Indirect Employment: Should Lead Companies be Liable?

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Written for a Symposium of the *Comparative Labor Law & Policy Journal* on David Weil, *The Fissured Workplace* (Harvard UP, 2014)

The Fissured Workplace[1] is the most comprehensive and penetrating account to date of indirect employment – a problem plaguing labor relations and labor law throughout the world. David Weil provides a wealth of data and analysis showing how extensive this practice is in the United States. He goes on to offer several proposals to "mend the fissured workplace", based to some extent on solutions already adopted by specific employers and some State legislatures and courts. The current contribution has two aims, both complementary to (rather than critical of) Weil's book: first, to use the Israeli example as background to consider some possible paths forward, and second, to consider the possible justifications for imposing liability on "lead companies" (the ultimate clients/brands/franchisors) towards indirect employees.

The article opens by describing the phenomenon of indirect employment in Israel, where it is widespread (Part I). I then critically consider the solutions adopted in Israel so far (Part II). The article then moves to discuss some additional/alternative solutions, to a large extent in line with Weil's proposals, offering some more details on the appropriate legal structures and their justifications. I begin by clarifying the legal questions, proposing some distinctions which I find useful and necessary (Part III). I then move to address the question least developed so far in the case-law and literature, which is whether firms (or other entities) could sometimes be held directly responsible for workers employed by their subcontractors/franchisors, even if they have no direct relationship with them (part IV). The final part concludes, and adds some preliminary suggestions regarding methods, i.e. possible legal routes to establish legal responsibility by lead companies, assuming it is indeed justified.

I. Indirect Employment in Israel

As in many other countries, attempts by employers to evade responsibility have been common in Israel for many years. During the 1980s such attempts concentrated on misclassification of employees as independent contractors. After this practice was curtailed to a large extent by the labor courts, employers shifted their focus to another legal method of evasion: indirect employment. At first, during the 1990s and early 2000s, employment through temporary

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[1] DAVID WEIL, THE FISSURED WORKPLACE: WHY WORK BECAME SO BAD FOR SO MANY AND WHAT CAN BE DONE TO IMPROVE IT (2014).

employment agencies (TEAs) became extremely prevalent. Employers subject to collective agreements used this method to lower costs and gain more flexibility by avoiding the job security, higher wages and other benefits secured by unions representing the "internal" workers.[2] Public sector employers used the same method also to avoid the limitations set by budget laws on the number of workers per each governmental unit. The *Histadrut*, Israel's major union, did not object (at least not strongly enough), neglecting the interests of new workers to protect the veteran insiders. At its peak, in 2000, employment through TEAs reached a staggering 5.8% of employees in the Israeli labor market, the large majority of them employed for long (usually indefinite) periods.[3]

In 2000 two parallel developments started to reverse the trend. First, the National Labor Court decided that a secretary employed by a governmental office through changing TEAs for many years was in fact a government employee. Second, the legislature adopted two limitations on employment through TEAs, both designed to limit this practice to short-term engagements only. According to the new law, those working through TEAs are entitled to equality in work conditions with direct employees working at the same establishment, including rights secured through collective agreements; and in case of employment through a TEA for a period longer than nine months for the same client/user, the worker will automatically become an employee of the client/user.

Although the new laws were in principle dramatic, in practice they led to a gradual shift rather than a quick transformation. The National Labor Court judgment was based on an extreme case and did not develop clear rules for less extreme situations, leaving much in doubt. The right to equal terms included in the legislation had some exceptions attached to it; most notably, there was an option to derogate from this right in a sector-wide collective agreement, which was quickly achieved between an organization of TEAs and the *Histadrut*, creating only little value to the workers involved. Finally and most crucially, the limitation of nine months was delayed repeatedly by budget laws which year after year postponed the entry into force of this provision. The government, as the biggest employer using TEAs for long-term employment, was fearful of the impact of this provision on itself as an employer. Only in 2008, after intense public pressure, the provision finally came into force – resulting in an abrupt, drastic decline in this practice.[4]

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2 On the meagre salaries of TEA workers, see Ronit Nadiv, *Licensed Temporary Employment Agencies in Israel* (Ministry of Industry, Commerce and Employment, 2005) [Hebrew].

3 Ronit Nadiv, *Employment Through Temporary Employment Agencies* (Ministry of Labor, 2003) [Hebrew]. For a discussion of this practice in historical context see GUY MUNDLAK, FADING CORPORATISM: ISRAEL'S LABOR LAW AND INDUSTRIAL RELATIONS IN TRANSITION, Ch. 7 (2007).

4 The government, which used to be the biggest employer through TEAs, now employs only a negligible number of workers this way; see Ori Tal-Sapiro, *Data on Temporary Employment Agency Workers, Service Contractor Workers, and "Shoulder-by-Shoulder" Workers in Government Services* (Knesset Research Unit, February 2014) [Hebrew]. Overall, in 2012 app. 1.6% of Israeli employees have been employed through TEAs; see the Central Bureau of Statistics data at http://www.cbs.gov.il/publications15/1565/pdf/t02_48.pdf.

Jobs previously contracted through TEAs for the most part did not become direct employment jobs. Rather, employers who started with independent contractor misclassification (in the 1980s) and shifted into indirect employment through TEAs (in the 1990s), now turned to another evasion technique: indirect employment through subcontractors. This shift started gradually in the early 2000s and since 2008 has almost completely replaced the previous two methods.

The two sectors that received most attention in the Israeli public discourse in this regard are cleaning and security services. Virtually all the major establishments in Israel – both public and private – no longer employ cleaning and security staff directly. They engage with contractors to provide these tasks. In practice, when the contractors change from time to time, the new contractor usually takes the employees of its predecessor, so the workers who clean and guard the workplace are often the same people even after a change of contractors. Solutions adopted in Israeli law (discussed in the next part) have mostly revolved around these sectors, who at least until recently have been notorious for repeated labor law violations.

However there is recently growing awareness to the fact that outsourcing to contractors has become widespread in many other sectors as well. In the public sector the leading (although not exclusive) examples are social workers and teachers. Many social services have been outsourced by the State to private (often not-for-profit) organizations, who are mostly funded by the State and provide these services on its behalf. As a result, numerous social workers are now employed by small organizations that are not subject to collective agreements, instead of being State employees.[5] It appears that this was one of the main reasons for the choice to outsource these services. As for teachers, as a result of budgetary cuts many public schools are unable to offer the level of education they aspire to without support from private (often non-profit) organizations as well as parents. As a result, some of the teachers are now employed by the supporting organizations or by parents' associations. This is especially the case with those teaching non-mandatory classes such as art, music or "enrichment programs" but also sometimes true for core-topic teachers, for example when the school needs extra staff to offer smaller classes or to help children with special needs.[6] Here as well, at least some of the supporting organizations now employing teachers are funded to a large extent by the State, suggesting that the shift to indirect employment is seen by the State as an advantage of the current system and one of its goals.

Another major example of employment through contractors, which is common in both the public and private sectors, concerns computer/programming/information technology services. Banks, for example, need thousands of workers for IT related tasks, but in Israel for the most part they

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5 Amir Paz-Fuchs & Inbal Shlosberg, *Social Workers in an Era of Privatization,* 90 SOCIAL SECURITY 257 (2012) [Hebrew].

6 Guy Davidov, *Workers Through Subcontractors in Schools*, in PRIVATIZATION AND COMMERCIALIZATION IN STATE EDUCATION IN ISRAEL (Orit Ichilov ed., 2010) 145-173 [Hebrew]; *Report by the Ministry of Education Internal Committee to Examine the Employment of Teaching Staff through Contractors* (December 2011) [Hebrew]; Yuval Wergen, *Employment of Teachers in the Education System: The Phenomenon of Teachers Employed Through Intermediaries* (Knesset Research Unit, December 2011 [Hebrew]; The State Comptroller of Israel, *Annual Report for 2014* (published May 2015) at 907 [Hebrew].

employ them indirectly, through IT contractors – even when they work only for the Bank, were hired specifically to do the work for the Bank, and at least to some extent work under the control of Bank officials. Governmental departments similarly prefer to employ IT staff indirectly.[7] In this area as well, indirect employment is found mostly in unionized settings – the Banks, for example, are all unionized – and it is used to avoid the costs and inflexibility of collective agreements. The unions often prefer not to object, at least not strongly. The workers are the ones who pay the price, with lower salaries, less benefits (compared to their peers who are employed directly), and no job security.

In the private sector indirect employment is also widespread in agriculture and construction, where workers are non-unionized and especially vulnerable. Numerous cases of regional labor courts expose the practice of employing Palestinian workers (from the occupied territories) through Palestinian contractors, and migrant workers through the agencies that facilitate the process of getting a license to employ them in Israel. In these cases the incentive is not to avoid the benefits secured in collective agreements, but apparently the subcontractors are used in an attempt to distance the user from repeated violations of labor and employment laws.[8]

II. Solutions Adopted in Israeli Law

The first legal response to the proliferation of indirect employment appeared in the Employment through Temporary Employment Agencies Act of 1996. The Act was adopted as a result of pressure from the *Histadrut* and its main response to the problem was to encourage collective bargaining with TEAs – this was the preferred method to improve the work conditions of workers employed in this structure. In practice this proved to be a complete failure, and in 2000 the Act was amended to include the two solutions mentioned above – equity with workers of the user, and a nine-month limitation (which was delayed until 2008). As noted, it was the last solution – which included an automatic switch into becoming an employee of the user after nine months – that eventually worked. Decisions of the National Labor Court placing responsibility on the user enterprise in several cases between 2000 and 2008 also helped, although they did not set clear rules, so many employers continued to enjoy the ambiguity (relying on the fact that most workers never sue).

The problem of sham outsourcing to subcontractors (as oppose to TEAs) has not been addressed by legislation. It did reach the courts several times, with mixed results. Mostly the suits were

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7 Michal Tabibian Mizrachi, *Employment of Contract Workers and Outside Service Providers by Government Ministries* (Knesset Research Unit, July 2007) [Hebrew]. And see LA 6818-10-10 *National Insurance Institute v. Dayan*, judgment of April 24, 2012 (National Labor Court); LA 478/09 *Itchak Hassidim v. The Jerusalem Municipality*, judgment of Nov. 13, 2011 (National Labor Court).

8 Labor courts usually reject such attempts and conclude that the user of the work is the legal employer or a joint employer. See, e.g., LC 49361-06-11 *Zaal Zin Alladin v. Amos Ozeri*, judgment of Oct. 1, 2013 (Jerusalem Regional Labor Court); LC 7068-09-10 *Ali Daabucki v. Y.B. Yuval Binuy*, judgment of July 7, 2013 (Jerusalem Regional Labor Court).

against the State – to be recognized as a State employee. For example, when the Ministry of Education employed through contractors an entire division of workers supervising security arrangements in school trips, the National Labor Court refused to look beyond the formal arrangements – even though in practice the workers were entirely integrated within the Ministry.[9] In contrast, when the same Ministry decided to employ indirectly a division of instructors teaching road safety at schools, the Court intervened, ruling that the State was in fact the legal employer.[10] A third alternative was also developed: when the Ministry of Agriculture shifted its entire research division to a contractor, except for the head of the division who remained a Ministry employee, the Court refused to consider the State a "full" employer, but nonetheless decided that it must guarantee the payment of minimum terms by the contractor.[11]

In all three examples – and several others that reached the courts – the contractor was little more than a funnel for the transfer of wages. Several contractors have changed but the same workers remained, supervised by State employees. The tests developed by the National Labor Court to decide "who is the employer" appear to lead more strongly to a conclusion that the "client" is the employer (or at least a joint employer). However these tests leave a broad margin of discretion so it was not inconceivable for the Court to reach the opposite result. The varying results can be explained by differences of opinions between judges, and perhaps (implicitly) by the differences in the level of wages and conditions: the closer the terms to those enjoyed by State employees, the less the courts feel necessary to intervene (although formally this is not one of the factors included in the tests).

Two specific sectors which attracted much regulatory attention are, as noted above, cleaning and security.[12] Despite the ubiquity of indirect employment in these sectors, very few workers have challenged this structure. In the rare occasions when a cleaning or security worker has tried to sue the client/user, this has usually failed,[13] with the exception of an extreme case of abuse of rights which the client had to know about (and in fact triggered, with its pressure on the contractor to lower costs).[14] However through individual suits against contractors, reports by NGOs, investigative reports in the media and demonstrations by student groups, it became clear to the public that workers in these sectors suffer from continuous violations of labor laws. A coalition of NGOs and activists which organized together under the heading "The Direct Employment Coalition" gave a significant boost to public pressure against these violations. The social protests that erupted in the summer of 2011 against a variety of social causes have also helped to solidify the public outrage against the situation of cleaners and security workers.

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9 LA 116/03 *The Ministry of Education v. Moshe Chagabi*, judgment of June 2, 2006 (National Labor Court).

10 LA 602/09 *The Ministry of Education v. Hanna Aloni*, judgment of Jan. 24, 2012 (National Labor Court).

11 LA 273/03 *Dovrat Shwab v. The State of Israel*, judgment of Nov. 2, 2006 (National Labor Court).

12 This part is based on Guy Davidov, *Special Protection for Cleaners: A Case of Justified Selectivity?*, 36 COMPARATIVE LABOR LAW AND POLICY JOURNAL 219-239 (2015) and reproduces some parts from there.

13 For a recent example see LC 10632/09 *Klodet Tsagir v. Bank Leumi* (judgment of Apr. 7, 2014, Tel-Aviv Regional Labor Court) (a person who cleaned a branch of the Bank for 17 years, formally employed through a number of contractors that changed from time to time, was rules *not* to be an employee of the Bank).

14 LC 3054/04 *Shmuelov Ayelet v. Moshe Pones*, judgment of Dec. 10, 2006 (Tel-Aviv Regional Labor Court).

Measures designed to protect these vulnerable workers first appeared in 2007, when the Israeli Accountant General issued Guidelines directed at government offices and agencies, which included a detailed calculation of the minimum cost of employing a worker in the cleaning and security sectors. The Guidelines prohibited any contract with a cleaning or security contractor based on a lower hourly sum. These new rules succeeded in revolutionizing the process of choosing contractors by government units, as well as other public sector employers (such as Universities, who adopted these rules voluntarily). Instead of looking for the cheapest offer (with tenders setting a *maximum* price), the clients/users now refuse to accept offers that are "too good to be true" (setting in their tenders a *minimum* price). By requiring the Government, in practice, to pay much more for its contractors, the Guidelines minimized the incentive for labor laws' violations. In addition they prohibited engagement with cleaning and security contractors known as "repeat offenders" of employment laws.[15]

The efforts to protect cleaning and security workers took a big step further in 2011, when the Act to Improve the Enforcement of Labor Law was enacted. A significant part of the Act is dedicated to cleaning and security workers employed indirectly.[16] The idea is to create incentives for the clients/users to make sure that cleaning and security contractors working with them are complying with employment laws. This is achieved by placing direct responsibility on the clients – not as employers but as guarantors – in cases of non-compliance by the contractor itself. So, if the worker is not getting overtime payments required by law (for example), and a demand issued to the contractor did not yield results, the worker has an option to sue the client directly for the same amount.[17]

The Act further lists a number of conditions leading to liability or exemption from liability of the client. *First*, the client must take reasonable steps to prevent any infringement of workers' rights by the contractor, including by setting a procedure for the workers to complain (complaints submitted to the client against the contractor). If such a procedure is not established, or is not made known to the workers, the client will be liable for any infringement of rights, even if the worker did not issue a demand to the contractor. *Second*, the client will be exempted from liability if it hires a "certified wage-checker" to perform periodical checks, and acts swiftly if violations are found.[18] *Third*, the client will be automatically liable if it does not pay the contractor per-hour compensation that exceeds the minimum required by the Act – a calculation

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15 The Guidelines prevented engagement with contractors that have been criminally convicted in a labor law offence in the past three years, or have been administratively fined twice or more during the same period.

16 The list of sectors relevant to many of the Act's new measures is included in an Appendix to the Act: cleaning, security, and catering (food) services offered to workers of the client (i.e. workers of a cafeteria inside a workplace). The last group is less significant and has not attracted much attention or discussion thus far. The Minister of Economy was given the power the change the sectors in the Appendix, subject to some conditions.

17 Article 25 of the Act.

18 The idea has some historical foundations, and proposals to resurrect it have been raised in the United States as well; see (on both points) Matthew W. Finkin, *From Weight Checking to Wage Checking: Arming Workers to Combat Wage Theft*, 90 INDIANA L.J. 851 (2015).

based on the minimum wage plus the cost of all other mandatory employment standards plus some minimal profit (i.e. no "losing contracts").[19]

The duty to take "reasonable steps" to ensure that the workers' rights are respected might not seem so important. Unlike the other two duties (to hire a wage-checker and to pay more than the minimum required) it does not entail direct costs. Nonetheless, it has crucial implications. In the past, clients/users have been very hesitant about showing interest in the rights of workers employed indirectly, out of fear that any direct contact will be used as an indicator of direct employment relations. The Act not only gives clients positive incentives to care about the cleaners/security workers, it also eliminates the negative incentives. If you have direct contact with the workers in order to make sure that their rights are not infringed, there is no reason to suspect that courts will view this as a relevant indicator of employment any longer, because it was required by the Act.

Overall the Act creates a significant bundle of unique regulations, specific for cleaning and security workers employed by contractors. The goal of these regulations is not to create a separate legal regime for cleaners and guards in terms of the substantive rights they enjoy, but rather to ensure that they are able to enjoy the universal employment rights in practice. Given a reality of poor compliance, bolstered by a problematic incentive structure, there were good reasons to create regulations designed specifically to overcome the cleaning and security sectors' problems.

At the same time, however, there is a cost to the solution chosen. While it has good potential to improve compliance with employment standards for cleaners and guards, it is also likely to perpetuate their inferior position. Although it is stipulated in the Act that it does not create direct employment relations nor refutes the existence of such relations,[20] in practice it is obviously based on the premise that indirect employment through contractors is legitimate and offers solutions within this structure. Moreover, by placing a duty on clients to care about cleaners and security workers, the Act has blurred the lines between direct and indirect employment, making it more difficult to place direct employer duties on clients. Overall, the Act is likely to lower the chances of labor courts concluding that a cleaning/security worker is in fact legally employed by the user enterprise.[21]

The expected improvement in terms of compliance did not satisfy the *Histadrut*. The public perception was that the work conditions of cleaners and security workers are unfair. In February

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19 The Act goes on to place criminal liability on the client for such "losing contracts" (Article 31). Furthermore, there is criminal liability on the client's managers for the same offence (Article 32); criminal liability on the client for not taking every reasonable step to prevent violations by the contractor (Article 33); and criminal liability on government officials responsible for relations with contractors for the same offence (Article 37). On the phenomenon of losing contracts see also Weil, *supra* note 1, at 137.

20 Article 46.

21 I discuss this at more length in Guy Davidov, *The Enforcement Crisis in Labour Law and the Fallacy of Voluntarist Solutions*, 26 INT'L J. OF COMP. LAB. LAW AND IND. REL. 61 (2010).

2012 the *Histadrut* called a general State-wide strike against the government's frequent resort to indirect employment ("contract work" is the common term in Israeli non-legal discourse).[22] After a five-day strike backed by broad public support, the government and the *Histadrut* reached an agreement on higher wages and new benefits for cleaning and security workers.[23] This was a significant development: for the first time the government agreed, under pressure, to sign a collective agreement with the *Histadrut* that does not concern government employees, but rather the employees of contractors engaged by the government. Given that the *Histadrut* has no formal status as the legal representative of the various contractors' employees, this was unusual and even questionable legally. However, this perhaps parallels the questionable employment of all cleaning and security workers through subcontractors, rather than directly.

The 2012 agreement sets the wages of cleaners and security workers at 8% above the minimum wage. Moreover, it was agreed that some of the workers will be entitled to merit bonuses, based on selection criteria decided by the government (and not by the contractor); those who have a supervisory role will receive a higher wage, set in the agreement; the employers' contributions to the employees' pension fund will be higher than the minimum required by law; workers will have a right to a new saving fund (commonly available in Israel for unionized employees) which requires the employer to pay an extra 7.5% of their salary into the fund; as well as some additional benefits. It was further agreed that in the future, any wage increase agreed between the parties for government employees shall apply to the cleaning and security "contract workers" as well.

The *Histadrut* also demanded, and the government agreed, to use legislation to extend these obligations to the entire public sector (including local municipalities, universities, hospitals, government-owned companied, and numerous other organizations wholly or partially funded by the government). On August 2013 the Knesset accordingly adopted the Act concerning Workers Employed by Cleaning and Security Service Contractors in Public Entities. According to this Act, all public entities (as broadly defined in the Act) must include in their agreements with cleaning and security contractors a stipulation that the wages and benefits as agreed in the 2012 collective agreement shall apply. This agreement with the government and the ensuing legislation have eventually led to collective agreements between the *Histadrut* and the employers' organizations in the cleaning and security sectors, applying similar terms on workers employed in the private sector as well.

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22 Haim Bior, *Israeli Workers Open General Strike, Disrupting Airport and Economy*, HAARETZ (February 8, 2012) available at: www.haaretz.com/news/national/israeli-workers-open-general-strike-disrupting-airport-and-economy-1.411688; Shai Niv, The General Strike is Over, GLOBES (February 12, 2012) available at: www.globes.co.il/news/article.aspx?did=1000723734 [Hebrew].

23 See Memorandum of Understanding dated Feb. 12, 2012, and a collective agreement between the Government of Israel and the Histadrut dated Dec. 4, 2012. For a detailed account of these developments see also Guy Mundlak, *Contradictions In Liberal Reforms: The Labor Regulation of Sub-Contracting* (forthcoming).

The end result of these developments is that cleaners and security workers employed indirectly are now able to enjoy wages and benefits somewhat above the minimum set by employment laws. The interesting story is about the way this has unfolded. The contractors are not against better terms and conditions for their workers, as long as they are paid on a "cost plus" basis, which is indeed the norm in these sectors. If the clients agree to pay more so that the workers will get more, there is no reason for the contractors to object. However the contractors were not in a position to impose higher payments on their clients – especially the major public sector clients, who are constantly under pressure to cut costs. Moreover, the *Histadrut* had little bargaining power to impose an agreement on the contractors, given that the cleaners and security workers are highly dispersed and mostly non-unionized.

The only way to change this difficult situation was through pressure on the clients, and specifically the biggest and most powerful client – the government. A general strike called when public opinion was favorable forced the government to agree to pay more to its contractors for the benefit of cleaners and guards. The agreement was then extended by way of legislation (which the government was obligated to draft and support, according to its agreement with the *Histadrut*) to the broader public sector. This was crucial: there was no other practical way to reach the numerous workers cleaning and guarding hospitals, universities, municipalities, schools and so on, all over the country. Once it was made clear that the legislation will make the higher wages and benefits a new standard in these sectors, it became possible to reach collective agreements with the contractors themselves, thus extending similar terms to the private sector.

III. Clarifying the Legal Questions and Distinctions

Having described the problems of indirect employment in Israel and the attempts to solve them, I now move to consider the general questions raised by these problems. Weil distinguishes between three kinds of indirect ("fissured" in his terms) employment: subcontracting, franchising, and supply chains. He mentions very briefly the use of TEAs as well. In legal terms, all four models represent similar difficulties: they are legitimate in principle (so there is no reason to prohibit them outright) but can lead to deterioration in workers' rights. This raises two crucial questions: first, in what circumstances is it justified to place responsibility on the client/brand/user, alongside or instead of the direct employer? A related question is what level of responsibility is justified: full (as a legal employer) or just residual/subsidiary (guarantee for minimum standards in case the direct employer fails to obey them). Second, assuming some responsibility is warranted, what are the legal techniques that can be used to achieve it? I do not attempt to provide full answers to these questions here. My goal in this part is to elucidate the questions and put forward some possible solutions, using the Israeli experience as background.

Thinking through the lens of the first (normative) question, there is a basic distinction between intentional abuses of the legal model, using it as a fictional structure to disguise a direct work

relationship, versus situations in which the deterioration in workers' rights is an indirect effect of an otherwise legitimate business arrangement, when the client/brand has no direct relations with the workers. Consider, for example, a secretary working for many years at a governmental office, side by side with government employees as part of the regular hierarchical structure of the workplace, but formally considered an employee of a TEA.[24] This is (or at least should be) an easy case; the attempt to portray the TEA as an employer is fictitious and should be ignored. Employers cannot be allowed to escape responsibility simply by giving the title of an employer (and nothing more) to another entity. Consider in contrast an agreement between McDonald's and another company that allows the latter to open a restaurant as a franchisee of the former, using the brand name but operating the place independently and having sole control over the employees. In such cases, one might still argue that McDonald's should bear some responsibility for the workers. However it is clear that there is a business reason for the franchising agreement which is unrelated to workers' rights. So the structure is not fictitious and the justification for imposing responsibility on McDonald's (if at all) would be different.

There are also some variations in between the two scenarios depicted above. Consider, for example, the delivery of cleaning services. Assume that a Bank contracts with a cleaning contractor to provide this service at one of its branches. In practice, a single specific employee is cleaning the establishment, on a full time basis, for many years. She is getting direct instructions from the bank employees. This is very close to the fictitious relations of long-term employment through a TEA.[25] In contrast, imagine that a University contracts with a cleaning contractor to deliver a clean campus in return for a lump sum, without having any control (or knowledge) of the workers who actually do the cleaning work – the contractor has sole discretion (real and not only contractual) on the number of workers and their identity, and the contractor is the only one supervising them. Such a scenario is closer to the franchising example above; the responsibility of the University, if at all justified, would have to rely on a different reasoning.

For legal purposes it is useful to maintain a number of distinctions, which could best be clarified by setting forth several scenarios. Assume a triangular work relationship that includes a worker, entity A enjoying her work, and entity B that is presented as the legal employer. B could be a TEA or a subcontractor. Assume also a franchise arrangement that includes a worker, entity A as the franchisor/brand, and entity B that is the direct employer. And finally, assume a supply/production chain that includes a worker, A as the lead company/brand, B as a subcontractor that contracts with C that in turn contracts with D that is the direct employer.

When considering legal responsibility, we should start by asking: who has the characteristics of an employer? That is, which entity has, vis-à-vis the worker, the characteristics that justify the application of labor laws? In my own view, the characteristics are democratic deficits

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24 LA 1189/00 *Ilana Levinger v. The State of Israel*, judgment of Oct. 2, 2000 (National Labor Court).

25 The Tel-Aviv Regional Labor Court thought otherwise; see the recent case of Tsagir, *supra* note 13. But see in contrast the case of Shmuelov, *supra* note 14.

(subordination, broadly conceived) and dependency – but other tests can be inserted here as well. There are three possible answers when asking who has the employer characteristics:

1. If the answer is A – i.e. if all (or almost all) the characteristics of an employer lie with A, even though another entity is presented as a legal employer – then this is a sham arrangement. In such cases we should ignore the sham and place full employer responsibility on A. Usually sham arrangements are found in triangular scenarios involving TEAs or subcontractors, but it is not impossible that franchising and supply chain arrangements will be abused in this way as well. Ignoring (looking beyond) sham arrangements is indeed the law in many countries,[26] although in practice this rule is often not applied, at least not consistently.[27]

2. If the characteristics of an employer are shared by two or more entities, we have four options in terms of ascribing responsibility:

   (a) Decide that one of them is the only legal employer, e.g. always the user, or always the TEA/subcontractor;

   (b) Divide the responsibilities of an employer between them, e.g. for purposes of the minimum wage law A would be the employer, for purposes of a working hours law B would have to assume responsibility;

   (c) Place joint responsibility on both/all of them, i.e. both/all will be jointly and severally liable as if they are the employer for all purposes (and the worker will have all the rights enjoyed by employees of A as well);

   (d) Place full responsibility on the direct employer and residual responsibility (sometime called subsidiary responsibility) on the other(s), i.e. A will have to guarantee the payments by B (or D) to the worker, if these were not paid, but the worker will not enjoy the same rights as A's employees.

   It is possible to find examples in the laws of different legal systems to all four solutions, although probably the most common result is simply to leave the responsibility with the entity that was designated as the employer by the formal contractual arrangements. This is unfortunate, because it legitimizes a system by which A evades responsibility, and the

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[26] See ILO Recommendation R198: Employment Relationship Recommendation (Recommendation Concerning the Employment Relationship) (95th ILC Session Geneva 15 June 2006) (ILO 2006) art. 9; ILO, Regulating the Employment Relationship in Europe: A guide to Recommendation No. 198 (March 2013) 33.

[27] See, e.g., A.C.L. Davies, *Sensible Thinking about Sham Transactions: Protectacoat Firthglow Ltd v Szilagy*, 38 INDUS. L.J. 318 (2009); Alan L. Bogg, *Sham Self-Employment in the Supreme Court*, 41 INDUS. L.J. 328 (2012).

rights of the workers are harmed. I have argued elsewhere that the best solution is (c) above, i.e. placing full responsibility on both A and B (or D) as "joint employers".[28]

3. Assuming that the direct employer (B or D) has all the characteristics of an employer, the question becomes: is it still justified to hold A legally responsible for the workers in some sense? This should be examined separately because absent a direct relationship in the sense of having at least *some* employer characteristics, it is not possible to place *full* employer responsibility on A. The relationship between McDonald's and workers of a franchisee, or Nike and workers at the end of a production chain (for example), cannot be likened to direct employment. Given the distance between such lead companies and the workers, they cannot be expected to take responsibility for working hours, privacy violations, sexual harassment, unfair dismissals and so on. Indeed, I am not aware of anyone who argues that franchising or supply chain arrangements should be "flattened"/ignored in the sense that A will be considered the employer of workers directly employed by B or D *for all intents and purposes*. The question is rather whether there should be some *specific* liability on lead companies, which is less than full employer liability. I discuss the question of whether such liability is justified in the next part. If indeed such specific liability is agreed upon, there is no reason to attach the title of "employer" to it. Admittedly, it is not impossible; titles do not matter so much, and in principle one can be an "employer" even with only partial liability. But the distance dictates many differences from direct employment, so using the same title will only create confusion.

IV. Lead Companies Responsibility – Justifications

The goal of this part is to consider whether (and when) there is normative justification to hold lead companies responsible for workers of their subcontractors/franchisees, in situations of "real" (rather than sham) subcontracting and franchising. Given the discussion in the previous part, the examination is based on the understanding that such liability, if at all justified, could at most be residual. Several possible justifications should be considered: first, that the lead company has *caused* the infringement of employment rights by the direct employer; second, that the lead company has the *power to prevent* such infringements, and if the harm (infringement) has occurred, to *spread the loss* among many clients/consumers; third, the lead company can be said to be responsible because it is *benefiting* from the infringement of employment rights; fourth, it could be argued that it has implicitly assumed such responsibility through *representations* to consumers or workers; and finally, if we believe in *citizenship at work*, arguably an entity must bear responsibility for those working within its community. I discuss each of these potential

[28] Guy Davidov, *Joint Employers Status in Triangular Employment Relationships*, 42 BRITISH JOURNAL OF INDUSTRIAL RELATIONS 727 (2004); and see more fully GUY DAVIDOV, A PURPOSIVE APPROACH TO LABOUR LAW Ch. 6 (forthcoming OUP).

justifications in turn, before moving to consider also the main critique/contradictory argument: the risk of *inefficiency*.

The list of possible justifications considered here is quite similar to the one developed by philosophers David Miller and Christian Barry,[29] and imported to the labor law context by Yossi Dahan, Hanna Lerner & Faina Milman-Sivan.[30] According to Miller, when asking which agent should bear responsibility to "put a bad situation right", four principles should be considered: causal responsibility, moral responsibility, capacity (to rectify the situation) and community (whether you and the harmed individual are part of some shared community). He concludes that none of these is necessarily determinative or sufficient in itself, but they are all relevant. Barry's articulation, adopted by Dahan et al., is similarly based on four principles: contribution (similar to causal responsibility), beneficiary (mirrors in many ways moral responsibility in Miller's discussion), connectedness (equal to community) and capacity. My discussion below covers the same justifications, adding a fifth one (representation) and another supporting argument (loss spreading), but uses somewhat different titles that I think better capture the crux of the normative claims. There are two additional (and more significant) differences from the previous contributions mentioned above. First, the discussion below is not general and philosophical but rather engages in more concrete and detailed terms with the problem of indirect employment and the potential for legal (rather than moral) liability – including an attempt to demarcate lines setting the limits of such liability. Second, the possible justifications are examined here in detail and critically, and adopted only partially; I argue that they are sufficiently convincing only in specific contexts, and reject the claim that they can justify the imposition of overarching liability on lead companies.

1. Causation

The principles of tort law conveniently encapsulate the moral standards concerning causation, telling us when one should be considered responsible for an action because of causing it.[31] Although I am not asking here whether the lead company should be liable in tort law, but rather more generally whether a new legal rule should be created to hold the lead company responsible, tort principles are helpful because they represent acceptable societal standards that are based on

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29 David Miller, *Distributing Responsibilities*, 9 J. OF POLITICAL PHILOSOPHY 453 (2001); Christian Barry, *Global Justice: Aims, Arrangements, and Responsibilities*, in CAN INSTITUTIONS HAVE RESPONSIBILITIES? COLLECTIVE MORAL AGENCY AND INTERNATIONAL RELATIONS (Toni Erskine ed., 2003) 218.

30 Yossi Dahan, Hanna Lerner & Faina Milman-Sivan, *Global Justice, Labor Standards and Responsibility*, 12 THEORETICAL INQUIRIES IN LAW 117 (2011); Yossi Dahan, Hanna Lerner & Faina Milman-Sivan, *Shared Responsibility and the International Labour Organization*, 34 MICH. J. INT'L L. 675 (2013).

31 For previous contributions relying on tort law to examine lead company liability, see Brishen Rogers, *Towards Third-Party Liability for Wage Theft*, 31 BERKELEY J. EMPL. & LAB. L. 1 (2010); Debra Cohen Maiyanov, *Sweatshop Liability: Corporate Codes of Conduct and the Governance of Labor Standards in the International Supply Chain*, 14 LEWIS & CLARK L. REV. 397 (2010); Radu Mares, *Responsibility to Respect: Why the Core Company Should Act When Affiliates Infringe Human Rights*, in THE UN GUIDING PRINCIPLES ON BUSINESS AND HUMAN RIGHTS – FOUNDATIONS AND IMPLEMENTATION 169 (Radu Mares ed., 2012).

normative justifications of deterrence (preventing harm), corrective justice and to some extent also distributive justice (mostly in the sense of spreading the loss).

The most relevant principles are those dealing with negligence. Briefly put, one is liable for damages if (a) the harm would not have occurred "but for" his/her act, and (b) the harm was a foreseeable consequence of the act. This is examined not only subjectively but also objectively – whether a reasonable person *should have* foreseen the harm. When considering responsibility for omissions rather than acts, some special connection between the parties is also required, i.e. people are not generally expected to actively help others and save them from harm, unless there is some previous relationship that the law sees as requiring such action (e.g. physician-patient or employer-employee).[32]

Two additional tort law doctrines are used to limit liability for harm-doers. First, in many legal systems there is a requirement of some proximity between the parties to create liability – which together with foreseeability is seen as creating a "duty of care". However such proximity is usually conceptual rather than physical or contractual – and determined based on public policy considerations.[33] So it is doubtful if it adds additional constraints in the current analysis. In any case it is usually understood to require a very minimal level of relations, much less than the special relationship required to create liability for omissions. Second, there is often a rule excluding liability for "pure economic harm", i.e. economic harm that is not attached to any harm to body or property. However the main reason behind this doctrine is not relevant in the current context. The fear is of over-deterrence and indeterminate infinite liability; many of our daily actions could cause harms to someone indirectly.[34] However this is not a problem when considering the adoption of a specific rule for specific circumstances. Indeed, many exceptions to the rule have been adopted over the years. The discussion here can be understood as an examination of whether it is justified to adopt another exception.

I will focus, then, on the "but-for" and foreseeability requirements. How are these principles applied in our context? Consider first the scenario of simple subcontracting: A contracts with B to provide a service or produce a product. The work is performed by B's employees. The starting assumption for this part is that the arrangement is not a sham; B has the characteristics of an employer and not A. Now we learn that B violates labor laws, for example, pays the employees less than the minimum wage. Are there any circumstances in which it could be said that the harm *would not have occurred but for* A's actions, and also that it is foreseeable? This seems be the case only in very specific situations. Thus, for example, imagine that A triggered the illegal

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32 See, e.g., SIMON DEAKIN, ANGUS JOHNSTON & BASIL MARKESINIS, TORT LAW, 7th Ed. (Oxford: Clarendon Press 2013) 178.

33 There is an ongoing debate about whether there is a general duty of care, and whether the concept still has, and should have, any useful meaning. See, e.g., John C. P. Goldberg & Benjamin C. Zipursky, *The Restatement (Third) and the Place of Duty in Negligence Law*, 54 VAND. L. REV. 657 (2001); W. Jonathan Cardi & Michael D. Green, *Duty Wars*, 81 S. CAL. L. REV. 671 (2008).

34 See, e.g., Dan B. Dobbs, *An Introduction to Non-Statutory Economic Loss Claims*, 48 ARIZ. L. REV. 713 (2006).

behavior by aggressive market behavior, i.e. pressured subcontractors to lower prices to the point of per-hour payment lower than the minimum wage (a "losing contract"); and also, B is not known to regularly violate labor laws (i.e. we cannot say that B would have violated anyway); the employees in question work only or mostly for A and not for other clients; and the payment is based on hourly compensation, which allows A to compare this payment with the minimum wage, or otherwise A has enough information to make this calculation. When all of these facts converge, we can see a direct connection between A's actions and the labor law violations, and since A had to know in this situation that this will very likely lead to labor law violations, it would be justified to hold A responsible according to tort law principles. This is not an unrealistic scenario; in Israel, it was quite often found, until a few years ago, in the cleaning sector. However it is not very common either.

Another example of causation is when A uses its influence/power over B to directly encourage/pressure labor law violations. Imagine that McDonald's has an anti-union policy, and it directs the franchisees operating its restaurants to prevent organizing at any cost, even by illegal methods. If freedom of association rights are infringed, the direct culprit may be the franchisee, but causation between the actions of McDonald's and the violation of labor laws is quite obvious.[35]

What about omissions, as opposed to acts?[36] While there is only a narrow set of cases in which A's actions could be said to have actively caused the harm, there is a much larger set of cases in which A could have prevented the harm but refrained from doing so. There are many things A can do to prevent labor law violations by B: choose reliable contractors; pay more; include provisions in the contract demanding adherence to labor laws and insisting on a right to monitor; enforcing this agreement and monitoring. But is it justified to legally require such actions? If we rely on tort law principles, such liability for omissions can be justified only if there is a special relationship between A and B's employees that creates a duty of the former to the latter.[37] It would be difficult to argue that such a duty exists in general. But arguably it arises in some situations, for example when the employees physically work in A's place of business and are in a sense part of the same community together with A's employees. I refer to this situation in section 5 below.

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35 In the US the National Labor Relations Board (NLRB) has recently issued complaints against McDonald's and 13 of its franchisees for labor law violations. The NLRB argues that the lead company exerts sufficient control/influence on the franchisees' operations to be considered a "joint employer". See NLRB, *McDonald's Fact Sheet*, available at http://www.nlrb.gov/news-outreach/fact-sheets/mcdonalds-fact-sheet.

36 Admittedly, the line between actions and omissions is not always clear, since theoretically, creating a risk can be seen as an action; see George P. Fletcher, *The Fault of Not Knowing*, 3 THEORETICAL INQUIRIES IN LAW 265, 279 (2002). In the current context, choosing unreliable contractors arguably creates the risk for workers. However, given that the risk was created by way of otherwise legal behavior, we are still faced with the same question: whether we should legally require A to take measures to prevent the risk to B's employees. See also Mares, *supra* note 31.

37 Cf. *Chandler v. Cape Plc*, [2012] EWCA Civ 525, [2012] 3 All ER 640.

Consider now the scenario of supply/production chains: A contracts with B that contracts with C which contracts with D to produce a product. D pays less than the minimum wage (or otherwise violates labor laws). In such situations it is very unlikely that the payment by A is based on the number of work hours (a per-hour rate), so A would not know what exactly the workers are getting. Even if A is oblivious to labor law violations it will be impossible to say that its *actions* have caused these violations. Can we say that A has caused the harm by omission? Again it would be difficult to make a case for a general duty to act positively to protect the rights of D's employees. But arguably such a duty arises when A makes representations to the public (explicitly or implicitly through the brand name) that can be construed as assuming such a duty. I refer to this situation in section 4 below.

2. Prevention and loss-spreading

One of the main goals of tort law is the prevention of harms. We hold the person who caused the harm responsible, in order to ensure that he/she has an incentive to prevent the harm in the first place.[38] But what if a third party that *did not* cause the harm has the power to prevent it? It could be the efficient solution to hold the third party liable, if he/she is the "cheapest cost avoider" – has the ability to prevent the harm most cheaply. It has been argued that this is often the case with labor subcontracting:[39] lead companies are in a position to detect violations through monitoring, which should be quite cheap because they already monitor subcontractors for quality and turnaround time; and they can often prevent violations simply by calculating the minimum payment required to obey labor laws and paying it. Moreover, unrelated to efficiency, if there is an entity that has the power to prevent harm (labor law violations leading to non-decent work conditions), it is tempting to require that this power will be used and the harm will be avoided.[40]

Brian Langille has argued for lead companies' responsibility in production chain cases for reasons of enhancing capabilities and human freedom.[41] He believes that when we focus on these goals, relationships do not matter anymore, just the workers themselves. However if our goal is to enhance capabilities and freedom, it says nothing about who should shoulder the burden of paying for this goal. Why should the lead company be responsible, instead of taxpayers at large? Langille does not answer this question, but implicitly, perhaps assumes that A should be responsible for D's employees because A has the power to prevent violations by D (and thus enhance the workers' capabilities and freedom). Indeed, other authors have argued that the best

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38 According to the famous Learned Hand formula, liability is imposed only when the cost of prevention is lower than the expected harm (taking into account the probability of the harm). In the current context, I assume this to be the case.

39 Rogers, *supra* note 31, at 36-38. And see Alan Hyde, *Legal Responsibility for Labor Conditions Down the Production Chain*, in CHALLENGING THE LEGAL BOUNDARIES OF WORK REGULATION (Judy Fudge, Shae McCrystal & Kamala Sankaran eds., 2012) 83.

40 If the "harm" is an infringement of employment laws, one might wonder why the direct employer (the subcontractor) is not the cheapest cost avoider. The answer is that the harm is usually intentional; when the subcontractor knowingly violates the law it obviously has no interest in avoiding it.

41 Brian Langille, *"Take These Chains From My Heart and Set Me Free": How Labor Law Theory Drives Segmentation of Workers' Rights*, 36 COMPARATIVE LABOR LAW AND POLICY JOURNAL 257 (2015).

way to solve the widespread infringement of rights in supply chains is by curbing competition among contractors, which can be achieved by forcing the lead companies to impose minimum terms for the contractors' workers.[42]

Nonetheless, the fact that one has the power to prevent harm cannot be sufficient to place responsibility on him/her. What if I have deep pockets that will allow me to shield strangers from harm? Obviously it is not enough to require me to do so. Even if I happen to be in a position to prevent the harm most cheaply – perhaps because I have created, for benevolent reasons, a monitoring apparatus – it does not justify making me legally liable if I fail to do so. Especially when prevention is costly; in the context of indirect employment, for example, it requires investing money in choosing the "good" (reliable) subcontractors, and later in monitoring them. There has to be some connection between the parties that justifies the imposition of these costs.

In tort law, the doctrine that places liability on people who did not cause the harm themselves – vicarious liability – is limited to employer-employee and principal-agent relations. If you send someone to do something on your behalf, you could be responsible for harms he/she has inflicted on others – even if you did not want the harm and the employee/agent has deviated from your instructions. The goal of prevention plays a central role in this case; it is assumed that employers/principals have the power to prevent harms by their employees/agents, and should be given an incentive to do so. The law thus sees sufficient connection between the principal/employer and the victim of the agent/employee to justify direct responsibility.

Tort law does not extend the same logic to subcontracting, because it is assumed that a client inviting work from a contractor generally does not have control over the contractor – so does not have the power to prevent harms either. The independence of the contractor presumably also creates some distance/disconnection between the client and the injured party. A principal does not necessarily control his agent, but the agent is seen as his "long arm", acting on his behalf. A subcontractor is not generally seen as the long arm of the client. However there are specific situations in which we can find a relatively high degree of control over the subcontractor (and thus power to prevent violations) as well as some proximity between the parties. For example, when a large organization engages with a small cleaning contractor, the organization has some control over the contractor because the work is performed on its premises and because of the inequality of power between them. And the connection between A and B's employees which is also required to justify liability arguably exists because they are part of the same community (see section 5 below). Also in the case of a production chain, we can sometimes see a high degree of (indirect) control over the subcontractors, and arguably the connection between A and D's employees is created through the representations of the brand (see section 4 below). We can see, then, that the goal of preventing the harm, just like the idea of causation discussed in the previous section, is not sufficient in itself to justify holding the lead company responsible. We

[42] Mark Anner, Jennifer Bair & Jeremy Blasi, *Toward Joint Liability in Global Supply Chains: Addressing the Root Causes of Labor Violations in International Subcontracting Networks*, 35 COMP LAB L & POL'Y J 1, 21 (2013). See also Weil, *supra* note 1, at 205-6.

need an additional element connecting the lead company with the workers. But such an additional element sometimes exists and would justify legal responsibility of the indirect employer.

Note that the idea of extending vicarious liability beyond the confines of employer-employee and principal-agent relations is not revolutionary. In several different cases courts have found it justified to place liability on third parties who were not employers/principals, when the same underlying rationales appeared to exist.[43]

A related justification places liability on the lead company to ensure that the loss is spread among many (clients/consumers) instead of falling entirely on a single, vulnerable party (the worker employed indirectly). If lead companies have to invest resources in prevention, they can be expected to (slightly) raise prices, and this is desirable from a distributive perspective – because it is done to avoid the situation in which vulnerable workers shoulder all the cost. If a lead company fails to prevent the harm and has to pay after the fact (when employment laws have been violated), the same result can be achieved. Loss-spreading is sometimes presented as a separate justification for vicarious liability, however it cannot be assumed that the lead company will always be able to distribute the cost rather than shoulder it. This depends on the actions of other competitors. So it seems more accurate to consider loss-spreading a supporting justification when the lead company is required (for other reasons) to prevent the infringement of employment rights. In such cases, it might have to internalize (bear) the cost, or it might succeed to spread this costs among many others. The point here is that the latter alternative is also justified.

3. Benefit

Another possible justification for lead companies' responsibility is based on the fact that they benefit from the subcontracting/franchising model. There are two possible variations to this argument. One is that A benefits from resorting to indirect employment instead of employing the workers directly. Assume that A is obligated by collective agreements to pay its own employees $20 per hour. Employees of B, in contrast, are paid only the minimum wage of $7.25 per hour. Instead of producing in-house, A prefers to outsource part of the production to B to save some of the labor costs. Assume that A pays B more than $7.25 per hour of work, enough for B to pay this sum to its workers and still make a profit. If B ends up violating labor laws, for example by paying less than the minimum wage, one could argue that A should be responsible because it benefited from the legal structure that created this risk.

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[43] See, e.g., John Doe v. Bennett, [2004] 1 SCR 436 (Supreme Court of Canada); Ewan McKendrick, *Vicarious Liability and Independent Contractors: A Re-Examination*, 53 MODERN L. REV. 770 (1990) (reviewing UK cases); Rogers, *supra* note 31, at 42-47 (reviewing US cases). Note that the law also recognizes vicarious liability for the acts of independent contractors when the activities they are required to do are "inherently dangerous"; although apparently only with regard to physical harms. See Restatement (Second) of Torts § 427.

But what is wrong about choosing a legal structure that is most beneficial to you? People are generally allowed to seek benefit/profit. If it's a sham arrangement, then you are evading the law by misrepresenting the relationship, i.e. making a profit by circumventing the law. But remember that this part only deals with non-sham arrangements. Seeking to maximize benefit is not in itself morally wrong.[44]

A different variation of the argument focuses on the more limited set of "losing contracts" – when A pays B a sum which makes it impossible to pay the minimum wage without losing. In this scenario B can be expected to find a route to avoid the loss, and this is likely to happen by shifting the loss to its employees. In such cases we can say that A is not only benefiting from the model of outsourcing/indirect employment, but also from the violation of labor laws itself. A enjoys such a low price only because it is based on non-decent (illegal) work conditions to B's employees.

In the "losing contract" scenario, there are cases in which we can say that A *caused* the harm and should be liable accordingly. However as we have seen in section 1 above, this requires several additional conditions. What if we know that B would have paid below the minimum wage anyway? Or the payment made by A is a lump sum, not allowing one to easily know that this is a losing contract? Or the employees perform work for other clients of B as well, making it impossible to link directly between A's actions and their situation? In all of these situations it is difficult (or impossible) to establish causation, but there is still a feeling that A's conduct is reprehensible. This can be explained, perhaps, by reference to principles of unjust enrichment. A is enriched and at least to some extent this is on the back of B's employees, and this enrichment is based on illegal behavior. Even though the illegal acts are by another party (B and not A directly), the use of a losing contract by A seems sufficient to make the enrichment "unjust".[45] Another way to explain the justification for liability in this case is by noting that A *should have known* that its actions are likely to lead to labor law violations from which it will benefit. Even if the link between the low payments to the contractor and the harm to the workers was not obvious on its face, at the very least it created a duty on A to examine this further, and avoid the situation of benefitting from these violations.

4. Representation

Assume that an organization (for example a University) contracts with a cleaning company to clean its premises. Due to public pressure the organization makes a public commitment to ensure that the cleaners' rights will be protected. Can such statements create a legal liability? In themselves, they cannot. General promises made to the public at large are not legally binding. However, while there is no contractual liability, such promises are arguably sufficient to create a

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[44] I therefore adopt a much narrower understanding of this justification than the one advocated by Barry, *supra* note 29, and by Dahan et al., *supra* note 30.

[45] For a moral discussion see Robert E. Goodin & Christian Barry, *Benefiting from the Wrong-doing of Others*, 31 J. of Applied Phil. 363 (2014).

"duty of care" towards the workers – some direct connection between the organization and the workers, that is needed to support tort-like liability in case the University is causing the harm to them, whether by action or (arguably even) omission.

An interesting question is whether a similar commitment – a representation to the public concerning the protection of workers' rights – can be seen as implicit in brand reputation.[46] A useful source of inspiration is the "apparent manufacturer" doctrine, according to which "one who puts out as his own product a chattel manufactured by another is subject to the same liability as though he were its manufacturer."[47] Representation therefore matters; if you present the product as your own, you are responsible for it, whether you actually manufactured it or not. This doctrine lost some of its relevance in the U.S., at least for physical injuries, after product liability laws have been further strengthened, with strict liability imposed on all sellers in the chain of distribution.[48] However what if you are not part of this chain, but only give your name to the product? And what if the harm is not physical injury? In this specific context, the rule in the U.S. is somewhat narrower: the law generally places liability on the trademark owner (the brand) only when it participated substantially in the design, manufacture, or distribution of the licensee's products.[49] This has been criticized by scholars who argue that brands should be responsible because of the appearance created by the logo, even without participation in the design or manufacturing.[50] Indeed, in other jurisdictions, presenting yourself (with the brand name) as the apparent manufacturer is seen as an assumption of responsibility; it is considered sufficient to create liability towards those harmed by the product (and not only for physical injuries).[51]

In a similar fashion, an "apparent agent" doctrine places responsibility on franchisors when an appearance is created to consumers that the franchisee operating the business is acting as their agent (even if this is not truly legally the case).[52]

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46 To clarify, I do not refer here to situations of false/misleading advertising, which can lead to an unfair competition claim.

47 Restatement (Second) of Torts, s. 400 (1965).

48 Restatement (Third) of Torts: Products Liability (1998).

49 Restatement (Third) of Torts, s. 14 comment (d) (1998).

50 David J. Franklyn, *The apparent Manufacturer Doctrine, Trademark Licensors and the Third Restatement of Torts*, 49 CASE W. RES. L. REV. 671 (1999); Katya Assaf, *Brand Fetishism,* 43 Conn. L. Rev. 83, 119-120 (2010).

51 EU Directive 85/374/EEC on liability for defective products, Art. 3; Consumer Protection Act 1987, s. 2(2)(b) (UK); Liability for Defective Products Act 1980, s. 1 (Israel).

52 The case-law in the U.S. regarding this doctrine is inconclusive and often contradictory; for reviews of cases see Randall K. Hanson, *The Franchising Dilemma Continues: Update on Franchisor Liability for Wrongful Acts by Local Franchisees*, 20 CAMPBELL LAW REVIEW 91 (1997); Heather Carson Perkins, Sarah J. Yatchak & Gordon M. Hadfield, *Franchisor Liability for Acts of the Franchisee*, 29 FRANCHISE L.J. 174 (2010). Some courts assumed that it is "common knowledge" among consumers that franchisees are operating branches independently and not as agents of the franchisors, but this was shown to be empirically false; Robert W. Emerson, *Franchisors' Liability When Franchisees Are Apparent Agents: An Empirical and Policy Analysis of "Common Knowledge" About Franchising*, 20 HOFSTRA L. REV. 609 (1992). On the use of this doctrine in

Applying the same logic to the indirect employment context, just as the lead company (brand) is assumed to be the manufacturer, even when it is not, it can be assumed to be the employer, even when it is not. We expect the lead company to be responsible for harms done to consumers even though it is not directly responsible for the defective product, because by giving its name to the product it created an illusion of controlling the manufacturing. This is perceived as an assumption of responsibility. In the same token, we can say that the lead company should be responsible for harms done to employees working on producing the product, because by giving its name to the product it created an illusion of controlling their employment.[53] If I am employed by a subcontractor of Nike sewing apparel products, I probably know that Nike is not my direct employer, but I do not know whether it has ultimate control over the terms of my work or not. It would be reasonable for me to assume that Nike has at least *some* control over my work environment/conditions. This is very similar to the consumer, who probably realizes that Nike did not produce the products in-house but has rather used subcontractors; at the same time, the consumer might reasonably assume that it exerted some level of control over them.

Representation is usually considered meaningful, normatively and legally, only when it leads to reliance.[54] If I make a decision (to buy something, or work somewhere) that could be said to reasonably rely on representations created to me/ appearances made, this could justify liability. Admittedly, the lead company cannot be said to assume responsibility through implicit representations if it makes *explicit* pronouncements to the contrary. Accordingly franchisors have been recommended to minimize the risk of liability by insisting on prominent signs indicating local ownership of the franchisees.[55] In theory, this could be an easy way for a lead company to prevent liability: it can let all the employees of its subcontractors/franchisees know in advance that it has no control over their work conditions and no responsibility for them. However this might not be easy to do from a public relations perspective and from a managerial perspective (the franchisors' interest in employees that are identified with the brand and motivated to uphold its high standards).

Assuming there was no explicit denial of responsibility (in advance), we are left with the question of whether workers have relied on the representations of the brand when deciding to (indirectly) work for it. Given that the workers involved usually have very few alternatives,

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Italy, see Gregg Rubenstein et al., *Vicarious and Other Franchisor Liability*, 9 INT'L J. FRANCHISING L. 3, 12 (2011).

53 For a recent case showing that court (at least in the U.S.) could be hostile to such claims, see *Courtland v. GCEP-Surprise, LLC*, 2013 WL3894981 (D. Ariz. 2013). In this case, the employee sued Buffalo Wild Wings (a restaurant chain) for discrimination, harassment and retaliation, but the case against it was summarily dismissed, even though the employee believed that she was employed by the franchisor. The Court rejected an apparent authority argument, because it did not consider this belief to be "objectively reasonable" and based on manifestations of the franchisor. Buffalo Wild Wings signs everywhere, a handbook with their logo, and statements by supervisors where not enough.

54 See Alan O. Sykes, *The Economics of Vicarious Liability*, 93 YALE L. J. 1231, 1276-77 (1984). Also John L. Hanks, *Franchisor Liability for the Torts of Its Franchisees: The Case for Substituting Liability as a Guarantor For The Current Vicarious Liability*, 24 OKLA. CITY U. L. REV. 1, 13 (1999).

55 Hanson, *supra* note 52, at 105; Perkins et al., *supra* note 52, at 180.

actual reliance is probably rare. However, it seems to me that even without reliance, representation is meaningful. It cannot by itself create legal responsibility; however it can be used as a supporting argument, showing the existence of some connection (even if minimal) between the lead company and the workers. As noted in sections 1 and 2 above, sometimes this small support is necessary to establish legal liability based on other justifications.

5. Citizenship

A final idea that can justify lead company responsibility is citizenship. The concept is used here not in the narrow legal sense of nationality, but in the broad sense of having rights because of being part of a community. Labor law scholars have been using the concept of citizenship to critique the exclusion of some workers from the scope of protection – their treatment as "non-citizens" – whether because they lack legal citizenship (nationality) or because they are otherwise on the margins of society.[56] Such writings have focused on the relationship of the workers vis-à-vis the State – the lack of legislative protection – advancing the claim that all workers should be treated as citizens (in the broad sense). However the same idea can be applied to the level of the workplace as well. Workers are not only part of the broader community (and therefore should enjoy protection from the State), they are also part of a local community at the specific workplace. Workers employed indirectly who work at the worksite of the lead company are in some sense part of the same local community as the employees of that lead company. Cleaning and security workers are an obvious example; although they are usually (at least in Israel, but also in many other countries) employed through subcontractors, in practice they work only for a specific client (lead company/organization) for a significant period of time. Arguably, they are part of the same community of workers together with the client's employees, and should be seen as "citizens" of the lead company/organization entitled to respect and to rights.[57]

This argument finds strong support in a theory developed by Cynthia Estlund,[58] who emphasized the importance of social bonds in the workplace, for the workers and also for civic engagement and democratic participation. Work is a major forum of civil society; a place for people from different backgrounds, races and genders to work side by side and interact with each other. This social integration enriches democratic life. Estlund argues that labor law plays – and should play even more – a role in supporting this aspect of work. She does not rely on the concept of citizenship, but she does refer extensively to ideas of community and connectedness, stressing their importance for society at large. The fragmentation of the workplace – specifically, with the relegation of some workers to indirect employment – is quite obviously detrimental to the

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56 Linda Bosniak, *Citizenship and Work*, 27 N.C.J. INT'L L. & COM. REG. 497 (2002). See also Jennifer Gordon, *Transnational Labor Citizenship,* 80 S. CAL. L. REV. 503, 510 ff (2007) (focusing on citizenship in unions).

57 Here as well, I suggest a justification much narrower than the one offered by Dahan et al., *supra* note 30. While they similarly place much emphasis on what they call "connectedness", they see it as inherent in labor relations in general (without reference to physical or other proximity). They do not explain why (and when) the indirect employer should be seen as a party to this connection.

58 CYNTHIA ESTLUND, WORKING TOGETHER: HOW WORKPLACE BONDS STRENGTHEN A DIVERSE DEMOCRACY (2003).

possibility of fostering connectedness. Placing responsibility on lead companies towards indirect employees working on their premises would send a strong message against this break-up of the workplace community.[59]

The integration of indirect workers as part of a local community in the workplace is often considered troubling by lead companies/organizations. The tests used in different countries to decide the identity of the legal employer usually include an examination of the level of integration in the organization.[60] Being integrated into the organization apparently suggests (whether rightly or not) subjection to hierarchical control, which leads courts to conclude that employment relations exist. Employers therefore try to mask any indication that indirect employees are integrated into the organization.[61] For example, where dining facilities are available in the workplace, those employed through contractors or TEAs can be prevented from eating together with internal employees.[62] Sometimes there is also an attempt to create a physical separation between internal and indirect employees, even within the same worksite.[63] When such methods are invoked to avoid responsibility, this should not change our understanding of the situation. In other words, the question is not whether some workers are *in practice* part of a community in the workplace, but whether as a matter of principle they *should* be seen as part of the same community.

I have argued in this section that a broad idea of citizenship (or community) in the workplace can help justify lead company liability. Should this be limited to workers who work at the same physical workplace? In today's world, communities are created not only based on physical proximity, but in other ways as well; various technologies are helping us to connect with others. Can we see all those working for the same lead company/organization, whether directly or indirectly, as part of the same community, and as a result, as having some "citizenship" rights vis-à-vis the lead company? Although in principle there could certainly be strong connections even without physical proximity, the problem is that there is no clear stopping point to this argument. Every company in the market is connected with other companies (buying/selling/getting services/delivering services) which in turn work with additional companies – in endless connections. While it is difficult to draw clear lines, it seems that physical proximity and face-to-face interaction – including informal interactions not planned in advance – usually create a stronger connection, thus supporting a stronger argument.

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59 On the importance of social inclusion as one of the main goals of labor law see also HUGH COLLINS, EMPLOYMENT LAW, 2nd ed. (OUP 2010) 22. On fostering solidarity as a goal of labor law – and its connection to the idea of citizenship – see Catherine Barnard, *The Future of Equality Law: Equality and Beyond*, in THE FUTURE OF LABOUR LAW: LIBER AMICORUM BOB HEPPLE (Catherine Barnard, Simon Deakin & Gillian S. Morris eds., 2004) 213, 214.

60 Davidov, *supra* note 28.

61 See also Weil, *supra* note 1, at 188, 196.

62 See, e.g., Hila Weisberg, *Bank Leumi Creates Social Classes Among Its Workers*, TheMarker Nov. 7, 2012 p. 14 [Hebrew].

63 *Ibid*.

6. Inefficiency

The previous sections examined several possible arguments in favor of placing some legal liability on lead companies towards indirect employees. There is also one major argument against it: by imposing liability on lead companies we will limit their flexibility in choosing contractors, and also inflict on them the costs of monitoring and/or paying for labor and employment law violations of the contractors. This will place impediments on the free market and lead to inefficiency. Imagine a company that is contracting with several companies who in turn use several subcontractors to produce its products; or a company that has numerous franchisees. Once we create direct legal liability on such lead companies towards the workers of the subcontractors/franchisees, they will have to change the way they do business. Although in theory they will still have the freedom to decide whether to "make" or "buy", in practice, at least to some extent such liability will force them to "make" more, or at least assume responsibility *as if* they are "making" rather than "buying".

This is an important consideration that we should take into account. However there are two answers that significantly mitigate such concerns. First, in a world without lead company responsibility, externalities are prevalent.[64] Harms created in the process of producing the lead company products are not borne by that company, and as a result the company might take decisions that ignore the full costs of its activities. Efficiency requires internalization of the full costs. In theory, the subcontractors can be expected to bear their own costs (including the harms they inflict on others), and these will be reflected in the payment they get from the lead company. In practice, however, market failures are prevalent, leading to externalities that lead company liability can solve.

Second, the discussion in the previous sections already took the concern of inefficiency into account, even if implicitly. It was not suggested that the lead company should internalize all the costs indirectly related with its activities, but for the most part only costs related to harms it has *caused*, or could have *prevented*. This was based on inference from tort doctrines (negligence and vicarious liability) that impose liability in similar situations, and have already been "vetted" as efficient.[65] The other arguments discussed in the previous sections have led to justifying liability only in very limited, specific situations: in case of "losing contracts"; when the lead company made representations that were relied upon; and when indirect employees work at the same worksite as "internal" employees. The first two of these practices are hardly ones that we should protect to enhance efficiency. Paying contractors such low sums that they cannot pay minimum wages does not improve overall efficiency in any way; it simply transfers resources from the employees who deserve them to the lead company. Making representations that lead to reliance and then failing to take responsibility goes against the general principles of contract law and does not enhance efficiency either.

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64 Weil, *supra* note 1, at 18-19.

65 See, e.g., RICHARD POSNER, ECONOMIC ANALYSIS OF LAW, 6th ed., Ch. 6 (2003); Sykes, *supra* note 54.

The practice of indirectly employing people who work at your own worksite is different. Assuming this is not a sham situation, we can see a business reason that appears efficiency-oriented: concentrating on core competencies.[66] In such cases, the issue of efficiency should be taken into consideration as a valid counter-argument.

V. Conclusion

David Weil's book offers a thorough description of the practice of indirect employment in the U.S. (through subcontracting and franchising), and a convincing explanation of the reasons behind this practice. The book also puts forward several proposed solutions. This article started with a description of the practice of indirect employment in Israel, which is similar in many ways to the U.S., although with some (relatively minor) differences. The first part thus confirmed that Weil's description captures a phenomenon which is general rather than specific to one legal system. Indirect employment is one of the main problems faced by Israeli workers in the last two decades, and a major challenge for labor law today and in the foreseeable future.

The second part provided a critical account of solutions adopted in Israel over the last two decades for indirect employment. The Act enacted to regulate TEAs was effective only once it included a maximum period of employment through TEAs (nine months), with automatic transfer to the client thereafter. As for subcontracting, the labor courts and the legislature have generally failed to prevent sham arrangements (in which little more than the title of "employer" is outsourced), and in recent years have opted for a model of "residual employer" in which the "client" can at most become liable as a guarantor of the contractor.

Weil brings together several different kinds of indirect employment under the heading of "the fissured workplace", and some additional types have been described here and in other contributions. However, while much is gained from such a broad view, there are also significant differences – and normatively, there *should* be differences – in terms of the appropriate legal treatment of different cases. The third part offered an analytical roadmap to confront indirect employment, distinguishing between solutions suitable for sham arrangements; instances when the characteristics of the employer are shared between two or more entities; and situations involving a lead company that lacks the characteristics of an employer. The possible legal responses for each scenario were outlined. With regard to sham arrangements and shared employer characteristics situations, I have detailed my proposals and justified them elsewhere. The issue of lead companies in situations of real outsourcing/subcontracting has been the focus of the fourth (and main) part.

The fourth part was dedicated to an examination of possible normative justifications for lead company liability towards indirect employees. It serves as a complement to Weil's book, which

[66] Weil, *supra* note 1, Ch. 3.

assumes that lead companies should bear some responsibility but does not justify this view normatively, at least not in any detail.[67] The starting point for this part was that the arrangement is not a sham (otherwise it should simply be ignored), i.e. the subcontractor/franchisee is the employer, not only formally but also in reality (because it has the characteristics of an employer). In the third part I have argued that the lead company should not be considered a full-fledged "employer" in such cases; the question for the fourth part was whether it should be required to assume responsibility as a guarantor for violations of the direct employer.

The discussion suggested that lead company liability can be justified in the following cases. First, when the lead company has *caused* the infringement of employment rights. Causing by action is possible, although probably rare. Causing by omission is more common, but I have argued, relying on tort law principles, that liability in such cases is justified only when coupled by citizenship/community claims or by representations that can be seen as an assumption of responsibility. These supporting justifications (citizenship, representation) are necessary to make the direct connection between the lead company and indirect employees, a connection that is necessary to legally require action. Second, the lead company should be liable if it could have *prevented* the infringement of rights, which is the case in some specific scenarios, and similarly requires a supporting justification (citizenship or representation). Third, in the case of "losing contracts" the lead company should be liable because it has *benefited* from the infringement of rights. Fourth, *representation* by the lead company (usually implied) that can reasonably be seen as suggesting that the company has some control over work conditions, can justify liability if coupled by reliance of the workers on this assumption. In practice reliance is probably rare, but representation in itself can be used to support other justifications (as noted above). Finally, when those employed indirectly work regularly at the same worksite together with the "internal" employees, they are part of the same community and for reasons of *citizenship* (broadly conceived) have a claim for liability of the lead company. This can be an independent justification, and can also be used to support other justifications (as noted above). Finally, I considered the risk of inefficiency, which pulls in the opposite direction. This turned out to be relevant mostly in the case of outsourcing performed on the worksite of the lead company, countering the citizenship argument. It seems fair to conclude that given the problem of inefficiency, citizenship cannot serve as an independent reason to impose liability on lead companies; however, it can certainly be used as a supporting argument in cases involving causation or prevention.

To summarize the practical conclusions of this normative discussion, lead companies/ organizations enjoying the work of employees employed by others should be directly responsible for them, as guarantors (or "residual employers"), in the following cases:

[67] In chapter 8 of the book Weil discusses the issue of lead company liability, but for the most part he is concerned with possible doctrinal routes for achieving it.

(a) In situations of outsourcing work to contractors, liability should be imposed when the engagement is based on a "losing contract". In such cases, the justifications of causation, prevention and benefit converge. Indeed, in some legal systems there is already legislation placing liability on lead companies towards indirect workers in situations involving losing contracts.[68]

(b) In situations of outsourcing work to contractors, liability should also be imposed in some circumstances (though not all) when the work is performed on the lead company premises – based on justifications of causation, prevention and citizenship. Given the difficulties of enforcement, it is suggested to create a presumption of liability in such cases, or alternatively decide on strict liability for specific sectors, such as cleaning and security.[69]

(c) In production/supply chains, as well as franchising, liability should be imposed on lead companies based on implicit brand representations, on the assumption that such companies also have the power to prevent the infringement of rights. It is proposed to create a presumption of liability, which can be refuted if the lead company proves that there was no representation suggesting (even implicitly) control over work conditions, or no practical ability to prevent the harm.

There are of course other possible methods to achieve lead company liability. For example, at the "softest" end of the spectrum, government-regulated "ethical consumption signs" have been proposed as a way to encourage competitive altruism (i.e. buying products that were made ethically, including in the labor sphere).[70] A more forceful technique used in the U.S. is the "hot cargo" provision of the Federal Labor Standards Act, which prohibits the shipment, delivery and sale of products in violation of the Act – unless the purchaser acts in good faith and has no knowledge of such violations.[71] This could be an effective method to put pressure on lead companies to prevent violations by subcontractors, and indeed it has been interpreted as imposing an affirmative duty on the buyers to check that the Act has not been violated.[72] However, without a private right of action, the effectiveness of this provision depends on the

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68 See, e.g., California Labor Code § 2810 (2008), and the Act to Improve the Enforcement of Labor Law § 28 (2011) (Israel), both dealing with losing contracts only in specific problematic sectors.

69 On the pros and cons of strict liability in this context, see Rogers, *supra* note 31, at 47 ff. Note that cleaners and security guards are sometimes (perhaps often) employed in arrangements that would justify *full* rather than residual employer responsibility by the user company – i.e. sometimes the user has some of the characteristics of an employer. Accordingly it would be justified to add a presumption of (full) joint employer liability in such cases.

70 Katya Assaf, *Buying Goods and Doing Good: Trademarks and Social Competition*, ALABAMA L. REV. (forthcoming). See also David J. Doorey, *Who Made That? Influencing Foreign Labour Practices through Reflexive Domestic Disclosure Regulation*, 43 Osgoode Hall L.J. 353 (2005) (proposing mandatory disclosure of information as a way to encourage firms to improve labor conditions down the supply chain).

71 29 U.S.C. § 215(a)(1).

72 Rogers, *supra* note 31, at 30; Weil, *supra* note 1, at 227.

political will of the government (that can ask for injunctions), and has generally been quite limited.[73]

Brishen Rogers proposed a negligence-like rule, requiring lead companies to take reasonable care to ensure that the goods and services they purchase are produced without labor and employment law violations. Depending on the circumstances, this might require them to take reasonable steps to prevent such violations, "up to and possibly including monitoring suppliers for compliance".[74] Rogers realizes the difficulties in such a case-by-case method, given that courts are poorly situated to examine preventive measures, and given the difficulties of bringing cases to courts – which will be necessary with the uncertainty inherent in the rule.[75] Accordingly he proposes to add some supplementary clear-cut rules in legislation, for specific sectors or circumstances.

My own proposals, as detailed above, could in principle fit into such a structure, supplementing a more general open-ended duty of lead companies. However the normative inquiry conducted in this article suggests that, while lead company liability is justified in some circumstances, this is not always the case. Imposing liability on lead companies when they have no characteristics of employers is not without costs. It should therefore be limited, in my view, to the situations listed above. Notwithstanding this qualification, this article follows the steps of *The Fissured Workplace*, as well as many other contributions of recent years,[76] by calling for the imposition of liability on indirect employers. At the most general level it supports such calls by clarifying the normative justifications behind them.

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73 *Ibid*. at 31.
74 *Ibid*. at 49.
75 *Ibid*. at 40, 54.
76 See, e.g., Langille, *supra* note 41; Hyde, *supra* note 39; Mark Anner et al., *supra* note 42; Rogers, *supra* note 31.