a *relatively less* regulated employment form, exploiting the advantages that flow from "shedding many of the costs, risks, and longer-term responsibilities that accompany de jure employer status, all courtesy of the agencies employer of record designation". Peck and Theodore, *Flexible Recession*, *supra*, note 2. See also Peck and Theodore, Temped Out, *supra*, note 2; Peck, Theodore, and Ward, *Constructing Markets*, *supra*, note 2.

[68] W.N. HOHFELD, FUNDAMENTAL LEGAL CONCEPTIONS AS APPLIED IN LEGAL REASONING (New Haven: Yale University Press, 1919).

a regulatory differential, and these may be categorized by the different types of mechanisms or characteristics at play. The following taxonomy of types of regulatory differentials is helpful in fleshing out the range of mechanisms at play.

1) *Formal (de jure)* differentials. For a *formal* differential to exist, some aspect of law or policy *explicitly* provides for a differential treatment between direct and triangular employment. These formal distinctions may be further categorized as embodying either a *pro-regulatory* or *de-regulatory* thrust with respect to triangular employment,[69] with corresponding expected effects on triangular employment growth. Examples of employment law embodying a pro-regulatory formal differential could include:
    - higher minimum standards for workers in triangular employment (e.g. a statutory pay premium)
    - additional notice or informational entitlements for workers in triangular employment
    - special rules enabling collective bargaining of workers in triangular employment
    - taxes or payroll premiums levied on triangular employment

    Examples of deregulatory formal differentials could include:
    - lower minimum standards for workers in triangular employment (e.g. exemptions from standards applied to direct employment)
    - additional formal barriers on collective bargaining, or access to collective bargaining, for workers in triangular employment.
2) *Contingent* differentials: Here, the law does not formally distinguish between direct and triangular employment. However, law does formally provide for a distinction in treatment of an "employer" contingent on some other circumstance, the occurrence of which may be influenced by the use of triangular employment. An important example of this category are numerical thresholds of various sorts, such as "headcount" rules, in which the firm's number of "employees" determines the applicability of a particular rule.[70] These contingent differentials occur both in simple "headcount" form, or may involve more complicated calculations and/or comparisons of numbers or categories of employees, along with various related measures of their treatment.[71] In each of these cases, shifting *de jure* employer status of even some *subset* of workers may in various contexts cause the alteration or elimination of some legal effect, either with respect to the employees whose status is affected directly, or with respect to other related employees.
3) *Informal (de facto)* differentials*:* This last category is a fairly large one in which the particular component of law or policy in question formally applies consistently across employment forms. However, for various potential reasons, the *de facto effect* of the law/policy is not perfectly robust across the two employment forms. The strength of the differential effect may depend upon the mediating effect of social, economic or organizational factors. Academic literature and

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

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

[71] See for example the various non-discrimination rules employed in U.S. tax law, discussed *infra* in Part VI.

ILO Reports have identified a fairly large set of these sorts of informal or sociological effects of triangularity on the effects of law. Explanations include:

a. Triangularity increases worker confusion and obfuscation over formal allocation of employer responsibilities as between the user and provider;
b. Triangularity increases the cost/burden on workers in seeking to (re)negotiate terms and conditions of work;
c. Triangularity increases the cost/burden on workers in seeking enforcement of their formal rights and standards;
d. Triangularity increases the regulatory cost/burden on local authorities in the enforcement of their law/policy domain.
e. Triangularity may alter workers identity, expectations, social interaction, and solidarity.
f. Given the above, triangularity produces a general shift in bargaining power, away from the worker.

The above taxonomy may be used as a guide to deconstructing the relationship between law/policy configurations and triangular employment growth. It also provides an improved lens for comparative analysis of the growth of triangular employment across jurisdictions, one that is theoretically superior to simplistic explanations based on "more" versus "less" employment regulation within a jurisdiction.

To complete the analytical framework on the relationship between law/policy and triangular employment growth, the prevailing rules within the jurisdiction on the allocation of employer status are also an important variable. These rules serve either a bridging or gate-keeping function affecting the regularity or degree of shifting of *de jure* employer status away from user firms. Assuming some form and degree of regulatory differential embedded in the law, the *easier* it is to achieve a shift in *de facto* employer status, the greater will be the expected benefit from triangular employment. Thus, employer status rules in a given jurisdiction *mediate* the relationship between regulatory differentials and triangular employment growth in that jurisdiction. In this light, although employer status rules are not in themselves the underlying *source* of benefit or incentive, and although their effect is inherently *interactive*, employer status rules are also an important *independent* variable in the relationship between law and triangular employment growth.

Given the broad range of potential regulatory differentials within various subfields of labour law, it seems reasonable to assume that some degree of triangular employment growth is a likely and inevitable outcome in most regulated labour markets, absent specific policy aimed at its prevention. However, the nature and scope of these regulatory differentials varies across jurisdictions, creating a range of effects upon triangular employment growth.

The analysis in the remainder of this paper employs this basic theoretical claim about the importance of regulatory differentials in determining triangular employment growth. As a rigorous test of the theory, it employs comparative legal analysis to examine whether the theory helps to explain diverging growth rates in triangular employment in two jurisdictions, Canada and the U.S.. Unlike some other approaches to comparative legal analysis, national regulation here is not simply compared for the purpose of uncovering regulatory diversity for its own sake, nor for examining differences in relevant rule categories.[72] Rather, analysis is anchored in what might be called a "difference of differences" approach. This involves an extensive review of labour law, here by sub-field, with a view to uncovering

[72] See for example Silvia Spattini, *Agency Work: A comparative Analysis*, 1 E-JOURNAL OF INTERNATIONAL AND COMPARATIVE LABOUR STUDIES 169 (2012). Aaron B. Sukert, *Marionnettes of Globalization*, 27 SYRACUSE J. INT'L L. & COM. 431 (2000).

whether, and the degree to which, those sub-fields embody regulatory differentials that help us understand the diverging rates of growth in triangular employment in Canada and the U.S. over the past few decades. The next section provides a statistical description of this divergence in triangular employment growth.

V. Staffing Services Growth in Canada and the U.S.

While recent growth in certain forms of triangular employment, like temporary help services, has attracted academic and policy interest, comparative analysis of growth in triangularity *per se* has been comparably limited. The relative lack of attention to triangularity in forms other than temporary help goes hand in hand with the lack of attention paid to the divergence in triangular employment between Canada and the U.S. over the past two decades, insofar as this divergence has been largely driven by staffing services other than temporary help.

Data on the staffing industry overall and its various subcomponents is somewhat limited, particularly with respect to Canada. From 1980-1997, official data employed the "3-digit" SIC 1980 industry category of "771 Employment Agencies and Personnel Suppliers," with "4-digit" subcategories of "7711 Employment Agencies" and "7712 Personnel Suppliers." The former subcategory referred to various types of placement and matching related services, excluding those relating to the "supply" of workers ostensibly employed by the staffing firm, which fall under the second subcategory. In 1997, Canada and the U.S. adopted the NAICS industrial classification system, renaming the "4-digit" industry category to "5613 Employment Services", now with 3 subcategories: "56131 Employment Placement Agencies", "56132 Temporary Help Services," and "56133 Employee Leasing Services." So, beginning in 1997, official data in Canada now was supposed to differentiate between two types of industries both involving triangular employment: temporary help and employment leasing services, the latter being non-existent in Canada prior to 1997. This shift was made in order to harmonize categories in the two countries, since official data in the U.S. had already previously employed such a distinction for some time. Then, with the revision of NAICS in 2002, industry category "56133 Employee Leasing Services" was renamed "56133 Professional Employer Services". This change in definition essentially mirrored the "rebranding" of this industry in the U.S..[73] However, despite the use of these new categories by Statistics Canada, there is very limited data available on this PEO industrial sub-category, likely because of the very small size of this sub-industry in Canada. For example, there is no reliable annual data series on the number of workers "employed" under PEO arrangements. However, in its annual Report on the Survey of Services Industry: Employment Services, Statistics Canada does provide some helpful data on annual aggregate industry *revenues*, broken down by industry sub-category. In the case of temporary help and PEO services, revenues may to some extent serve as a proxy for the total market value (and volume) of "employment" embedded within these different types of services.

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

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

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

Source: Survey of Employment, Payroll and Hours.

Table 1 contains data on employment[74] levels in the aggregate "employment services" industry (read staffing industry) in Canada for years 1982-2009. The data reveal some important trends. First, it is clear that employment in the industry overall grew substantially in Canada from 1983 to its peak in 2007. Further, this was disproportionate to the growth in aggregate employment, and thus the industry's share of aggregate employment levels similarly experienced a growth trend up until 2005, after which its employment share has declined slightly.

[74] Employment levels reported for these industries would include staff directly employed and working in staffing services firm administration. Nevertheless, the vast bulk of employment reported in these statistics represents workers assigned to clients, and thus most prior literature uses this as one potential proxy for employment levels and growth. Since data may be affected significantly by variations in assignment length, industry revenues are also used as a helpful additional proxy.

Available data does not allow us to decompose these employment levels in Canada across industry subcategories. Despite the clear growth trend, based on the measures employed in Canadian official data, the industry's share of aggregate employment overall peaked at about 1.1% in 2006.

Table 2 presents employment data for the U.S. employment services industry. The data fairly clearly confirms that the industry overall experienced substantial employment growth from 1982 to 2009. Unlike the Canadian case, the data does not suggest the occurrence of a previous peak in employment levels for the employment services industry overall. Other important contrasts also emerge. First, the U.S. employment services industry appears to be comparably much larger than the Canadian, when calculated as a share of aggregate employment. Further, until approximately 2000, significant growth in the temporary help sub-category yielded a positive trend in this sub-industry's share of aggregate employment. However, since 2000, this sub-industry's growth has not outpaced aggregate employment, resulting in it having a fairly stable (Ie. stagnant) employment share.[75] This positive trend to approximately 2000, and the peak at that time, is confirmed by both the CES and CBP data sources. However, the U.S. data also reveals that despite bounded growth in temporary help, the combined staffing industry's overall employment share nevertheless continued to grow, due to remarkable employment growth in "professional employer" services. The CBP data series reveals that employment in this sub-category grew from approximately 436 thousand employees in 1988 to about 2.07 million employees in 2008, a growth rate of 374% over two decades!

An additional perspective reinforcing these growth patterns is provided by data on industry revenues, a proxy for the market value of labour supplied under these triangular arrangements. Table 3 provides data on operating revenue for the employment services industry category in Canada from 1982 to 2010, along with a breakdown of the allocation of these revenues across the industry subcategories beginning in 1998. By the year 1998, the first year for which annual breakdowns of revenues across sub-categories are available, temporary help services constituted the largest share of aggregate revenues by far at 81%. This very high proportion of overall revenues remained fairly stable, with some variation through 1998-2005, after which it appears to have declined. While Canadian industry revenues overall continued to grow, a disproportionate share of revenue growth since 2005 resulted from growth in employment placement and executive search services.

At the same time, prior to the most recent years of 2009-10, the data fairly clearly shows that "professional employer" services have throughout the entire period of study remained a very small and insignificant portion of the Canadian staffing services industry. Indeed, it is instructive to note that in its annual publication of these statistics, Statistics Canada has consistently presented this third sub-category of revenues – those resulting from neither placement nor temporary help services – as a category of "Other" services, suggesting a lack of confidence in the ability to attribute these revenues to "professional employer" services. Even as an ambiguous catchall, the proportion of services represented by this "Other" category only grew very recently (during 2007-10).

[75] Peck and Theodore similarly discuss an upper limit to the growth in the proportionate size of the temporary help industry (without analyzing the other components of the staffing industry) in Peck and Theodore, Temped Out*, supra*, note 2.

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

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

Source: SIC 736, 7361, 7363 data from Current Employment Statistics; NAICS 5613, 56131, 53132,56133 data from County Business Patterns.

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

Overall, the data reveal an important divergence in growth in staffing services involving triangular employment in North America. Such growth has been far greater in the U.S. in recent decades, where it has been based in two separate sub-industries and business models (temporary help and professional employer services), compared to the largely singular industrial source of triangular employment in Canada (temporary help services).

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

Year	Total revenues	Temporary Help %	Placement %	Other[76] %
1982	433.0			
1983	537.0			
1984	713.0			
1985	945.0			
1986	1154.0			
1987	1422.0			
1988	1776.0			
1989	2105.0			
1990	2105.0			
1991	1891.0			
1992	1752.0			
1993	1844.0			
1994	2110.0			
1995	2479.0			
1996				
1997				
1998	4,047.3	81.0	18.0	--
1999	n/a	n/a	n/a	n/a
2000	5144.1	75.7	21.5	2.8[77]
2001	5125.0	79.0	18.4	2.6
2002	5420.7	79.3	18.6	2.1
2003	5689.1	79.7	19.5	0.8
2004	6268.9	79.0	19.3	1.8
2005	7402.0	77.2	21.7	1.1
2006	8217.5	68.9	29.7	1.4
2007	9108.2	59.6	36.4	4.1
2008	9323.1	60.2	36.8	3.0
2009	8583.7	60.7	30.7	8.6
2010	9298.6	56.3	35.6	8.1

Source: Annual Report on the Survey of Services Industry: Employment Services, Statistics Canada
Note: Wherever applicable, "revised" estimates are used for each year published in subsequent annual reports.
Note: Data for 1982-1995 are based on the SIC 1980 industry 3-digit category 771 Employment Agencies and Personnel Suppliers. Data from 1998 are based on the NAICS.

[76] The title "Other" is used by Statistics Canada in these annual Reports, and seemingly reflects a view that this latter category is more of a catchall category, one that cannot be said to simply represent revenues relating to employee leasing or professional employer services.
[77] Statistics Canada estimates that in 2000, 1.3% of overall industry revenues were from "payroll services" and 1.5% were from "other" services.

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

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

Source: Economics Census for applicable years.

VI. Comparing Regulatory Differentials in Canada and the U.S.:

The paper now explores the extent to which regulatory differentials provide a potential explanation for the divergence in triangular employment growth in the U.S. and Canada. Of course, it is possible that the divergence in triangular employment growth may be rooted in multiple fields, but a complete analysis pertaining to all potentially relevant subfields in Canada and the U.S. is beyond the scope of this paper. Rather, analysis is limited to sub-fields of regulation of retirement plans, and the regulation of employer provided health care benefits. First, however, a brief review of the common law approach to determining employer status in Canada and the U.S. is provided.

The most common legal test for determining employer status in the U.S. has been referred to as the "common law agency test", which relies heavily on indicia of control and supervision, and thus has sometimes been referred to as the "right to control" test.[78] This approach involves case-by-case application of an extensive, although non-exhaustive, list of relevant factors, including thirteen factors cited by the Court in Community for Creative Non-Violence v. Reid,[79] and applied with approval by the Supreme Court in Nationwide Mutual Insurance Co. v. Robert T. Darden ("Darden").[80] In this approach "special weight is given to the control of the manner and means by which assigned tasks are completed."[81]

Over time, there have been other "tests" employed by U.S. courts and adjudicators in different contexts, emphasizing somewhat different criteria. While some commentators have argued that there is little substantive difference between the alternatives, conceivably they signal some subtle emphasis of certain factors over others. Some of these alternatives have been referred to as the "economic realities" test, the "hybrid" test, the "common law entrepreneurial control" test, or the "statutory purposes" test.[82] The "statutory purpose" test is an approach that is *broader* than the common law approach[83] in which the adjudicator expressly looks to factors seemingly beyond the normal indicia of control emphasized in the common law approach to other factors based upon an interpretation of the

[78] See Nationwide Mutual Insurance Company v. Robert T. Darden 503 US 318; 112 SCt. 1344 (1992). ("Darden").
[79] 490 U.S. 730, 751-52 (1989). Darden was a case involving issues of entitlement to employer benefits, while the Community for Creative Non-Violence case concerned copyright protection.
[80] Darden, *supra*, note 78.
[81] See Mitchell Rubinstein, "Employees, Employers, and Quasi-Employers: An Analysis of Employees and Employers Who Operate in the Borderland Between an Employer-And-Employee Relationship", 14 U. OF PENNSYLVANIA JOURNAL OF BUSINESS LAW 605, (2012), at 652.
[82] See Rubinstein, *Ibid,* at 619-624.
[83] Darden, *supra*, note 78.

goals of the particular statute in question and/or the mischief it is aimed at redressing.[84] The "economic realities" test purportedly looks beyond indicia of control to examine underlying factors generating "economic dependence" of the worker upon the entity. One court sited the following as additional factors suggesting dependence: relative investments of the worker and alleged employer, the degree to which the worker's chance of profit or loss it determined by the alleged employer, skill and initiative required in work performed, and the permanency of the relationship.[85] While there is some uncertainty and debate about the precise scope of this test and the degree of substantive difference between it and the general common law test, it is fair to say that this approach is considered to be a relatively more expansive, and inclusive concept of employee status.[86] The so-called "Hybrid" test is said to combine the common law and economic realities test and attempt to steer a middle ground.[87] Here, the court gives significant weight to both indicia of control, and economic dependence.[88]

In the triangular employment context, at least one employer exists. Since many of the questions animating the alternative tests are aimed at distinguishing employees from independent contractors, (eg. presence of entrepreneurial control) these aspects of the differences between the alternative approaches are less significant for the purposes of this paper.[89] In any event, in Darden, the U.S. Supreme Court narrowed the acceptable approach to determining employer status. It held that the common law agency test (emphasizing indicia of control/supervision) should be the "default" test for employment, unless the underlying statute explicitly specifies an alternative definition of "employee".[90] This suggests that the U.S. approach to employer status determination in recent decades has been one that shuns a broader "purposive" approach in favour of a more mechanical approach focused on indicators of control, and that restrains adjudicators wishing to apply the employer concept more expansively.[91]

This adjudicative shift shunning a purposive approach to employer status determination has arguably made it easier to construct staffing arrangements in which the supplier would be deemed a *de jure* employer. Lobel argues that over time, industry actors have undoubtedly learned to adjust the factual

---

[84] See the decision of the U.S. Supreme Court in NLRB v. Hearst Publications, Inc., 322 U.S. 111 (1944). Rubinstein notes that since the Court in this case also referred to "underlying economic facts" and "economic relationships", the line between this test and the economic realities test is "blurred", to the extent that some commentators simply refer to this approach taken in *Hearst* as the economic realities test. See Rubinstein, *supra*, note 88; Noah D. Zatz, *Beyond Misclassification: Tackling the Independent Contractor Problem without Redefining Employment*, 26 ABA J.LAB. & EMPL. L. 279 (2011).

[85] Hopkins v. Cornerstone Am, 545 F.3d 338, 343 (5th Cir. 2008), *cert. denied*, 129 S. Ct. 1635 (2009).

[86] Darden, *supra*, note 78

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

[88] See Rubinstein, *supra*, note 81, at 626-628.

[89] For similar reasons, I have not been concerned with the question of whether the factors involved in the tests for employee status are different from those employed in assessing whether workers are employees of the entity. IN other words, this paper ignores the more obscure question of whether *employer* status may somehow exist in the absence of *any* corresponding employee status. See Rubinstein, *supra*, note 81, at 632-38.

[90] See Darden, *supra*, note 78. As noted earlier, courts have seemingly sanctioned the slightly broader approach of applying the concept of "dependency" under the Fair Labor Standards Act. See Tony & Susan Alamo Found. v. Sec'y of Labor, 471 U.S. 290 (1985).

[91] Jeffrey Sack, Emma Phillips and Hugo Leal-Neri, *Protecting workers in a changing workworld : the growth of precarious employment in Canada, the United States and Mexico* in THE EMPLOYMENT RELATIONSHIP: A COMPARATIVE OVERVIEW (Hart: Guiseppe Cassale, ed., 2011).

characteristics and contractual provisions in staffing arrangements, in order to maximize the likelihood of the staffing firm being the *de jure* employer.[92] Similarly, Lenz notes that through the use of onsite managers or "managed services", it is usually possible to construct the necessary degree of control in the hands of the staffing firm required for it to hold *de jure* employer status.[93] Such arrangements may be constructed for either temporary or non-temporary purposes.

Canadian law contains somewhat similar tests for the determination of *de jure* employer status as used in the U.S., involving a review of numerous relevant factors on a case-by-case basis. The most commonly articulated test for determining the "true" employer, set out in York Condominium, involves a review of various factors:

- the party exercising direction and control over the employees;
- the party bearing the burden of remuneration;
- the party imposing discipline;
- the party hiring the employees;
- the party with authority to dismiss the employees;
- the party who is perceived to be the employer by the employees; and
- the existence of an intention to create the relationship of employer and employee.

In 1997, the Supreme Court of Canada in *Pointe-Claire*[94] identified similar criteria in its decision concerning the *Quebec Labour Code* which has slightly different criteria for establishing the identity of the employer. However, the Court signaled that a broad analysis is often required, looking beyond indicators of control or supervision. The Court stated:

> "According to this more comprehensive approach, the legal subordination and integration into the business criteria should not be used as exclusive criteria for identifying the real employer. In my view, in a context of collective relations governed by the *Labour Code*, it is essential that temporary employees be able to bargain with the party that exercises the *greatest control over all aspects of their work--and not only over the supervision of their day-to-day work*. Moreover, when there is a certain splitting of the employer's identity in the context of a tripartite relationship, the more comprehensive and more flexible approach has the advantage of allowing for a consideration of which party has the most control over all aspects of the work on the specific facts of each case. Without drawing up an exhaustive list of factors pertaining to the employer-employee relationship, I shall mention the following examples: the selection process, hiring, training, discipline, evaluation, supervision, assignment of duties, remuneration and integration into the business.[95]

The Supreme Court of Canada also noted that within the extensive jurisprudence on the question of the true employer, over time certain factors have become more important than others.[96] The most

---

[92] Orley Lobel *The Slipperiness of Stability: The Private Employment Agency and Flexible Work Arrangements*, *Symposium: The Role of Contract in the Modern Employment Relationship,* 10 TEXAS WESLEYAN LAW REVIEW 109 (2003).
[93] Lenz, *supra*, note 19.
[94] [1997] 1 S.C.R. 1015
[95] Ibid, para 48.
[96] Ibid.

important goal is to try to guage which entity has the greatest overall control over the employment relationship *in its entirety*.

Overall, while there is much consensus in Canada that "control" remains a very important factor, it is fairly clear that no one set of factors is determinative, and that the approach must be a broad and "purposive" one, designed to ascertain the true overall "substance" of the relationship, implying potentially less focus on surface "form".[97] Compared to trends in the U.S., Canadian adjudicators seem to have embraced the broader, expansive and more "purposive" examination of the "essence" of the relationship, reminiscent of the "economic realities" approach in the U.S., that was rejected by the U.S. Supreme Court in 1990 in Darden. This suggests that there are comparably fewer degrees of freedom in the hands of US adjudicators to reject the transfer of employer status from user to client, based on the transfer of day-to-day control functions consciously assigned to suppliers under many modern staffing arrangements. Thus, to the extent that there are regulatory differentials in Canadian or U.S. law, U.S. common law enables the realization of potential gains available, to a comparably greater degree.

VI.1. The Regulation of Retirement Plans

Neither Canadian nor U.S. law requires employers to provide their workers with retirement/pension benefits. However, other aspects of regulation may affect employers' incentives when deciding whether to provide benefits, the quantity provided, and the distribution of benefits. As well, both countries have, for more than a half-century, provided workers with access to public pension programs providing limited retirement-age benefits.[98]

In 1974, the U.S. federal government adopted a protective regime establishing various minimum standards in administration, disclosure and content controls in the Employee Retirement and Income Security Act (ERISA),[99] which regulated (albeit to quite different degrees) both "pension"[100] and "welfare" benefits plans of various sorts. In addition to the "labour law" standards set out in the ERISA regime since 1974, the Internal Revenue Code ("IRC") also contains various other crucially important components of pension regulation in the U.S., in the form of substantial tax subsidies for "qualified" pensions, along with the myriad of rules determining plan qualification.[101] Some of ERISA's rules on vesting, service, benefit accrual requirements, and pension content controls were duplicated in the Internal Revenue Code, imposing them as additional requirements for pension qualification, and hence preferential tax treatment.[102] The aggregate size of this tax subsidy for qualified private pension plans in the U.S. is huge, in the range of $100 billion annually,[103] and thus it is generally recognized that the tax

---

[97] See 671122 Ontario Ltd. V. Sagaz Industries ([2001]2 SCR 1983, Rizzo and Rizzo Shoes (Re) [1998] 1 SCR 27; Sack, Phillips, and Leal-Negri, *supra*, note 121, at 255.

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

[99] P.L. 93-406, 88 Stat. 829 (Sept. 2, 1974).

[100] The definition of a pension plan under ERISA is quite broad, and is broader than the meaning of a pension plan under the Internal Revenue Code. Under ERISA, a pension plan includes the plans covered by the tax definition of pension plan, plus most profit-sharing, stock bonus, and annuity plans. See Peter J. Wiedenbeck, "ERISA: Principles of Employee Benefits Law", (New York: Oxford University Press, 2010), p. 6.

[101] I.R.C. s. 401(a).

[102] The PBGC termination insurance system contained within ERISA was the main exception. See Wiedenbeck, *supra*, note 100, at 288. Note also that while some of ERISA is reproduced in the tax code, the opposite is not generally true, in that the I.R.C. rules on tax qualification, such as the non-discrimination measures, are not part of ERISA.

[103] Ibid, page 21.

rules have "an enormous influence that largely determines the structure and scope of any employer plan (considered singly) and of the entire employment-based pension and health insurance systems of the United States".[104]

There are three aspects of the preferential treatment flowing from plan qualification under the IRC: the employer may claim the cost of the plan benefit as a tax deduction;[105] earnings on the pension trust funds are exempt from taxes until distributed[106]; and covered employees do not have to pay income tax on the employer's contribution to the plan.[107] The IRC "exclusive benefit rule" requires that funds must be held in trust for exclusive benefit of "employees"[108] and their beneficiaries, and thus the common law test for "employee" is an important concept in this area.

Given the significant size of the tax subsidy provided to private pension plans, the Internal Revenue Code has also for a long time contained provisions designed to encourage a more egalitarian distribution of retirement benefits than what would otherwise occur. In this vein, U.S. tax law has linked qualification of retirement plans to satisfaction of certain egalitarian principles of "non-discrimination" in coverage and benefits.[109] The Revenue Acts of 1938 and 1942 imposed certain basic requirements that qualified plans could not discriminate in favour of highly compensated employees (HCEs). In 1942, Congress began to close the "loophole that permitted discriminatory plans" by adopting legislation that "disqualified pension plans that discriminated in favour of officers, shareholders, supervisors, or highly compensated employees."[110] In 1974, Title II of ERISA amended the IRC in various ways, including the adoption of rules aimed at preventing the skirting of existing non-discrimination provisions through creative (re)arrangements in corporate structure.[111]

In addition to creative corporate (re)structuring, third party staffing arrangements also emerged as potentially valuable tools in the skirting of IRC pension plan qualification tests. From the outset, the IRS applied the traditional common law tests for employer status to scrutinize the "legitimacy" of the growing number of staffing arrangements and protect against the use of staffing arrangements as a loophole around plan qualification requirements.[112] However, this approach seemingly left space for the

---

[104] Ibid., page 5.

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

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

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

[108] I.R.C. s. 401(a). In other words, employers may not include workers in their plans that are not their common law employees. See Darden, *supra*, note 78.

[109] Purcell and Staman, *supra*, note 107.

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

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

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

construction of staffing arrangements that would result in the transfer of employment status to the staffing firm, enabling avoidance of these rules to some degree in a range of potential circumstances. As Cohen notes:

> "In these rulings, the IRS typically found a common-law employer-employee relationship to exist between a leasing organization and its leased employees where the organization operated in a manner which was similar to the organization described in [Revenue Ruling 75-41] (e.g., the leasing organization had the right to control and discharge the employees and was in charge of recruiting, hiring and evaluating employees. Notably, many of the rulings found an employer-employee relationship between the leasing organization and the leased employees notwithstanding the organization's practice of hiring former employees of the subscriber."[113]

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

> "…any person who provides services to the recipient if
>
> (A) such services are provided pursuant to an agreement between the recipient and any other person (in this subsection referred to as the "leasing organization"),
> (B) such person has performed such services for the recipient (or for the recipient and related persons) on a substantially full-time basis for a period of at least 1 year,[114] and
> (C) such services are of a type historically performed, in the business field of the recipient, by employees."[115]

This language contained multiple ambiguities. One significant issue was the relationship between the traditional common law concept of an employer-employee relationship and this new concept of a "leased employee". Did one concept preclude, or alternatively presuppose the existence of, the other?[116] To supposedly aid in the interpretation of this subsection, in 1984 Congress passed a slight revision to 414(n)(2), changing the language in the definition from "any person who provides services

---

[113] Ibid, p.3.

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

[115] IRC, s. 414 (n) (2).

[116] See Arlin, *supra*, note 110. Arlin cites this as a significant ambiguity despite the fact that at the time, IRS Question and Answer Guidelines stated that a common law employee of the recipient "is an employee of the recipient for all purposes and without regard to the provisions of section 414 (n). Notice 84-11, 1984-2, C.B. 269, 270."

to the recipient" to "any person *who is not an employee of the recipient and* who provides services to the recipient".[117] Although arguably still ambiguous, since the word "employee" continued to be undefined, this revised language seemingly suggested that workers would thereafter be treated as "employees" of the recipients under the IRC provisions to which 414(n) applied in two separate ways. First, they would be treated as employees wherever traditional common law tests suggested they were employees. Secondly, even where they were not found to be employees under the common law, they were to be deemed employees where they met the requirements of 414(n)(2). Although some ambiguity continued to linger over this relationship between the common law tests and section 414(n)(2), this interpretative approach was eventually confirmed by the U.S. Court of Appeals (9th Circuit) in its 1998 decision in *Burrey v. Pacific Electric & Gas*.[118]

Beyond the question of the relationship between s. 414(n)(2) and the common law definition of employee, additional ambiguity embedded in this provision remained for some time, particularly with respect to subsection (c),[119] since it was quite unclear how the requirement that the "services are of a type historically performed, in the business field of the recipient, by employees" was to be applied. First, there was no clear understanding of the threshold level of regularity that was meant by work being "historically performed" by employees. Arlin notes that proposed Treasury regulations in the early 1980's

> "consider services to be historically performed by employees in a recipient's service organization or business field if it was 'not unusual' for employees to perform the services. This language implied that if services are performed perhaps thirty percent of the time by unleased employees, it is 'not unusual' for employees to perform those services. The IRS may, therefore, treat a leased employee as an employee under section 414(n), even though he provides services that are predominantly provided by leased employees in the relevant business field."[120]

Further, the scope of activities that should be deemed to constitute the "business field" within which comparison must take place was uncertain, and this could significantly affect the application of the provision. These significant ambiguities in the interpretation of IRC 414(n)(2) remained intact until a further revision to this provision occurred in 1996, discussed below. Notably, each of these ambiguities relating to subsection (c) of the definition, which remained intact throughout much of the 1980's, may be understood to have produced a relatively more *expansive* conception of a "leased employee", expanding the scope of enforcement of s 414(n)(2), *narrowing* the scope for using staffing arrangements to avoid plan qualification testing rules like the non-discrimination requirements.

As well, the three subsections in IRC 414(n)(2) are conjunctive, meaning that they all must be satisfied prior to supplied workers being deemed "leased employees" and counted as the user's employees under the pension qualification tests. The requirement in subsection (B) that the definition of leased employees would not be applied to workers unless they have supplied services to the recipient on a "substantially full-time basis for a period of at least 1 year" has from the outset functioned to narrow the scope of the provision, expanding the space for using staffing arrangements to avoid the pension

---

[117] Tax Reform Act of 1984, Pub. L. No. 98-369, s. 526 (b)(1), 98 Stat. 494, 874 (codified as amended at 26 U.S.C.A. s 414(n)(2) (West Supp. 1985)).
[118] 159 F.3d 388.
[119] See Arlin, *supra*, Note 153 for an analysis of the various interpretive issues under this section that persisted throughout the 1980's and much of the 1990's.
[120] Arlin, *supra*, note 110 at 867.

qualification testing rules in those contexts in which it is feasible to utilize staffing firms to supply workers on either a temporary (less than 12 months) or part-time (or less than "substantially full-time") basis. This section also mirrors the more general rule allowing for exclusion of workers from plan participation where they work on either a temporary (less than 12 months) or part-time basis (the "1000 hour rule").[121]

In 1986, Congress adopted much *stricter* coverage tests for retirement plans beginning in 1988.[122] Lenz summarized the new non-discrimination qualification requirements as follows:

> "A plan must cover (1) a percentage of rank-and-file employees equal to at least 70% of the percentage of higher paid employees benefited, or (2) a nondiscriminatory classification of employees based on objective standards and provide lower-paid employees an average benefit that is at least 70% of the average benefit provided to higher-paid employees… employers can no longer provide qualified retirement benefits simply by covering a nondiscriminatory classification of employees (eg. full-time salaried employees)."[123]

This prohibition of discrimination in favour of highly compensated employees applies with regard to coverage, amount of benefits, and availability of benefits, and applies to both "defined benefit" and "defined contribution" plans.[124] A highly compensated employee is defined as any employee who owns 5% or more of the firm, or whose compensation in 2009 exceeded $110,000 (indexed to inflation).[125]

The 1986 Tax Reform Act not only imposed these more stringent anti-discrimination measures, but also contained drastic reductions in income tax rates, particularly on higher income earners, with the top bracket marginal tax rate falling from 50 to 28 percent. Together, these two measures embody a contradictory tension. On the one hand, the new non-discrimination requirements tightened and increased the redistributional dimension of plan qualification rules, in that they may effect a transfer, to some extent and in certain contexts, from higher to lower income earners. However, the subsidy provided to high income earners, in the form of tax savings from qualification, reduces resistance to this redistribution, since there is space for a net gain to high income earners. The higher the underlying marginal tax rate on income, then the higher the value of the tax subsidy under plan qualification.

Thus, the 1986 tax reforms dramatically cut the tax subsidy to higher income earners for plan participation, with less being available for transfer to lower income earners via plan participation, and

---

[121] I.R.C. s. 202 (a)(1)(A).

[122] 1986 Tax Reform Act, Pub.L. 99–514, 100 Stat. 2085.

[123] Lenz, supra, note 19, at 26. Precise details of the coverage tests are in IRC s. 410(b). The definition of the concept of "highly compensated employee" is provided in IRC s 414 (q). For a much more detailed overview of the specifics of the non-discrimination tests, see Wiedenbeck, *supra*, note 143, pp 306-332.

[124] See Purcell and Staman, Supra, note 107 page 50.

[125] As well, "an employer may elect to count as HCEs only employees who rank in the top 20% of compensation in the firm, but must include anyone who owns 5% or more of the company." For a more detailed summary of the various tests, including tests relating to "actual contribution percentages" measuring the relative contribution rates for employee 401(k) plans, see Purcell and Staman, *supra*, note 107 page 51.

with less residual gain to induce/coerce continued participation in more relatively egalitarian plan arrangements.[126] The overall combined result is that after 1986, there was likely a substantial decline in employer (and high earning employee) willingness to participate in egalitarian qualified pension plans. This in turn would have increased pressure on employers to either reduce or discontinue pension benefits provision, or to develop strategies for avoiding the redistributional effects of plan qualification rules. Increasingly, with subsequent legal shifts in tandem, staffing services became an instrument to this end.

As noted, the Supreme Court issued its decision in Darden in 1992. To the extent that this expanded the space for transferring employer status to staffing firms, as already argued previously in this paper, a similar interpretive shift could reasonably be assumed to have occurred in the the application of the common law test within the taxation field. Additionally, in 1996, Congress enacted the Small Business Job Protection Act, which revised the definition of "leased employee" in IRC 414(n)(2) as of Jan 1, 1997. The new provision removed the reference to the requirement in subsection (C) that services were of the type historically performed by employees in the recipient's field of business, eliminating the two key sources of ambiguity in the previous definition. In the new provision, this element of the test in subsection (C) was replaced with the requirement that "such services are performed under *primary direction or control* by the recipient" (emphasis added).

This revision narrowed the definition of a "leased employee", in turn narrowing the circumstances in which supplied workers would fall under the definition. This meant expanding the space for firms to use supplied workers, without including them in pension coverage calculations. As Lenz notes: "This test [the *previous* subsection (C)] was widely criticized as being too broad in its application. The *control test significantly narrows the scope of the leased employee rules*" (emphasis added).[127]

Logically, the test only effectively applied to those workers not already deemed employees of the user under the common law (confirmed in Burrey v. Pacific Electric & Gas) which already placed significant emphasis on indicators of control. Therefore it is not likely that workers deemed staffing firm employees under common law would subsequently be deemed "leased employees", given that the latter test now required that "*primary* direction or control" reside with the user.[128] Thus, the 1996 revision was akin to *repealing* the requirement in subsection (c) that had previously broadened the scope of s. 414(n)(2) to function as an additional restriction *beyond* the common law test. Again, as noted repeatedly, the common law test itself also shifted to a degree after the 1992 Darden decision.

Although staffing firms have often faced a relatively heavier burden of proof on the question of "control" with respect to certain classes of workers (eg. office and clerical service workers),[129] in general the new definition of "leased employees" favoured staffing arrangements in which day-to-day direction and control was in the hands of the staffing firm. Services that explicitly transfer significant managerial control over the workers, sometimes referred to as "managed services", have become an increasingly valuable - and feasible – instrument, not only for avoiding common law de jure employer

[126] This insight about the interaction between the marginal tax rate and the degree of coercion that the non-distributive rules embody is from Wiedenbeck, *supra*, Note 100 pp. 306-311.
[127] See Lenz, *supra*, Note 19 at 28.
[128] Additionally, as Lenz points out, in the area of employee benefits, the concept of joint employment is generally not recognized, and thus the interpretive approach focuses on selecting the "true" common-law employer.
[129] Ibid.

status, but also for avoiding the effects of being deemed "leased employees" under IRC 414(n)(2).

Further, Lenz also points out that clients using "professional" workers supplied by a staffing firm, are also likely able to avoid the application of 414(n)(2). Here, Lenz notes that various kinds of professional workers (e.g. computer programmers, system analysts, engineers, doctors, lawyers, accountants, actuaries, etc.) will generally not be considered "leased employees":

> "if they regularly use their own judgment and discretion on matters of importance in the performance of their services and are guided by professional, legal, or industry standards. They do not have to be counted by the client, even though the staffing firm does not closely supervise them on a continuing basis and even though the client requires their services to be performed on site and in accordance with client-determined timetables and techniques."[130]

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

Further, the "safe harbor" rules, which allow for exclusion of "leased employees" where a pension meeting certain alternative tests is provided by the staffing firm,[131] do not significantly alter the analysis or conclusions of this section, given that the nature of the rules has almost completely eliminated the existence of qualified "safe harbor" plans in the U.S.[132]

U.S. regulation in this area has for much of the past century embodied a significant internal tension resulting from its attempt to use the employment relationship as a regulatory platform within a

---

[130] Lenz, *supra*, note 28.

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

[132] Lenz summarizes the effect of these provisions as follows: "Employees will not be treated as leased employees for pension plan purposes if they participate in a safe harbor pension plan provided by the leasing organization that meets the following conditions: The leasing organization must contribute at least 10% of the employee's compensation to the plan. The employee must be 100% vested in the contribution. In general, all leasing organization employees who provide services to clients must participate in the plan without any waiting period. This provision prevents a leasing organization from providing safe harbor plans that cover only the employees assigned to certain clients. If for any plan year, leased employees constitute more than 20% of an employer's non-highly compensated workforce, all of the leased employees furnished to the recipient will have to be counted, notwithstanding the existence of a safe harbor plan. Of course, a safe harbor pension plan does not relive recipients of the obligation to count leased employees for any other benefits plan subject to coverage testing. Few, if any safe harbor plans exist." See Lenz, *supra*, note 19, at 29.

market-based system for pension provision. Specifically, precise measurements of "discrimination" in distribution amongst groups of "employees", calculated at the decentralized level of the individual "employer", serve as fairly weak tools for achieving egalitarian pension coverage and distribution. This approach also sets in motion counteracting employer (and high earner employee) strategies to avoid the remaining coerced redistribution.

Non-discrimination rules in U.S. tax law have formed an important example of what this paper has referred to as a "contingent differential" within pension regulation, favouring triangular employment. The size of the relative gain, and the probability of access to it through a staffing services strategy, has been gradually expanded since 1986. Shortly after the creation of the "leased employee" rules in 1982, a double movement took place in tax regulation that increased pressure in favour of staffing services growth. On the one hand, in 1986, the non-discrimination rules themselves became sharper, increasing the relative gain in their avoidance. Simultaneously, revisions to the "leased employee" rules narrowed their scope, liberating firms to use triangular employment increasingly without being caught by these rules. Developments in tandem in the common law (Ie. Darden) further enabled employers to use staffing services, without threatening pension plan qualification and resulting tax subsidies.

Canadian regulation of employer pension plans do not contain analogous rules that can be interpreted as embodying the same sort of incentives/payoffs from employer status transferal. The pension standards rules contained in each province's legislation in general neither mandate the provision of any minimum coverage, nor any comparable rules about distribution amongst different groups of employees.

The closest analogue in Canadian pension regulation would be rules that specify that within classes of employees, which employers are free to establish in the plans themselves, employees must be treated "equally" in certain regards. However, since there are seemingly no rules requiring equitable treatment as between different classes, and significant freedom in the creation of alternative plans for different classes, these constraints would seem to barely, if at all, restrict employer freedom in allocation of pension benefits.[133] Rather, there is primarily emphasis placed on capping the size of tax savings that may be captured with respect to benefits provided to each *individual* employee, such as maximum contribution limits and related rules.[134] For defined benefit plans, there are also rules limiting the maximum pension that may be paid to an individual employee under such plans. These sorts of rules do not embody a regulatory differential in favour of triangular employment.

In general, Canadian pension law does not contain analogous sorts of "headcount" rules, nor any analogous rules conditioned by either the number of employees or the comparable treatment of different groups of employees. Overall then, in the area of regulation of retirement benefits plans, U.S. law has contained a stark regulatory differential favouring the use of triangular employment in a range of contexts that has been absent in Canada. Access to this differential has expanded significantly since 1986. This is consistent with the timing of the observed divergence in triangular employment between Canada and the U.S., suggesting that this area of law potentially helps explain this divergence.

---

[133] Some provinces have rules that prevent discrimination against part-time workers, which are similarly, not directly relevant.

[134] In Canada, there is a Registered Retirement Savings Plan contribution limit of 18% of an individual employee's income, up to a maximum aggregate contribution of $22,970. In the U.S., analogous rules exist in IRC s. 415.

VI.2. The Regulation of Employer Sponsored Healthcare Benefits

As with retirement plans, U.S. law similarly does not require employers to provide employees with health benefits. However, employment relations in the U.S. are mediated by the absence of universal health care, with the allocation of healthcare resources being relatively more determined by market mechanisms and private insurance schemes than in many capitalist economies, including Canada. The U.S. health care system thus relies much more substantially upon private employer provision of health insurance coverage, along with forms of employment-based regulation, to achieve healthcare policy goals.[135] However, even the provision of healthcare via "employers" ought to be understood as being at most *semi*-private in nature, given the preferential tax treatment (Ie. a tax subsidy from the state) that it garners. Recent estimates of the tax expenditure associated with exclusion of employer contributions towards medical insurance premiums and medical care range from $137-155 billion in 2010,[136] making health care benefits the most costly of all types of employer welfare benefits.[137]

While the tax preference given to retirement benefits is tax deferral, employer healthcare expenses are granted an outright tax exemption in the current year.[138] Further, tax treatment of *employer-sponsored* health benefits is comparably favourable to other health care financing arrangements such as individual self-insurance,[139] reinforcing the historical practice of using the employment relationship as a key platform for the governance of health care financing.[140]

This rather deep policy preference for employer provision of health care insurance coincides with a number of related dynamics in the market for "fully insured" health plans (Ie. plans purchased by employers from insurers) that are important for understanding the relationship between this regulatory field and triangular employment. The market for employer health insurance plans has historically been quite influenced by the reality of a wide distribution in employer sizes and, and certain quasi-fixed costs that are required to be absorbed by insurers in the sales, service and administration of each separate employer health plan. This produces significant economies of scale, enabling larger firms to reduce their costs of health insurance, while smaller firms pay substantially more, per employee.[141] In addition to this cost differential, the U.S. government also became increasingly concerned over time that small

---

[135] Medicare and Medicaid are available for the elderly and poor, respectively. In 2007, 61% of non-elderly Americans received health insurance coverage through an employer-sponsored program. See Henry J. Kaiser Family Foundation, Health Insurance Coverage in America, 2007, at 1 (cited in Wiedenbeck, supra note 100 at 383.

[136] Wiedenbeck, *supra*, note 100, at 7.

[137] Wiedenbeck, *supra*, note 100, at 6.

[138] Wiedenbeck, *supra*, note 100, at 384.

[139] Here both income and payroll tax advantages work to favour employer sponsored plans. See Wiedenback, supra, *note* 100, at 387-9. As well, preferential tax treatment in favour of employer provision also applies with respect to "income replacement" or "disability insurance" benefits. See Wiedenbeck, *supra* note 100 at 398.

[140] As healthcare costs have risen and cost-sharing arrangements have evolved, many employees have been increasingly required to contribute portions of the total costs of coverage. While the various rules are complex, in some cases this has lead to a reduction in the tax advantage overall, since employee expenditures generally received less favourable treatment. However, certain other arrangements may allow for employee contribution to be structured as part of a so-called "cafeteria plan", such as a "flexible spending arrangement", which may largely preserve preferential tax treatment for employee expenditures as well. See Wiedenbeck, *supra* note 100 at 390-2. Beginning in 2013, the PPACA limits the maximum amount that an employee can elect to contribute to a health care FSA to $2,500 per year.

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

employers were being disproportionately discriminated against, or otherwise mistreated by insurers. As a result, insurance law in the U.S. has for several decades bifurcated the market for employer health insurance into two notional product markets, namely "small group" and "large group" markets, and has imposed a relatively greater regulatory burden on insurers in the small group market.[142] This regulatory approach was intensified in 1996 with the passage of the Health Insurance Portability and Accountability Act ("HIPAA")[143], which imposed further regulatory standards and requirements, disproportionately directed towards small group plans.[144] Not surprisingly given this context, larger employers in the U.S. have a much higher healthcare benefits coverage rate.[145]

In this specific market context in the U.S., there would seemingly be significant latent economies of scale available for potential realization by a more coordinated system of insurance purchasing/provision across multiple smaller firms. Staffing firms, particularly those more commonly identified as PEOs, have been emerging as an increasingly popular tool for this task. Using the economies of scale from having multiple clients, PEOs may be able to purchase health insurance plans covering each client's "worksite employees", and provide clients' with greater insurance purchasing power. NAPEO claims that the average workforce size of PEO clients in the U.S. is approximately 19 employees.[146]

However, keeping with the analysis in Part II of the paper, the existence of this potential efficiency gain from this service is not in itself a sufficient justification for the triangular employment generated by the service. Yet, this healthcare insurance pooling function forms one of the key grounds for why the PEO industry embraces the concept of "co-employment", and struggles to preserve the PEO's status as "an" (if not at times "the") *de jure* employer of its clients' workforces.[147] This requires understanding certain aspects of the underlying structure of regulation of employer-provided health insurance in the U.S.

As noted above, employer provided health insurance plans are a form of "welfare plan" regulated under ERISA, a federal enactment, which largely pre-empts state regulation of employer sponsored health insurance. By contrast, state insurance regulation applies to insurance contracts and the relationship between the insurer and insured. The dividing line between state and federal authority in this area is fairly complex. Self-funded schemes are excluded from the preemption, while fully-insured arrangements more clearly fall under state regulation.[148] Further, since 1983, ERISA also exempted from preemption plans defined as "multiple employer welfare arrangements" ("MEWA"), reinforcing state-level authority to regulate these insurance arrangements.[149] With certain exceptions, a MEWA is defined fairly broadly as an "employee welfare benefit plan or any other arrangement … established or maintained for the purpose of offering or providing any benefit described in paragraph 1 [welfare

---

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

[143] Pub.L. 104–191, 110 Stat. 1936, enacted August 21, 1996.

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

[145] MARK MERLIS, THE AFFORDABLE CARE ACT AND EMPLOYER-SPONSORED INSURANCE FOR WORKING AMERICANS (Academy Health, 2012).

[146] NAPEO, 2009 Financial Ratio and Operating Statistics Survey. Note however that there maybe some concern about the reliability of measures of size of client firms measured by employee counts. For example, it is not clear in such surveys whether client self-reported headcounts include or exclude the very employees supplied by (or "co-employed" by) the staffing firm. See also Lombardi and Ono, *supra*, note 2.

[147] Stanton et al., *supra*, note 45.

[148] Wiedenbeck, *supra*, note 100, pp. 204.

[149] Public Law 97-473.

benefit plans] to the employees of two or more employers, including one or more self-employed individuals, or to their beneficiaries…".[150]

Although a plain reading of these provisions would seem to suggest that a PEO-constructed health plan arrangement, in which the PEO purports to sponsor a health insurance plan for the employees of its multiple clients, would constitute a MEWA, the PEO industry has long struggled to resist this classification. Instead, it has sought to have PEO health plan arrangements recognized as "single employer" plans, regulated by ERISA and not under the scope of state regulation of MEWAs. Here, the industry has faced significant hurdles. Significantly, the federal Department of Labor has consistently applied the common law employer status tests in this context, typically concluding that PEO plans fall within the definition of MEWAs set out in ERISA.[151] Varying somewhat with the specific context and state regulation in place, being legally designated a MEWA would almost always result in the PEO arrangement facing a much higher degree of regulatory burden, oversight, and typically cost, imposed by state insurance regimes.[152] This context generates significant competitive pressure on PEOs to be able to function at the margin of MEWA regulation, and to defend the legal position that they are (at least) an employer of the worksite employees, and that insofar as all of the workers therefore *share* the PEO as an employer, their plans ought to be accepted as single employer plans for the purposes of insurance regulation. To this end, NAPEO has pro-actively fashioned some additional insurance oversight rules into its model PEO statute for which it lobbies at the state level, along with statutory provisions that clarify that fully-insured PEO plans are to be treated as single-employer plans under state insurance law, and many states have adopted this regulatory compromise proposed by NAPEO.[153] Overall, it is fairly clear that this deeper historical and institutional structure of the market for health insruance, the systemic biases favouring "employer" provision, and the regulatory approach towards single versus multi-employer plans creates a range of contexts in which triangular employment relations have become effectively advantageous. These deeper healthcare and insurance based rules constitute regulatory differentials favoring triangular employment, and important factors in the staffing industry's expanding drive to claim "employer" status over the past few decades.

Various other examples of regulatory differentials arising out of the particularities of regulation of employer-based healthcare can also be identified Basic rules governing fiduciary standards, reporting and disclosure requirements, and procedures for appealing denied benefit claims have been in effect in the health policy field, as part of ERISA, since its adoption in 1974. Similar to the approach taken with retirement plans, tax rules relating to health benefit plans largely mirror ERISA's "labour law" standards on health plan content controls and process requirements. However, despite preferential tax treatment for health care expenditures similar to that given employer sponsored retirement plans, over-arching non-discrimination tax rules pertaining to health benefits have, until very recently under PPACA, not been imposed.[154] However, there are 3 exceptions to this general rule. First, s. 105(h) of the IRS prohibits discrimination in favour of highly compensated individuals under employer "self-insured" plans (in which the employer, rather than an insurer, assumes the risk of benefits costs). Second, where health benefits are offered as an option under the "cafeteria plan" rules, those rules also prohibit such

[150] 29 U.S.C. s. 1002 (40)(A).
[151] U.S. DEPARTMENT OF LABOR, MULTIPLE EMPLOYER WELFARE ARRANGEMENTS UNDER THE EMPLOYEE RETIREMENT INCOME SECURITY ACT (ERISA): A GUIDE TO FEDERAL AND STATE REGULATION, available at http://www.dol.gov/ebsa/Publications/mewas.html.
[152] Interview with key informant from National Association of Insurance Commissioners.
[153] See Stanton et al., *supra* note 45.
[154] PPACA reinstituted limited non-discrimination rules for welfare plans starting in 2010 or 2011. See discussion of PPACA *infra*.

discrimination. Third, a final set of rules prohibit contributions to "health savings accounts" in favour of highly compensated employees, without comparable contributions to rank and file employees.[155] Each of these exceptions represents a potential contingent differential, making triangular employment relatively advantageous in certain contexts.

Other legislation has been adopted over time that imposed additional rules upon employers requiring more extended coverage as a condition of tax qualification, while generating further regulatory differentials. The Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) added a new Part 6 to ERISA, which included various new rules requiring employers providing health coverage to temporarily *continue* plan coverage for plan participants and beneficiaries in various "qualified events", which would otherwise result in coverage loss.[156] These qualified events included the death of the covered employee, a reduction in the employee's working hours, and termination (except in the case of employee gross misconduct). Generally, continued coverage must be the same as that provided to similarly situated employees that have not experienced a "qualified event."[157]

Notably, COBRA applied these new coverage continuation requirements only to plans maintained by an employer with *20 or more employees*.[158] This "headcount" rule constitutes another contingent differential, creating potential savings from avoiding the higher premiums associated with plans caught by COBRA's extended coverage requirements if the organization's overall count of "employees" is below 20. The pressure to take advantage of this exemption would likely be felt mostly by small to medium size firms, where smaller changes in employee headcount could make the difference between being completely exempt from the extra burden under COBRA or not.

In the following year (1986), when Congress adopted the more rigorous and precise non-discrimination testing rules for pension plans, these requirements were not extended to health benefits plans.[159] Thus, most health plans remained covered by rules that permitted employers to provide benefits to nondiscriminatory classifications of workers.[160] As well, the "leased employee rules" set out in s. 414(n), adopted as part of TEFRA in 1982, do not apply to group health plans, leaving employer status to be essentially determined by the common law tests.[161]

In 1996, two other legislative revisions increased the regulatory burden on employer sponsored health care plans. The Health Insurance Portability and Accountability Act, amended Title 1 of ERISA by limiting the circumstances under which a health plan may exclude a participant with preexisting condition from coverage,[162] and prohibiting group health plans from basing coverage eligibility rules on certain health-related factors, such as medical history or disability, and prohibiting higher premiums based on such

---

[155] See Wiedenbeck, *supra*, note 100, at 395-7.

[156] Time limits for continuation of coverage requirements are contained in 29 U.S.C. s 1162 (2). Staman and Purcell note that under this section the typical requirement is that coverage continue for [up to] 18 months, but may be longer in certain circumstances. See Purcell and Staman, *supra*, note 107, p. 46.

[157] ERISA 602(1).

[158] 29 U.S.C. s. 1161, E.R.I.S.A. 601.

[159] Lenz, *supra*, note 19, at 26.

[160] Lenz notes that it is "not entirely clear, though, to what extent the determination of what is a nondiscriminatory classification is affected by the new objective standards applicable to retirement plans." See Lenz, supra note 19.

[161] The 414(n) leased employee rules apply to pension plans, life insurance plans, and so-called "cafeteria" plans. To qualify, a cafeteria plan must allow employees to choose from a selection of two or more benefits consisting of cash or qualified benefit plans. See IRC s. 125(d)(1).

[162] 29 U.S.C. s 1181 (a) (1)-(3). Such exclusions are now no longer permitted under PPACA.

health related factors.[163] The Mental Health Parity Act ("MHPA"), also adopted in 1996, imposes new rules requiring that plans offering mental health benefits must not impose lower annual and lifetime limits placed on medical and surgical benefits. Plans covering employees with 50 or fewer employees are exempt from the requirements of the MHPA, creating yet another additional, albeit minor, regulatory differential.

The recent overhaul of healthcare regulation adopted in The Patient Protection and Affordable Care Act ("PPACA")[164] contains three additional new sets of provisions containing regulatory differentials arguably reinforcing the tendency of health benefit regulation to generate triangular employment. First, PPACA adds a new section 45R to the IRC[165], providing a tax credit for employee health insurance expenses of "eligible small employers", defined as employers with fewer than 25 full-time equivalent employees ("FTEs"), who earn average annual wages of less than $50,000 per FTE, for whom the employer maintains a "qualifying arrangement".[166] The latter is a plan for which the employer pays a uniform percentage of the premium cost for each employee enrolled.[167]

Secondly, the PPACA's "Shared Responsibility" rules impose penalties on large employers, defined as those with 50 or more FTEs, if any of the employer's full-time employees becomes certified to receive an applicable premium tax credit or cost-sharing reduction payment under PPACA (which would generally occur where employers are failing to enroll employees in "minimum essential coverage", or the employer has offered such coverage that is unaffordable or fails to provide minimum value.[168]

Thirdly, PPACA extends the scope of plans covered by "non-discrimination" testing rules. While previously the only plans affected by non-discrimination rules were self-insured plans (under I.R.C. s. 105(h)), and cafeteria plans, PPACA prohibits discrimination in provision of health benefits in favour of highly compensated employees, by applying rules similar to those in I.R.C. s. 105(h)[169] to (non-grandfathered) fully-insured group health plans as well.

Overall, the combination of these new provisions in PPACA create certain economic incentives for firms to seek to adjust their headcount and employer status in various contexts, which will be particularly strong for those firms already closest in size to the applicable threshold.

Canadian health policy is substantially different in nature, given the existence of universal public health care provision in every province. In this context, although some employers provide extended health related benefits of various sorts that provide coverage beyond what is provided by the public system,[170] employer provided health care plays by comparison a very minor role as part of the health care system overall.

The only comparable laws in Canada that may conceivably be seen to embody any regulatory differential favouring triangular employment are certain rules within payroll tax systems established to help finance the public health system. In some cases, tax rates are levied in a progressive manner, with higher rates being levied on larger employers, defined by payroll size. However, using the Ontario rules as an

---

[163] 29 U.S.C. s 1182(b)(1).
[164] Pub.L. 111–148, 124 Stat. 119.
[165] Enacted by s. 1421 of PPACA.
[166] I.R.C. 45R(d)(1).
[167] IRS Technical Release No. 2012-01. , pp. 1-2.
[168] IRS Technical Release No. 2012-01. , pp. 1-2.
[169] See Public Health Service Act s. 2716.
[170] Dental plan coverage is one of the most common examples of such benefits.

example for analysis, there appears to be little reason to believe these rules would have any significant effect on triangular employment growth. The Ontario Employer Health Tax Act imposes a levy on the aggregate payroll of employers, with differential treatment being applied only to the first $400 thousand in payroll. Thus, differential treatment only occurs at very small payroll levels, affecting only very small employers. "Eligible employers" under the Act may be entitled to an exemption on this first $400 thousand, while others face a progressive scale of tax rates ranging from .98% on the first $200 thousand to 1.95% on payroll above $400 thousand. Here, there would seemingly be very few circumstances in which user firms would save substantially on employer status transfer, and the pooling of workers into the status of being employees of a third party staffing firm would in most cases result in the staffing firm having a payroll above the $400 thousand threshold.[171]

Overall, it is clear that health care costs are prohibitive and there are undoubtedly economies of scale to exploit in their delivery and/or financing of it in any jurisdiction. In the U.S., the existing model of health insurance provision by tax-subsidized employers poses a major problem for smaller employers. Triangular employment, notably the PEO concept, provides a mechanism for some potential improvements in economies of scale, while largely preserving or complementing the range of existing institutional arrangements. As understood in the literature on varieties of capitalism, triangular employment arrangements serve as a complementary institutional arrangement within the broader pattern of coordination in this specific liberal market economy. From a more critical lens, triangular employment concept may increasingly empower firms to avoid remaining egalitarian coverage-based rules in healthcare (some of which are the residue of insurance industry practices) not only because of formal avoidance of *de jure* insurance responsibility, but also because of the symbolic social importance that the concept of "employer" plays in allocating social and/or moral responsibilities. In this vein, it has been previously argued that triangular structures like PEO "co-employment" arrangements increase user firms' capacity to "wash their hands" of responsibility in the face of employee morale issues, bolstering their relational power and ability to further transfer the cost of insurance to the workers themselves, and/or to impose less egalitarian, tiered systems of coverage.[172]

VII. Conclusions

This paper has argued that there is an important relationship between triangular employment growth and characteristics of domestic labour law resulting in regulatory differentials, from the ultimate perspective of the user, between direct and triangular employment forms. The ways in which these regulatory differentials function and the different forms they take, is quite extensive, and a typology of these was developed. To the extent that certain staffing services embody, or are based upon a platform of triangular employment, this theory helps explain the uneven development of staffing services industries and implicated volumes of triangular employment across jurisdictions. As an important example, the recent divergence in growth in related staffing services in Canada and the U.S. was explored in this light. Comparative labour law analysis based in two key subfields, identifying the respective regulatory differentials within the two countries provided support for the theoretical claim by revealing how certain key regulatory differentials favouring triangular employment in the U.S. are absent in Canada, and that the timing of their emergence in the U.S. was fairly consistent with the timing of the observed empirical divergence in staffing services growth.

---

[171] The only remaining possibility for savings from employer status arbitrage under these rules would be from the use of a very small third party staffing firm.

[172] CENTRE FOR A CHANGING WORKFORCE, PEOS AND PAYROLLING: A HISTORY OF PROBLEMS AND A FUTURE WITHOUT BENEFITS (CFCW, 2001).

Although there is arguably a range of regulatory differentials in both countries fueling triangular employment growth, analysis illustrated the importance of somewhat extraordinary differentials in the U.S. embedded in the regulation of retirement plans and employer-sponsored healthcare benefits. While other areas of law may contain other regulatory differentials, the research goal was not to identify all potential examples of regulatory differentials. Rather, as an arguably more rigorous test, the paper explored whether this theory helped explain diverging growth patterns in two jurisdictions.[173] Of course, in reality, there are also various other causal factors driving triangular employment growth besides regulatory differentials.[174] For example, a key recent difference in the Canadian and U.S. industrial relations systems, which may be an important causal factor itself, has been the relatively more severe decline in unionization in the U.S.. In a separate work, I argue that labour relations law (Ie. law dealing with collective bargaining and access thereto) in Canada and the U.S. illustrate a similar pattern of there being more severe regulatory differentials in the U.S., exacerbating access to unionization in the U.S., for both supplied workers and direct employees. This suggests a potentially important *interactive* effect between the labour relations and the retirement and health benefits subfields, as developments in one field reinforce those in the other. As retirement and health benefits regulation encourages triangular employment growth, this reinforces union decline. In turn, as unionization declines, employee bargaining power to demand egalitarian pension and healthcare coverage declines, freeing user firms to use staffing arrangements to further avoid regulatory effects. Given a potential to exacerbate union decline, triangular employment growth may conceivably generate some self-reinforcing tendencies.

As noted, the expansion of regulatory differentials and the resulting growth in triangular employment may be understood as a complementary institutional arrangement within the larger configuration of inter-firm coordination and regulation in the archetypal liberal market economy, the U.S. Indeed, these developments may be understood as having deepened the (neo)liberal character of the U.S. variety of capitalism. The relaxation of the "leased employee" rules with the resulting eroded effect of the non-discrimination rules, amount to an indirect abdication of the egalitarian potentiality of the non-discrimination rules. Through a critical theoretical lens, widespread growth in staffing services and corresponding triangular employment may be seen as a tool in obscuring this policy abdication from view, and in preserving the social legitimacy of the large and increasingly regressive tax subsidy favouring the remaining pension plans and participants. Similarly, the PEO concept helps preserve the legitimacy of broader policy preferences towards private, employer-based health insurance plans, which have become increasingly less egalitarian over time. Expanding regulatory accommodation by the state to the industry-generated concept of "co-employment" would seem to work to preserve this trend.

Finally, the analysis here supports the claims in literature that forms of triangular employment embody the potential for a general deregulation of employment relations broadly,[175] insofar as triangular employment growth interacts with, and erodes regulatory effects across multiple labour policy sub-fields. It does this by exploiting the available regulatory differentials dispersed throughout various

---

[173] For example, there seems to exist anecdotal evidence that triangular employment growth has also been driven by aspects of regulation of unemployment insurance and workers compensation in the U.S.. However, the author's preliminary analysis involving the role of other fields suggested that workers compensation rules have been a similar driver of triangular employment growth in Canada, and thus this subfield was not included in the comparative analysis.

[174] For the argument in favour of a finely grained analysis that takes into account of much more local, urban-based factors, see Peck and Theodore, *Temped Out*, *supra*, note 2.

[175] See Peck and Theodore, *Flexible Recession*, *supra*, note 2 and Gonos, *The Contest over 'Employer' Status*, *supra*, note 18.

labour law subfields, and the available space for accessing these advantages under prevailing employer status rules. It is hoped that this paper has provided an improved analytical foundation for the assessment and potential reversal, of some of the causes of triangular employment growth.