

Contract vs Regular Employees: An Analysis

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Abstract: Contract work is a type of employment that many organizations practice; it allows for more options to fit the needs of a firm while offering more choice in employment for workers. Management and workers have the choice between permanent internal employment and contract work. There is a lot of research regarding the rationale and nature of contractual relationships. This paper focuses specifically on the key benefits and setbacks of contract workers from both firm and worker perspectives with real life examples.

The research provides the reader with an in depth understanding of the topic and allows direct comparing and contrasting between the benefits and drawbacks of contract work. Solutions to the drawbacks are further supplemented to aid management in mitigating risks associated with contract work. This paper specifically discusses:

Employer and Employee Advantages to Contract Work with specific focus on the fiscal, flexibility of employment, time investment, and commitment and loyalty for both employers and employees.

Employer and Employee Disadvantages to Contract Work with specific focus on power discrepancy, performance, employment structure, legal issues, and organizational relationships for both employers and employees.

Potential Solutions to Drawbacks with specific focus on building relationship to increase mutual trust, integration of contract workers in company policy and culture, and restructuring the classification of employees.

To further illustrate key points discussed, examples of contract workers impact on human resource management, through analysis of Uber and Microsoft, are discussed.

Keywords: Contract work, Uber and Microsoft.

1. INTRODUCTION

As technological advances continue to grow and shape our economy, many companies and organizations are reshaping the dynamics of their workforce by employing contract employees rather than permanent employees. There are a range of benefits which are apparent for both the employer and the employee. From the employer perspective, the company can satisfy the demand of the economy and ramp up their workforce quickly and efficiently with experienced workers that fit their needs. Furthermore the employer benefits from reduced cost and savings, escaping the burden of having to pay for benefits or look after the employee's future in pension plans. From the employee perspective, workers can yield greater short term benefits in the aspect of increased hourly and overtime pay, as well as have control and autonomy of the type of work they choose to align themselves with.

However, although this relationship seems to be mutual between employer and employee, there are several underlying issues that are being overlooked; that is the effect on contract employee morale, and the effect on organizations and human resource management. Research in the field indicates that there is a status distinction between contract employees and permanent employees leading to lower performance, morale and the unexpected turnover of contractors. Furthermore, organizations are suffering from the long term ramifications of this segregation, with increased lawsuits and back pay of benefits and wages.

This paper will be focusing on the advantages and disadvantages of contract employees and its effects on employee morale, organizational performance, and impact on human resource management. Through analysis of Uber and Microsoft, real problems in external employment are identified and potential solutions are proposed.

2. LITERATURE REVIEW

Employer and Employee Advantages to Contract Work:

As organizations strive to reduce costs at all levels of operation, the driving factors for employing contract employees versus permanent employees are reduced staffing costs and economic flexibility. Organizations immediately benefit from lower training costs as contract employees are generally experienced and hired to fill a specific job or project. These employees move from project to project as they are hired “for needs in special seasons, peak-time hours, and unexpected surges or increases in demand” (Chen & Brudney, 2009) and there is marginal variance in the type of work they are asked to perform. As a result little job specific training is required. Furthermore, employers save on expenses from “fringe benefits, such as pension and health insurance” (Chen & Brudney, 2009) allowing a significant portion of capital to be utilized elsewhere.

This leads to the next benefit, economic flexibility. Since contract employees are hired for a specific job, it allows the organization to show no further obligation, commitment or loyalty to the employee once the project is complete, thereby allowing the firm to “lay off short-term direct-hire workers with little threat of litigation” (Chen & Brudney, 2009). This hiring and firing practice gives the organization huge amounts of flexibility where the firm can quickly satisfy economic demand yet not have to invest a significant amount of money in human capital.

Similarly, individuals choose contract employment to benefit from increased hourly pay, flexible hours and autonomy over one’s work. This is particularly relevant for “parents of young children, careers, students and others to fit work around their home lives or studies” (Cheese, 2013) by having a flexible schedule and hours. In regards to pay, firms “recognize that in order to make short-term or project work attractive, they must pay a premium price” (Peel & Boxall, 2005). Because of this, individuals are willing to overlook the long term benefits that come with permanent employment in job security, pension and health insurance, and opt for contract employment for increased wages in the short term. In addition, although most contract employees work in tandem with the organization for which they are hired, they are either hired on through a contracting agency (where no direct supervisor is present) or are independent. This absence of a direct supervisor allows for more control and choice over their day to day operations of tasks which have shown to be a fundamental determinant in choosing contract or self-employment (Peel & Boxall, 2005).

Employer and Employee Disadvantages to Contract Work:

Despite these advantages, the relationship between contract and permanent employment is not without flaws. One significant downside is employee segregation. Research has suggested a status or class construct within workplaces are starting to be created as a result of this type of employment, similar to those of race and gender. As the provision of resources in the form of benefits, compensation, and decision-making autonomy differs between contract and permanent employees, a difference in perceived identity also develops. This difference in identity leads to a construct of class (Boswell, Run, Triana, Umphress, Watkins, & Zardkoohi, 2012). The hierarchy of said class would then reflect the amount of resources received, resulting in various forms of organizational injustice or inequality found in other social settings.

Another disadvantage for contract employees is the perceived difference in utility or use value between a contract and permanent worker. For instance, as contract workers carry the persona of supplemental or temporary help, they do not hold the same level of solidarity within an organization. They are instead perceived to be more dispensable in comparison to permanent workers that have more opportunity and upward mobility, where their utility is often associated with managerial potential and leadership.

The theory of social categorization has also been studied to support the idea segregation within the workplace. This theory states that in-groups and out-groups are created for an individual’s recognition of his and her social surroundings based on the similarity one identifies with one’s self (Boswell, Run, Triana, Umphress, Watkins, & Zardkoohi, 2012). This perception of similarities is argued to have a similar effect within organizations based on their status as contract or

permanent employees. The damaging nature of this process is the biases placed on each group not based on observation or empirical evidence, but based solely on the perceived similarity to one's self (Boswell, Run, Triana, Umphress, Watkins, & Zardkoohi, 2012). For example, permanent workers may have a less trusting bias towards contract workers based not on these workers' actions but simply on their membership in the out-group.

Organizations are concerned with the disadvantages contract employment presents, in terms of centralization of information, employee turnover and low job performance. To begin, contract work by its nature involves inter-organizational exposure of information. The contract worker's skills set is often targeted towards a single industry or a particular department within an organization. This identifies the worker as a source of potential risk for the client firm and restricts the amount of information exposure they receive (Chen & Brudney, 2009). This can lead to centralization of information which negatively impacts dissemination of information, team building and does not foster a sense of belonging for the contract worker. Furthermore, workplace inefficiencies can arise, creating roadblocks, miscommunication and complications in worker tasks.

Another crucial disadvantage when contracting workers is the increase in unexpected turnover. Various factors contribute to this and mostly root from the negative aspects of contract work experienced by workers. According to Foote's article "Temporary workers" there are several explanations for this. The first is from inadequate socialization, which is a failure to align and connect with organizational culture due to the emphasis on task oriented training. The second aspect is exclusion from decision-making due to the limited role contract workers play within the client organization as they are often viewed as temporary supplementation. The third aspect is the lack of security once contract workers seeking permanent positions come to realize such positions are unlikely to be offered by the client organization. The fourth aspect is low tolerance for perceived inequity due to the class distinction and social categorization theory. The final contributing factor is low levels of commitment due to a feeling of expendability and overall organizational injustice (Foote, 2004).

Finally, organizations are concerned with low performance from contract workers. This has been discussed in the literature through the relative deprivation theory. This theory states that employees compare themselves to their peers when formulating a reaction to a work situation (Crosby, 1984). More specifically, the outcome they expect to receive from said situation is compared directly to the outcome their peers may receive. For instance, a worker with a certain level of education may be forced to hold a temporary contract position while his or her peer with a similar background is in a more secure permanent position. This deprivation of outcome from the investment in education may result in negative reactions to the work environment. The contract worker may then attempt to increase the equity they receive from the position by lowering their performance. This sense of fairness can contribute to an overall decrease in workforce performance (Feldman, D. C., Tunley, W. H., 2004).

Potential Solutions to Disadvantages:

Human resource management plays a key role in governing the contract versus permanent employee relationship and its effect on organizations. In order to increase performance and morale, and to reduce turnover, organizations need to show commitment to all employees. One possible solution is for management to consider the two-factor leadership model or situational leadership theory which focuses on high task and high relation orientation with the employee (Svensson, Vinberg, & Larsson, 2014). Studies show when management takes a more active role in the employee tasks with support and communication, as well as connect to their employees on a personal level, this involvement leads to higher levels of well-being, job satisfaction and job performance, while maintaining low levels of stress (Svensson, Vinberg, & Larsson, 2014). An example of this would be to have management set up weekly or monthly one on one meetings with the employee, where both parties discuss any issues or blockers that are occurring within the workplace, and what steps each can take to rectify the problem. This creates mutual trust between the parties, where both are on the same page and working towards a common goal. Furthermore, it creates a support network and personal connection with management and the employee, ultimately increasing job performance and satisfaction.

Human resource management should also look to integrate the contract employees with the organization and align individuals with company policy, procedures, and strategy. By having clearly structured onboarding and training practices, employees can feel a sense of inclusion and part of the team. Furthermore it shows the company is willing to invest in them and genuinely cares for their success at the company and not seen as "just a temp" or part of a "disposable workforce" whereby creating an environment of unfair and disrespectful treatment of employees (Feldman, 1994).

Another approach is to tackle the classification between contract employees versus permanent employees itself, by defining an intermediate class. The problem arises because employers seek to benefit from reduced employee costs as well as flexibility in hiring/firing human resources to satisfy demands of economy. Contract employees seek to benefit from autonomy and control over one's work yet still desire job security and health benefits from an organization. However, both of these options are on extreme ends of the spectrum and promotes misclassification of employees because one party wants to benefit yet see no tradeoffs in the arrangement. By creating an intermediate classification, both parties can benefit by having organizations "cover some costs (e.g., expenses) but not others (e.g., social security)" (Andrei Hagiu, 2015). This would satisfy both party's needs and "allow firms and workers to continue reaping the benefits of contracting while reducing the temptation to misclassify workers" (Bidwell & Brisboe, 2009).

3. DISCUSSION/ANALYSIS

Uber's Misclassification Case:

Uber has been in the news for their issues with contracting workers, which has left a gap between employees and employers. Uber is part of an up and coming industry called the "sharing economy". This industry consists of service companies that do not employ their providers or own the assets used to provide the service and emphasize the use of networks and sharing resources with clients. The following paragraphs will discuss Uber's misclassification lawsuits and what a similar company has done to avoid the same problems.

Current Problem:

Uber's problem with drivers stem from their misclassification of drivers as contractors when drivers feel like they are employees of the company. Uber considers itself as just a "technology platform" that connects drivers to any potential passengers, which means that drivers should be considered independent contractors because they use their own vehicles, can easily move to another company, and can set their own schedule of working. However, drivers argue how driving for Uber has left them dependent on the company to create an income, and should be given expense reimbursements and additional benefits for their work (Kokalitcheva, 2015). Therefore, when Uber changes the price of fares without discussing it with drivers, contract employees feel like they are being undermined. Recently, courts have favored for the workers, and will cost Uber hundreds of millions of dollars to compensate workers (Mendelsohn, 2016).

Potential Solutions:

Compared to Uber's difficulty with complying to their providers' needs, Airbnb is an example of the opposite. While both Uber and Airbnb share traits of providing services through an external host, the latter has been different by creating a strong community and partnership with those who provide their houses to Airbnb. One example of Airbnb building a strong community is the use of host groups or meetups between hosts and executives (Sundararajan, 2014). These meetings allow the company to align their beliefs with the hosts', share stories of past experiences, and to exchange important information. Airbnb also shows their community appeal through branding, and their priorities of making everyone involved with Airbnb feel like they belong; both as a host and as a member of the neighboring areas.

Uber should realize that the type of culture they want to create can make a big impact on worker satisfaction in their company. Workers feeling stressed that Uber executives are trying to undermine them in any way deteriorates trust in the long run. By providing a supportive company culture, Uber can assure drivers more convincingly that they care for the well being of each driver.

Microsoft's Contract Worker Policy Case:

Another example where the contract employee versus permanent employee relationship is causing issues is Microsoft. Over the course of 2014 till now, Microsoft has changed its vendor policy to force contractors to a mandatory six month break after working 18 consecutive months, limiting contractor's access to property and assets. Contracting firms are worried that large amounts of their employees that deal directly with Microsoft are going to "walk out the door" due to this change in policy (Day, 2015). Contractors believe that this policy is in place to mitigate risk of improperly categorizing employees, which Microsoft has done in the past and resulted in a \$97 million settlement. Contractors and firms believe that Microsoft has used vendors in the past to circumvent hiring regular employees. Microsoft now aims to maximize efficiency in use of external workers.

Current Problem:

Microsoft's new policy change instigated a substantial change in contracting firm's workforces. This change of status quo may also have implications on internal staff members; the policy may cause collateral damage in decreasing the number of contractor workforce which in turn will increase the workloads of internal employees. Microsoft also runs into the issue of misclassifying regular and contract employees. In the past, some managers at Microsoft have used a vendor loophole where contractors brought onto specific projects have their contracts endlessly renewed and worked as regular employees but were not eligible for the same benefits as regular employees. As with the vendor loophole, this new policy may also be exploited.

Potential Solutions:

To counter the decrease in external staff availability, managers can nurture a strong relationship with internal employees (high task and high relation) to prevent burnout as a temporary solution. To mitigate the finite supply of contract workers, managers can start by familiarizing themselves with their external employees and build relationships which can lead to advancement into internal employment. When the contract expires there should be the opportunity to hire them to be internal employees. Microsoft should also remodel the vendor policy to prevent loophole abuse. Microsoft will better alleviate risk of employee misclassification and loophole abuse by having distinctive qualities to classify regular and contract employees and clarifying the amount of managerial control over external employees.

4. CONCLUSION

Human resource management is especially important when contract employment is involved. The client organization experiences many benefits such as a decrease in cost and flexibility in employment while the external worker experiences higher wage and flexible hours. There are substantial savings because the nature of contract workers require very little training and are also not entitled to benefits such as medical and pensions. Additionally, employing external workers give organizations lots of flexibility. The client organization can outsource tasks to professionals specialized in specific fields while not having any obligations towards said individuals aside from paying a wage. This enables the client organization the ability to satisfy different workloads that may occur due to cycles or other reasons. Contract workers they are paid a premium in lieu of benefits, which may be more beneficial for certain individuals. The workers also have job autonomy; their work hours are flexible and can work without direct supervision.

Individuals need to be aware of the drawbacks associated with contract employment such as high turnover and low performance for the client organization. Likewise, the external employee experiences drawbacks such as a split sense of belonging and difficulty moving up the corporate ladder. The external employee is in a middle ground of being and not being an associate at the same time, which creates a split sense of belonging and lack of familiarity of client organization corporate culture which results in high turnover. This factor on top of difficulty securing a permanent position in the client organization results in low performance of the contract worker. The worker is more likely to burn out when they lack a relationship with the client organization manager and with the corporate culture and is likely to lose motivation of performing to full capabilities when there are no future job prospects. A potential solution to mitigating or resolving the issues that arise from contract employment is to build relationships with the workers, integrate the workers into the culture of the organization, and restructure the way employees are classified.

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