



**Monday, October 20**  
**4:30 pm-6:00 pm**

## **311 Contingent Workers**

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## Faculty Biographies

### Alice Conway

Alice Conway is assistant general counsel, commercial and employment law, and also advises the business conduct office, at Monsanto Company in St. Louis. She handles a full range of nonunion employment law matters and Code of Business Conduct issues, assists with contract drafting and negotiations, and advises on privacy, competitive intelligence, risk assessment and other matters. Ms. Conway's other specialties at Monsanto have included records management, antitrust, and the Foreign Corrupt Practices Act.

Ms. Conway is vice-chair of the board and chair of the board's policy committee of the St. Louis Society for the Blind, and is a member on the board of Opera in the Ozarks and the opera committee of the Missouri Federation of Music Clubs.

Alice simultaneously received her JD and PhD in comparative literature from Washington University.

### William Davis Harn

William Davis Harn is a senior attorney for Southern California Edison Company (SCE) in Rosemead, CA. Mr. Harn specializes in representing SCE and other employers on employment and labor matters, actively litigating cases through jury trial and appeal in both state and federal courts. He has handled over 30 labor arbitrations, appeared in regulatory proceedings before the California Public Utilities Commission, and provides practical legal advice and solutions to client organizations on a broad panoply of employment, labor and benefits matters daily.

Within ACC, Mr. Harn is the current chair of ACC's Employment and Labor Law Committee and secretary for ACC's Council of Committees. Mr. Harn is also a member of ACCA SoCal's board of directors, serving as the chair of ACCA-SoCal's golf tournament committee and 'Martinis till Midnight' events. Mr. Harn has been a past ACC and MCLE panelist on several subjects including discovery in employment law matters, workplace privacy, leave and disability management, wage and hour law, legal intern programs, and the elimination of bias within the legal profession.

Mr. Harn is a graduate of the University of the Pacific McGeorge School of Law, and he is also the current president of the Pacific McGeorge Alumni Association.



## The Roadmap

- Who are those guys?
- Do they really work for us?
- We're not responsible for that! Are we?
- Staying out of trouble
- (Un)real life stories



## Who are those guys ... ?

- Independent contractors
- Leased employees
- Part-timers/Temps
- Statutory Employees

Whether and when these individuals/workers are deemed employees can impact not only employer liabilities but can create unintended consequences from misclassification. The determination of status may be different depending on the legal context involved – e.g. Taxes, FLSA, Title VII, OSHA, ERISA, NLRA, workers compensation etc.



### Advantages of Independent Contractors, and Temporary/Leased Employees

- Cost savings, better handling of peak workloads, highly specialized projects, or work that is not part of the core business.
- Easier to let them go
- Hiring process may be delegated or abbreviated.
- Don't bother managing them or administering payroll and benefits
- No paid vacation, sick days, holidays.
- They can audition for their future jobs.



### Advantages of Independent Contractors and Temps (cont'd.)

- Employee jobs are more stable because they do not partake in the spikes and dips of the noncore workers.
- And, either because temp agency handles it or because they're independent contractors:
  - Need not be covered by workers' compensation
  - Do not have employment taxes deducted from their earnings by an employer
  - Have no rights to employee benefits
  - Are not employees subject to the Immigration Reform and Control Act (IRCA) of 1986



### Because they're Independent Contractors... (cont'd)

- Are not covered by many state and federal anti-discrimination laws
- Do not generally subject you to vicarious liability for their acts
- Are not included under OSHA and Federal/OSHA in an employer's duty to provide a safe and healthy work environment
- Are not covered by state and federal wage and hour laws
- Are not entitled to unemployment insurance benefits from your account
- Are excluded from coverage under the National Labor Relations Act (NLRA) (unions); and
- Do not count for purposes of the Warn Act (plant closure law).
- With freedom and flexibility for all.



### Disadvantages of Non-employees

- Less loyal, less accountable
- Not as attuned to Company value's and culture
- Demoralized by lack of advancement, status; not feeling like part of team
- Will they keep your secrets when they leave?
- Loss of control over quality and quantity of work



## Risks and Ramifications of Misclassification, in General

- Many of the same risks of misclassifying people whether you get them through temp agencies or directly.
- But the greater risk is when there's no temp agency to assume any responsibilities under the laws below.



## Ramifications under various laws for erroneous/intentional misclassification

- Tax laws, ditto. Payroll, FICA, FUTA, Medicare. State taxes.
- FLSA: overtime, child labor, minimum wage, double the unpaid wages, interest, fees, plus penalties if willful.
- Equal Pay Act prohibiting different pay for different genders for work of similar skill, effort, responsibility, working conditions. (amended FLSA) BIGGEST danger if temps or IAC'S work side by side in employee jobs.
- Anti-discrimination, harassment, retaliation statutes Title VII, ADA, ADEA.
- ERISA and COBRA: Big judgments possible-- pension, medical, savings, disability, vacation, etc. May end up settling even if you are right.



## Ramifications... (cont'd)

- Damages, DOL enforcement and state counterpart enforcement under MSPA: requiring disclosure to workers of info about wages, hours, working conditions; compliance with that info; maintenance of payroll and employment records, proper payment of wages, no "company store"; safe housing and transportation if provided by employer.
- FMLA: counting the IC'S may mean you do have 50 employees within 75 road miles and have been violating FMLA with respect to them and the people you know you employ.
  - OSHA: Safe conditions and work methods, hazard communications, PPE, medical monitoring, workplace monitoring. Training and recordkeeping obligations usually go to the company creating and controlling working conditions. may be shared with temp agency.
- Worker's Compensation, if temp agency not providing.
- USERRA: job reinstatement, accommodation, double wages and benefits lost.



## Some Advantages of Employee Leasing and or Temporary EE's vs. Use of Independent Contractors

- Usually avoid exposure for misclassification and related penalties
- ERISA issues tend not to come into play if plans are written to expressly exclude leased and or temporary employees
- Termination/Discrimination risks reduced/spread
- More continuity of relationship as a cost effective solution in meeting personnel and or skill set needs of a finite duration, but avoid going too long
- "Test Drive" future personnel without costly commitment



## Utilizing Leased Employees – Precautions

- The contracting business will almost always be deemed “joint” or “special” “employer” jointly responsible for compliance with workers’ compensation, tax, labor, wage and hour, and anti discrimination laws affecting such workers notwithstanding the independent contracting relationship with the leasing firm.
  - See e.g. *Burrey v. PG&E*, 159 F3d 388 (9<sup>th</sup> Cir. 1998), IRS Letter ruling 200017041
    - In CA, contracting entity is known as a special employer.
- Headcounts may create unexpected compliance and liability issues under statutes such as Title VII and FMLA



## Leased Employees – Precautions

- ERISA Gotcha’s – Absent careful wording, contingent workers can be unintentionally covered by a plan
  - Big risk for disqualification
  - Big cost increases
  - Leased employees are counted for non-discrimination testing - IRC 414(n)
- More on this later!



## Considerations for use of Contingent Workers

- Is there a question of legal classification and if so which test will apply to a determination?
- Is there a safe harbor provision re Independent contractors?
- Are there statutory or regulatory exceptions?



## Do they really work for us?

- The tests for determining the legal employment relationship
  - Contractor vs. Employee
- Common Law v. Economic Realities vs. Hybrid - three tests or one?



## Misconceptions

- My independent contractor and I both think that's what she is; she likes the flexibility.
- Our agreement defines the relationship. It says "independent contractor" or it says "Employees of only the temp agency".
- We don't withhold taxes; we use 1099, so these people are IC.



## Misconceptions... (cont'd)

- Her company is incorporated--Acme Consulting, Inc. Obviously she's an independent contractor. Although each supplier employer will have its own individual contract, the typical temporary employee contract places the burden of withholding and payroll taxes, workers' compensation insurance, unemployment insurance and employee benefits on the supplier rather than the customer employer. Additionally, the supplier employer may be contractually responsible for complying with all laws regarding recruiting, interviewing, testing, hiring, disciplining and terminating employees. Typically, the customer employer will be responsible for protecting its intellectual property rights and its confidential and proprietary information.



## Tests for Determining Worker Classification

- What's dry as crackers,
- Slippery as old carrots,
- Convoluted as a cheap, self-knotting necklace
- And as hard to deal with as a "some assembly required" toy?
- It's the three major classification tests.



## Tests for Determining Worker Classification (cont'd)

- They are: "Common law", "economic realities" and "hybrid".
- They borrow each other's factors and take each other's names in vain.
- Same test used for determining if we are co employer with temp agency, or employer of purported independent contractor.
- No one factor is decisive.
- Contract is not decisive.
- All facts of the relationship must be considered.



### Tests... (cont'd)

- Same test doesn't have the same factors from case to case.
- Most iterations of them will lead to the same result most of the time, but employers are a little better off with the common law test.
- Most rules about which test to use have exceptions.
- You could be an employer for some purposes and not others.



### Tests... (cont'd)

- Control over manner, method and means (whatever that means) of the work is the most important factor in all three (control over day to day activities most important, also hiring and firing).
- "Realities" and then "Hybrid" were developed to effectuate broad remedial purposes of employment laws, most popular from sixties through nineties.
- Trend toward decline in number of classification cases.



### Economic Realities test used in FLSA

- The more plaintiff-friendly realities test is used for FLSA also FMLA, because employee has same broader definition under those statutes.
- It answers the question: is the worker economically dependent on employer.



### Economic Realities test used in FLSA

- Typical factors:
  - Degree to which worker is subject to principal's control
  - Worker's opportunity for profit or loss
  - Worker's investment in facilities of the business
  - Permanence of the working relationship
  - Degree of skill
  - Degree to which worker's services are an integral part of principal company's business



### Typical Factors (cont'd)

- Degree to which they are free to work with someone else or restricted by various circumstances including licensing laws.
  - *Chao v. First National Lending Corp.*, 516 F. Supp. 2d 895 (ND Ohio 2006) (mortgage brokers were employees under FLSA so eligible for minimum wage/ OT)
  - *Bonnetts v. Arctic Express, Inc.*, 7 F. Supp. 2d 977 (SD Ohio 1998) (Truck driver sought protection of FMLA; court looked at duration, skill, control, worker's investment, worker's opportunity of profit and loss, and whether work was integral part of employer business; cross motions for SJ denied - questions of fact re control and whether work was integral part of business even though other four factors pointed toward independent contractor.



### Hybrid test

- Like Economic Realities test but more focus on control including hiring and firing.
- Also used in FLSA, FMLA.
- Before Clackamas in 2003, used for discrimination cases.
- Difference without distinction, as compared to the modern common law?



### Hybrid Test (cont'd)

- Some courts, notably in California, have used a hybrid test, looking at control over manner and means, plus:
  - The alleged employee's opportunity for profit or loss depending upon his/her managerial skills
  - The alleged employee's investment in equipment or materials required for his/her task
  - The alleged employee's employment of helpers
  - Whether the services rendered required a specific skill
  - The degree of permanence of the working relationship; and
  - Whether the service rendered is an integral part of the alleged employer's business.



### And the Common Law Test is Winning...

- Three Supreme Court cases: trend to using it instead of realities or hybrid,
- But S. Ct. test not pure; has some "realities" factors like "integral part of hiring party's business" and tax, benefit and duration considerations.
- Common law test also recently applied to tax, NLRA, OSHA, state statutes.





- *Community for Creative Non Violence v. Reid*, 490 US 730 (1989). (Common law test of employment status applied in copyright case).
  - Sculptor with "work for hire" contract was commissioned by nonprofit to create statue. Artist and non-profit claimed copyright ownership.
- Lower court found "work for hire" arrangement to create employment relationship so nonprofit owned it.
- But Supremes found Sculptor was independent contractor, so artist owned it.
  - Side bar: deal with this situation by copyright assignment, not "work for hire".



- *Nationwide Mutual Insurance v. Darden*, 503 US 318 (1992), (common law test applies under ERISA).
- Remanded for Court of Appeals to look at these factors:
  - (1) the skill required
  - (2) the source of the instrumentalities and tools
  - (3) the location of the work
  - (4) the duration of the relationship between the parties
  - (5) whether the hiring party has the right to assign additional projects to the hired party
  - (6) the extent of the hired party has discretion over when and how long he or she actually works



- (7) whether the worker receives a salary or is paid per job or by commission
- (8) the hired party's role in hiring and paying assistants
- 9) whether the work is part of the regular business of the hiring party
- (10) whether the hiring party is in business
- (11) the provision (or non-provision) of employee benefits; and
- (12) the tax treatment of the hired party



- *Clackamus Gastroenterology Associates PC v. Wells*, 538 US 440 (2003) (use of common law test re status is proper in Title VII, ADA, ADEA, and EPA cases, i.e. where EEOC has jurisdiction and status is relevant to determine coverage under the acts.
  - So don't let plaintiffs tell you EPA is like FLSA, though it amended it and has same definition of employee.
  - Question was whether director-shareholders of professional corp. were employees, putting corp. within jurisdiction of these laws.



- Since *Clackamas*, the Fifth Circuit has concluded that the touchstone of the analysis in ADEA cases is control of the employee, and looked at the following factors:
  - (1) whether the putative employer can hire or fire the plaintiff or set the rules and regulations with respect to the plaintiff's work
  - (2) whether and to what extent the putative employer supervises the plaintiff's work
  - (3) whether the plaintiff reports to someone higher in the putative employers organization
  - (4) whether and to what extent the plaintiff is able to influence the putative employer's organization
  - (5) whether the parties intended that the plaintiff be an employee; and
  - (6) whether the plaintiff shares in profits, losses, and liabilities of the putative defendant organization
- See *Coleman v. New Orleans and Baton Rouge S.S. Pilots' Assn.*, 437 F. 3d 471 (5<sup>th</sup> Cir 2006) (Pilots were not employees of association; controlled their own work and assumed liabilities).



### State Laws – Treatment Will Also Vary

- Generally the common law test will apply
- But see CA – “**Borello**” test
  - Common law is tempered by an economic realities analysis as well as deference to the purposes of the protective legislation at issue.
  - CA Supreme Court (in dicta) noted that the test it set forth could also be applied in other cases involving state law (e.g. FEHA, wage and hour)



### The Common Thread Among the “Tests”

Under either the common law, economic realities, or hybrid analyses, no one factor is necessarily special or controlling but right to control the manner and means of work is often given significant emphasis.



### Some Special Arrangements Regularly Deemed Independent Contractor Relationships

- Agent/Commission drivers of food products and or laundry services
- Full Time insurance salespersons
- Other traveling or outside salespersons engaged in full time solicitation of and transmission of sales orders to a principal (i.e. Mfgr's Reps.)
- Home workers performing work on supplier goods or materials (or performing some routine service) and then returning the items in a pre-established completed fashion to the contracting entity.



### The two-minute, two-factor, too convenient test

- See control and duration.



### Summary of Which Determinative Tests Apply

- |                      |                       |
|----------------------|-----------------------|
| • Federal Taxes      | • IRS "20"/Common Law |
| • NLRA               | • Economic Realities  |
| • FLSA               | • Economic Realities  |
| • Title VII/ADA/ADEA | • Split               |
| • ERISA              | • Common Law          |
| • IRCA               | • IRS "20"            |
| • WARN & Other       | • Usually Common Law  |



### Consequences of Misclassification

- Payroll & withholding tax liabilities may accrue to as much as double what would have been paid absent misclassification if found willful.
- May end up costing more than having hired the individual in the first place.
- Safe Harbor provision of IRC section 530 may help avoid stiff penalties.
  - 1099 issued, no treatment as employee at any time, not treatment of similarly situated individuals as employees, reasonable basis for treating individual as independent contractor (e.g. reliance on IRS private letter ruling, good faith advice of counsel, industry practice).
  - Only helps re tax issues, as worker will be treated as employee for all other purposes.



### More about ERISA, and the amendment to it called COBRA

- Section 510 forbids discriminating against or terminating employee to interfere with their right to plan benefits.
- Section 502: plaintiff claims he was improperly excluded under the terms of the plan, or the plan was wrongfully written to exclude him.



### More about ERISA... (cont'd)

- Under 502, plaintiff (or class reps) must exhaust procedures and remedies under plan. Plan administrator's decision is reviewed de novo unless plan gives her discretionary authority to interpret plan, and she has made a reasoned decision according to sound procedures established by the plan. Then the standard is the deferential "arbitrary and capricious" one. (See *Firestone Tire and Rubber Co. v. Bruch*, 489 US 101 (1989); *Hensley v. Northwest Permanente PC Retirement Plan and Trust*, 5 F. supp 2d 887 (D. OR 1998) (defining employee by W-2 instead of common law was deferentially reviewed because consistent with plan wording and past interpretations.)



### More about ERISA... (cont'd)

- If deferential review does not apply, most courts construe the plan against the employer where it is ambiguous, because it was drafted by employer.
- Exceptions to exhaustion under 1502: no meaningful access to plan or procedures, or the "futility" argument, or plan administrator has "conflict of interest"
- DOL can bring "breach of fiduciary duty claims" and some courts let private plaintiffs bring them also, especially if employer's breach of fiduciary duty caused them to give up plan rights or fail to participate in plan.



### More about ERISA... (cont'd)

- If employee has "colorable (arguable) claim" to plan benefits, must receive plan documents upon request
- Some courts say plaintiff has no standing to sue without "colorable claim",
  - but see *Capital Cities/ABC, Inc. v. Ratcliff*, 953 F. supp 1228 (D Kan. 1997) (employer's declaratory judgment action, assumed standing and went straight to common law employee and plan benefit eligibility determination for judicial economy because standing issue involved the same facts).
- If PLAN excludes but SPD appears to include, SPD controls.



### Statute of Limitations

- Courts have debated which statute of limitations applies under what circumstances.
- Argue that the statute of limitations began running when plaintiff reasonably could have known (e. g. because of agreement or paycheck) they were being classified as non employees. Some courts require more "actual knowledge" than others. See *Kryzer v. BMC Profit Sharing Plan*, 2001 US Dist. Lexis 18300 (D. Minn 2001).



### The bitter with the sweet

- Easier than other types of employment cases for defendant to win
  - But it's really bad to lose.
- To win, plaintiff must meet two requirements:
- Common law employee and
- Eligible under terms of plan.
- So if plan says "all employees" and the so-called temps and IC'S are common law employee's, you're sunk.
  - Even if agreement says no employment relationship is intended or created.



### And if you lose...

- Plan could be "Disqualified" either because you didn't include all eligible employees when you excluded the purported contractors or
  - because you now favor highly compensated people, now that these skilled contractors are in your plan.
- Disqualification means that the plan and the employees under it would have to pay more taxes.
- If you misclassified skilled people as independent contractors and you have to reclassify, plans may be disqualified because they may now favor highly compensated employees. NOT so much a risk if you made a less understandable mistake misclassifying less skilled people as contractors.
- IRS generally will not visit retro disqualification on employer that acted in good faith.



### Special Risk Area

- Terminating employees and bringing them back as temps or IC's ostensibly ineligible for benefits.
- Whatever the business reason for doing this, plaintiffs will have an argument that it was to save money in a way that Section 510 forbids.



### ERISA (cont'd)

- Although ERISA often preempts state laws, breach of contract claims can thrive in a state court.
- Descriptions of plan benefits can be considered unilateral offers, binding if employee fulfills the terms, such as being "employed" (as common law employee) and providing requisite amount of service.



## And Watch Out For This...!

- IRS says even if leased workers are common law employees of leasing agency, Section 414 says they may be counted as client employees for purpose of determining whether client's employee benefit plan discriminates to favor highly compensated workers.
- Section 414(n) requires that the leased workers be considered the client's employees for tax purposes if their services are provided to the client (1) on substantially a full-time basis, (2) for a period of at least one year, and (3) under the client's primary direction and control



## More about Taxes

- Payroll, FICA, FUTA
- Big risk, especially if contractors (as opposed to temp agency employees) are misclassified.
- Back taxes, penalties, 100 percent of FICA, FUTA, payroll taxes that employer and employee would otherwise have shared.
- In May, 2007, IRS announced that worker classification cases are "major area of emphasis" 2007-2008.



## More about Taxes

- Thirty percent of IRS audits this year will be based on employee classification issues according to chief of employment tax operations in small business and self employed division.
- GAO estimates that misclassification cost government \$4.7 billion in income taxes in 2006.
- IRS sharing info with DOL and several state IRS's. They send each other leads.
- Estimated \$1.5 billion in income, Social Security, and unemployment tax revenue is lost annually due to misclassification of as many as 3.5 million workers as independent contractors.



## The IRS formal test for determining employment status:

- Good news: 20-factor IRS test for determining employment status is gone.
- Bad news: They have three factors, now, with about 17 sub-factors
- They see:
  - Behavioral control: (of when and how what work is done)
  - Financial control over how the business aspects of the worker's activities are conducted; whether worker has significant investment or incurs significant expenses, whether she can make a profit or loss, and whether she also works for others.
  - Relationship of the parties: duration, agreements, are the individual's services a key aspect of client's business; and freedom to terminate.



## More Bad News

- The informal test:
  - Does the worker do tasks integral to the hiring company's business?
  - If so, control probable; employee; case closed; you pay.



## Pray for your Safe Harbor

- Section 530 safe harbor for employers who have consistently and reasonably classified workers as IC's, may be replaced by definition of EAIC, under the Taxpayer Responsibility, Accountability and Consistency Act which passed the House.
- If you filed 1099's and your classification mistake was reasonable, penalties greatly reduced.
- 530 not likely to be there for you if you dismiss employees and bring them back as IC's.
- And will not generally resolve plan disqualification issues under ERISA



## Pray for your Safe Harbor (cont'd)

- 530 protects client employer if the leasing company has proper money purchase pension plan and leased workers are not 20 percent of client's non highly compensated workforce
- Clients have additional protections if they work with a Professional Employee Organization (PEO) that has proper multiemployer plans



- Some Recent decisions indicate that if the supplier employer defaults on its payroll tax or withholding obligations, the customer employer may be liable for those obligations concerning its temporary workforce, even if customer employer has remitted the taxes to the supplier employer for payment to the IRS.



## In Co-employer situation, who is responsible for withholding taxes?

- Paymaster rule says it's the temp agency, if the temp agency controls payment of wages. Just delegating check-writing is not enough.



## Special Vulnerability

- Class Certifications by Temps Or Independent Contractors
- ERISA is where they most often succeed in getting class certified, because plaintiffs argue that the same facts are common to all--common law employees, eligible under plan terms.
- FRCP 23a: class must have all of these:
  - numerosity, (too many for joinder)
  - commonality of questions of law and fact
  - typicality: named members have same claims as the rest)
  - named plaintiffs adequately protect interests of rest of class.
- And under 23b, generally, in these cases, because class action must be superior to individual actions or advantages of class outweigh disadvantages.



- Your defense: they weren't treated the same; there were differences in control and duration, so no commonality and typicality.
  - See *Rumpke v. Rumpke Container Service, Inc.*, 240 F. supp. 2d 768 (SD Ohio 2002) (former route supervisors and route drivers suing a garbage company).
- Also, if class must be certified, try to get it under 23(b)(3) where opt-out opportunity must be given to class members. See *In re Allstate Insurance Co.*, 400 F. 3d 505 (7<sup>th</sup> Cir. 2005).
- If you want to settle before certification, court must find the class certifiable and the settlement arms-length.



- Possible Class action under discrimination laws if temps do same thing employees do.





## NLRA ISSUES

Will temporary workers be accreted into bargaining unit for representative elections?

- May depend on the administration
- In *M.B. Sturgis, Inc.*, 331 NLRB 1298 (2000) NLRB said yes if temps worked alongside employees and shared community of interest.
- But in *Oakwood Care Center*, 343 NLRB 76 (2004), the Board overruled itself holding unit could not include jointly employed workers (leased employees) without the consent of both employers.



## What about IRCA?

- Morsel of Good News – personnel supplier is primarily responsible for verifying eligibility to work.
  - Exception may be if client should have known the assigned worker was ineligible.



## Morsel of Good News

- MSPS: Agricultural companies generally not found to be co employers, and farm labor contractor is sole employer, if (perhaps a big if) AG company refrains from directly supervising.



## Does Independent Contractor Status Bar Discrimination Claims?

- No, they can sue for discrimination and retaliation under 42 USC. Section 1981. See *Wortham v. American Family Ins. Grp.*, 385 F. 3d 1139 (8<sup>th</sup> Cir. 2004).
- State laws sometimes more expansive.



## More Laws

- WARN (and state counterparts): Could temps or contractors count toward number of employees and trigger notices of plant closings?



## State Laws

- See *Montesano v. Xerox Corporation Retirement Income Guarantee Plan*, 117 F. supp 2d 147 (D. Conn 2000), aff'd in part and vacated in part 256 F. 3d 86 (2<sup>nd</sup> Cir. 2001), (leased employees sued for ERISA benefits as well as for vacation under NY law; handbook excluded leased employees from vacation so they lost.)



## Practical Approaches and Solutions

- Ditch some risks without losing all control
- Don't be inadvertent.
- Periodically do cost benefit analysis--employment versus temp or contractor. Risk mitigation usually costs something, such as using agencies that pay benefits.
- Periodically reevaluate risks. Have too many people become long term? Have we begun managing people who at first were autonomous?
- Make sure agreements with temp agencies, contractors, reflect reality of work practices.
- Be prepared to take action if you find that things have gotten problematic.



## Practical Approaches and Solutions (cont'd)

- Use contingent workforce for the traditional reasons--spikes in Workload, skills we don't have internally, work that is not part of core business, which may in fact be either specialized or unskilled.
- If you look at the continuum after hiring to firing, can you relinquish control?
  - If you had control over hiring and firing, could you forgo managing?
  - If you must treat them like employees, can you keep it to less than a year? Microsoft has had policy of one year plus 100 day break in service.)
- Choose agency with benefits. (More expensive but mitigates risk)
- Try to bring people in through agency rather than as solos.
- Have procedure for requisitioning temps so you don't get inadvertent relationships
- Try not to use side by side with employees unless duration short!



## What to look for in temp agency

- Is the leasing company well-versed in the payroll and personnel record keeping requirements under state and federal law? Request a sample personnel file and a description of the leasing company's payroll process.
  - How does the leasing company screen employees in the hiring process, so we're not liable for negligent hiring or unlawful employment practices?
  - Does the leasing company provide and administer employee benefits for the leased employees?
- Request proof of bonding or insurance and written assurance of indemnification, then review the leasing company's assets to ensure it is a solid company apt to remain in business.
  - Who will provide workers' compensation coverage for the leased employees? (Exclusive remedy doctrine will protect the other joint employer)
  - Who will be responsible for workplace safety issues (for example, training)? Existing case law indicates that an employer cannot divest itself of its duties under the occupational safety and health laws.



## Solutions

- Close partnership with temp agency so that they can manage temps for great results.
- This takes many meetings, follow-up meetings, training agency management, quarterly reports, audits, hand holding.
- Best with a small, motivated company that wants to be a department for you.



## Solutions

- Make agreement with temp agency work in your favor; risk mitigation but not risk elimination.
- Have bidding. Involve procurement.



## Solutions (cont'd)

- Contract should specify:
  - Thorough pre-employment screening, drug, background, references, education and licensing verification, immigration verifications, get temps to sign our confidentiality and IAP protection agreement signed;
  - Who's responsible for safety training, recordable injuries, PPE? Who is liable: creator, controller, corrector, exposer? Client employer may not be able to avoid; perhaps agency does generic training.
- Agency responsible for minimum wage at least; overtime, recordkeeping



### Solutions (cont'd)

- Agency recruits against well defined requisitions, perhaps a veto or courtesy interview for employer, if you need to take that risk.
- Deliverables of temp agency
- Agency responsible for setting pay and for payroll, AFICA, FUTA and other taxes
- Agency's management responsibilities--onsite manager?
- Agency responsible for safety and harassment training?
- Indemnification, insurance, broad, covering the laws mentioned earlier
- Agency supplies worker's compensation and whatever benefits workers have.



### Solutions (cont'd)

- ADA responsibilities for reasonable accommodations; who provides; who pays?
- IF FMLA applies, agency does notices, recordkeeping, reinstating, client cooperates.
- Agency should be responsible for complying with all laws controlling every aspect of an employment relationship.



### Solution: ERISA Plan Language that Excludes Temps and Contractors

- Plan applies to "common law employees paid directly by Payroll Department"
- Plan does not include "leased employees or independent contractors") (Recent cases say this excludes these people even if they are common law employees in Section 502 claims.
- "Notwithstanding any subsequent determination of employee status, employees are ineligible if they were hired pursuant to an agreement providing that such individual is ineligible to participate in the plan". Specifically excluded from coverage under this plan are independent contractors
- Standard provision: "You are eligible if you are a regular employee. You are not eligible if you are a temporary or seasonal employee or an independent contractor or if your services are provided to plan sponsor through unrelated entities or if you have an agreement saying that you will not be covered by the plan.



### Solutions, IC contract

- Use incorporated IC's, preferably a real Company and not your captive.
- Have consultant contract that treats consultant as business, a supplier.



### “Safeners” – mitigation of misclassification risks

- Workers so highly skilled and so far from your core business that you're glad they're autonomous
- Workers that are in business, have employees, investments in that business.
- An entire department, leased, managed onsite by the agency.
- Longer than a year, but specialized skills, defined project, little control.



### Misclassification risk mitigation (cont'd).

- Captive consultants
- ‘Safen’ by allowing them to work for others
- And allowing yourself to hire others for the same work.
- Intermittent, not economically dependent.



### Should we train them?

- If it's really important like safety, for harassment, then yes, though it's one "control over manner and means" subfactor.
- Should we invite them to the employee picnic?
  - if they clearly are employees because of control and duration, you're sunk anyway; invite 'em.
  - if they clearly aren't employees, picnic won't change that; invite 'em.



### Can you incentivize temps with bonuses and still not be employer?

- Hard question in close cases.
- Fairly safe to ask temp agency to design and administer bonus program to reward certain competencies.



## Summary

- Use contingent workers for traditional purposes, not just to save money
- If you really need loyalty, confidentiality, institutional knowledge, you are probably better off with employees.
- Remember control, duration, and all that (other) jazz.
- Unlike the real life, you can lower risks by losing control.



## Unreal Life story

- HYPO



## A lesson in unintended consequences...

BigCo uses Installs-R-me to deliver and install their giant convention display screen and materials at marketing conventions and other events. Installs has about 25 full and part time workers doing this activity. This includes some drivers, some electricians and some clerks in addition to the three shareholders who also do some of the work. Shareholder and manager Betty Krocka goes out to BigCo during a 'dry run' to check on the four member team assigned to do BigCo's set up for the ACC Annual Meeting in Seattle. After she arrives, she observes BigCo marketing director Hector telling two installers how to assemble and unassemble certain delicate parts of the display. He provides them with special screw drivers and wrenches designed for the assembly stating they must be used. He says, he will tell them where and when to set up the display. He tells Betty the display has to arrive on time or they will lose a \$20MM order. Joe, Install's regular driver, guarantees on-time delivery or its free. Betty nods. Frank, Installs Foreman, tells Joe the safest route to get the display to Seattle in BigCo's rented truck. Joe says he's short on cash and needs expense money so Frank gives Joe an Install debit card but tells him he can't use it for anything other than gas and food. Betty decides a meeting is in order finalize the details and they all head to the BigCo breakroom.



## A lady comes out of a bathroom ...

- Betty and one of the install helpers, Syrah Leigh, swing by the ladies room first. Syrah is the grand niece of Betty's husband and from Canada, Betty agreed to have her help out in the summer for cash. Upon emerging Betty slips on some oil injuring her leg. Syrah tries to catch Betty and injures her back.
- Betty and Sara sue BigCo for negligence. Do they recover?



### From bad to worse ....

- During an MRI in treatment for Syrah's back injury, doctors find out she has bone cancer. She is cleared to return to work in a week but, she wants and needs health care and long term disability benefits.
- Under the BigCo and Installs benefits plans eligible participants are defined as "all employees" who will be eligible to elect coverage as of the date they first perform work for the Company.
- Syrah files claims and appeals but they are denied by the plan administrators. She sues in federal court. Does she get relief?



### As luck would have it ....

- Joe delivers the equipment a day late due to a storm related detour and a stop at a gaming casino where he charges and loses \$500 on the debit card. In transit, the BigCo booth and equipment are damaged. Installs gets the display up quickly but BigCo loses the \$20MM sale. As a result, BigCo doesn't pay Installs invoice. Installs doesn't pay Joe.
- BigCo sues Installs for lost profits related to the late delivery and damage to the booth. Does it have a case?
- What about Joe who wants his money for delivery and overtime for having to "work" extra due to the storm?

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Occupation	Statute	Status	Applicability
Traveling salesmen	IRC §3121(d)(3)	Employee	FICA, FUTA
Officers of corporations performing official duties	IRC §3121(d)(1)	Employee	FICA
Real estate agents	IRC §§3121(a)(10), (d)(3)(C)	IC	FICA, FUTA
Direct sellers of consumer products	IRC §§3121(a)(10), (d)(3)(C)	IC	FICA, FUTA
Household workers	IRC §§3306(a)(3), 3401(a)(3), 3121(a)(7)(B), (x)	IC	FUTA, if worker is paid less than \$1000 per calendar quarter and work is performed in private home, college club, sorority or fraternity; FICA and withholding, if worker is paid less than \$1000 per year
Casual labor not in the course of principal's business	IRC §§3121(a)(7)(C), 3401(a)(4)	IC	FICA, if less than \$100 per year is paid; FUTA and withholding, if less than \$50 per quarter is paid
Child of principal under 18	IRC §3121(b)(3)	IC	FICA, FUTA. For withholding requirements, see IRS Circular E
Child of principal 18-21	IRC §3121(b)(3)	Employee	FICA. For withholding requirements, see IRS Circular E
Child of principal 18-21, or spouse	IRC §3306(c)(5)	IC	FUTA. For withholding requirements, see IRS Circular E

IX. FORMS

§3.67 A. Form: Sample Independent Contractor Data Sheet

3.67-1 Independent contractor data sheet

CONTRACTOR DATA

Business name (obtain copy of business card for file):

\_\_\_\_\_

Contractor's name: \_\_\_\_\_

Phone number: \_\_\_\_\_

Fax number: \_\_\_\_\_

Address: \_\_\_\_\_

Social Security or Employer Identification Number: \_\_\_\_\_

\_\_\_\_ Corporation \_\_\_\_ Partnership \_\_\_\_ Sole Proprietorship

Does the contractor hire employees? \_\_\_\_ Yes \_\_\_\_ No  
(If yes, obtain name of workers' compensation carrier and policy number.)

Does the contractor have:

(1) Health insurance? \_\_\_\_ Yes \_\_\_\_ No

(2) Disability insurance? \_\_\_\_ Yes \_\_\_\_ No

(3) A pension or other tax deferred savings plan? \_\_\_\_ Yes  
\_\_\_\_ No

(4) Business liability insurance? \_\_\_\_ Yes \_\_\_\_ No

Names of other customers:

\_\_\_\_\_

\_\_\_\_\_

Does the contractor advertise? \_\_\_\_ Yes \_\_\_\_ No  
(Attach copies of ads if possible.)

Has the contractor worked for this company before?  
\_\_\_\_ Yes \_\_\_\_ No (If yes, projects should be separate and distinct.)

Identify the contractor's special skills and relevant educational background to help establish that he or she did not need instruction or training.

\_\_\_\_\_

\_\_\_\_\_

How many years has the contractor has been an independent contractor? (to help establish that he or she is in a "distinct business") \_\_\_\_\_

Is the contractor actually looking for a position as a regular, permanent employee? \_\_\_\_ Yes \_\_\_\_ No

*Comment:* The form in which the contractor conducts business is very important because a partnership or corporation will help to show that the contractor is "engaged in a distinctive business" (see §3.9). Corporations do not have to be given IRS Form 1099s and are therefore less likely to trigger audits.

When the contractor maintains the insurance coverage noted above, it protects the hiring party and shows that the contractor has made an investment in a distinct business.

Administrative law judges often ask whether the contractor is looking for a position as a regular, permanent employee to distinguish true independent contractors from employees taking freelance work between jobs.



§3.68

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§3.68 B. Form: Sample Agreement Between  
Principal and Independent Contractor

3.68-1 Agreement between principal and independent  
contractor

SERVICES OF CONTRACTOR

Contractor agrees to perform the services described in Exhibit "A" (the "Services") attached to this Agreement.

Contractor will determine the method, details, and means of performing the Services.

Contractor may, at Contractor's own expense, use employees or other subcontractors to perform the Services under this Agreement.

COMPENSATION

Company agrees to pay Contractor   [dollar amount]   for the Services, as set forth below. See Exhibit "A."

Contractor shall be responsible for all expenses incurred in association with the performance of the Services.

TERM OF AGREEMENT

This Agreement will become effective on   [date]  .

This Agreement will terminate on the completion of the Services, unless it is terminated as set forth below. See Exhibit "A."

Either party may terminate this Agreement at any time by giving thirty (30) days' written notice to the other party.

Should either party default in the performance of this Agreement or materially breach any of its provisions, the nonbreaching party may terminate this Agreement by giving written notification to the breaching party. Termination shall be effective immediately on receipt of the notice, or five (5) days from mailing of the notice, whichever occurs first. For the

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purposes of this section, material breach of this Agreement shall include but not be limited to the following:

1. Nonpayment of compensation by Company after twenty (20) days' written demand for payment.

2. Failure of Contractor to comply with the delivery schedule set forth in Exhibit "B."

This Agreement terminates automatically on the occurrence of any of the following events: (a) bankruptcy or insolvency of either party; (b) sale of the business of either party; or (c) death of either party.

RELATIONSHIP OF THE PARTIES

Contractor enters into this agreement as, and shall continue to be, an independent contractor. Under no circumstances shall Contractor look to Company as his/her employer, or as a partner, agent, or principal. Contractor shall not be entitled to any benefits accorded to Company's employees, including workers' compensation, disability insurance, vacation, or sick pay. Contractor shall be responsible for providing, at Contractor's expense, and in Contractor's name, disability, workers' compensation, or other insurance as well as licenses and permits usual or necessary for performing the Services.

Contractor shall pay, when and as due, any and all taxes incurred as a result of Contractor's compensation, including estimated taxes, and shall provide Company with proof of payment on demand. Contractor indemnifies Company for any claims, losses, costs, fees, liabilities, damages, or injuries suffered by Company arising out of Contractor's breach of this section.

Contractor agrees to devote a minimum of   [number]   hours per month to performance of the Services. Consistent with this requirement, Contractor may represent, perform services for, or be employed by any additional persons, or companies as Contractor sees fit.

CONTRACTOR'S REPRESENTATIONS AND INDEMNITIES

Contractor represents that Contractor has the qualifications and ability to perform the Services in a professional manner,

without the advice, control, or supervision of Company. Performance of the Services in a professional manner includes meeting the requirements of the prime contract under which Company is obligated to perform services for the Customer, and failure to do so shall constitute a material breach of this Agreement. Contractor shall be solely responsible for the professional performance of the Services, and shall receive no assistance, direction, or control from Company. Contractor shall have sole discretion and control of Contractor's services and the manner in which they are performed.

Contractor shall and does hereby indemnify, defend, and hold harmless Company, and Company's officers, directors, and shareholders, from and against any and all claims, demands, losses, costs, expenses, obligations, liabilities, damages, recoveries, and deficiencies, including interest, penalties, and reasonable attorney fees and costs, that Company may incur or suffer and that result from, or are related to any breach or failure of Contractor to perform any of the representations, warranties, and agreements contained in this Agreement.

Contractor further agrees to maintain a policy of insurance in the minimum amount of      [dollar amount]      to cover any negligent acts committed by Contractor or Contractor's employees or agents during the performance of the Services.

#### OWNERSHIP OF INTELLECTUAL PROPERTY

Contractor agrees that all designs, plans, reports, specifications, drawings, schematics, prototypes, models, inventions, and all other information and items made during the course of this Agreement and arising from the Services ("New Developments") shall be and are assigned to Company as its sole and exclusive property. On Company's request, Contractor agrees to assist Company, at Company's expense, to obtain patents or copyrights for such New Developments, including the disclosure of all pertinent information and data, the execution of all applications, specifications, oaths, and assignments, and all other instruments and papers that Company shall deem necessary to apply for and to assign or convey to Company, its successors and assigns or nominees, the sole and exclusive right, title, and interest in such New Developments. Contractor agrees to obtain or has obtained written

assurances from its employees and contract personnel of their agreement to these terms with regard to Proprietary Information and New Developments.

Contractor warrants that Contractor has good title to any New Developments, and the right to assign New Developments to Company free of any proprietary rights of any other party or any other encumbrance whatever.

The written, printed, graphic, or electronically recorded materials furnished by Company for use by Contractor are Proprietary Information and the property of Company. Proprietary Information also includes, but is not limited to, specific customer requirements, customer and potential customer lists, including information concerning Company's employees, agents, or divisions, and pricing information.

Contractor will maintain in confidence and will not, directly or indirectly, disclose or use, either during or after the term of this Agreement, any Proprietary Information or confidential information or know-how belonging to Company, whether or not it is in written or permanent form, except to the extent necessary to perform the Services. On termination of Contractor's services to the Company, or at the request of Company before termination, Contractor shall deliver to Company all material in Contractor's possession relating to Company's business. The obligations concerning Proprietary Information extend to information belonging to customers and suppliers of Company about whom Contractor may have gained knowledge as a result of performing the Services.

Contractor shall not, during the term of this Agreement and for a period of two (2) years immediately following the termination of this Agreement, or any extension of it, for any reason, either directly or indirectly: (a) call on, solicit, or take away any of Company's customers or potential customers about whom Contractor became aware as a result of Contractor's Services to the Company, either for Contractor or for any other person or entity; or (b) solicit or take away or attempt to solicit or take away any of Company's employees or contractors either for Contractor or for any other person or entity.

## MISCELLANEOUS PROVISIONS

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The foregoing is agreed to by:

Dated: \_\_\_\_\_ Contractor

Dated: \_\_\_\_\_ Company

*Comments:*

**Purpose:** A major purpose of this agreement is to increase the defensibility of an independent contractor relationship. The absence of a contract may be seen as the absence of the worker's consent to the relationship.

**Drafting party:** Form contracts that are drafted by the principal and not negotiated carry little weight. Consider asking the contractor for a proposed contract.

**Term of Agreement:** As an alternative to the language used above, the agreement could provide that it continues in force for a specific period of time.

**Relationship of parties:** A contract that does not reflect the actual relationship between the parties also will be given little weight. Balance the necessity to limit control with the drawbacks of no control. Do not use the terms, "employ," "employment," "employee," or "employer" in the contract.

**Description of services:** Although the services to be performed can be described in the body of the contract, attaching a description as an exhibit allows the parties a little more flexibility. The description should be written in terms of *the desired end result*; to preserve the independent contractor relationship, the contractor must determine the "method, details, and means" of performing the services.

**Delegation of duties:** If possible, include this clause, because delegation of services is incompatible with employee status.

**Compensation:** As an alternative to the "job rated" arrangement for compensation, the company could compensate the contractor on

an hourly, weekly, or monthly basis. It is also common for the contractor to invoice the company on completion of the project, or at intervals during its progress. Using a flat rate of compensation makes the independent contractor relationship more defensible because the principal is buying an end result rather than the worker's time. Similarly, compensation based on productivity, rather than hours of work or a salary, indicates an independent contractor relationship. Compensation that is set by the principal, rather than mutually negotiated, is evidence of an employer-employee relationship.

**Terms of payment:** Monthly invoicing is more businesslike than weekly billing. However, invoicing should not coincide with the principal's payroll, because that would create the appearance that the contractor was being treated as an employee.

**Conditional payment in three-party relationships:** Having the contractor share the risk of nonpayment by the customer both serves the principal's business needs and makes the relationship more defensible.

**Expenses:** The contractor should bear responsibility for expenses because an employee, not an independent contractor, is more commonly reimbursed for expenses. More significantly, being out of pocket for expenses is a risk of loss that is an indicia of independent contractor status.

**Termination:** Because termination at will is a strong indication of employment, be very specific about the way the relationship can be terminated. However, do not put in so many grounds for termination that the relationship becomes at will.

**Place of work:** If there is a reason why the contractor must work at the principal's place of business, the Agreement should specify that contractor will work there and indicate the reason. Otherwise, administrative agencies will infer that this arrangement is just to allow the principal to exert control.

**Contractor's agreement to indemnify:** Use this provision to both establish a defensible independent contractor relationship and to protect the principal's business interests.

**Ownership of intellectual property:** Do not use the term "work for hire," which implies, and may even create, employment status. See Lab C §3351.5(c); *Community for Creative Non-Violence v Reid* (1989) 490 US 730, 104 L Ed 2d 811, 109 S Ct 2166.

**Miscellaneous provisions:** For standard clauses to include in the contract (e.g., choice of law, survival, force majeure), see Drafting

Business Contracts: Principles, Techniques & Forms, chap 17 (Cal CEB 1994).



## EMPLOYMENT DETERMINATION GUIDE

### Purpose:

This worksheet is to be used by the proprietor of a business to determine whether a worker is most likely an employee or an independent contractor.

### General Information:

Generally speaking, whether a worker is an employee or an independent contractor depends on the application of the factors contained in the California common law of employment and statutory provisions of the California Unemployment Insurance Code.

If a worker is an employee under the common law of employment, the business by which the worker is employed must report the worker's earnings to the Employment Development Department (EDD) and must pay employment taxes on those wages. If the worker is an independent contractor, reporting to EDD is not required. However, if total payments to the independent contractor for the year are equal to or greater than \$600, the business must file a Form 1099 with the Internal Revenue Service (IRS) and the California Franchise Tax Board.

The basic test for determining whether a worker is an independent contractor or an employee is whether the principal has the right to direct and control the manner and means by which the work is performed. When the principal has the "right of control," the worker will be an employee even if the principal never actually exercises the control. If the principal does not have the right of direction and control, the worker will generally be an independent contractor.

If it is not clear from the face of the relationship whether the worker or the principal has the "right of control," reference is made to a list of secondary factors that are evidence of the existence or nonexistence of the right of control.

If use of the attached worksheet clearly demonstrates that a worker is an employee, you should contact EDD and arrange to report the worker and pay the relevant taxes. You may also want to contact the IRS and your workers' compensation insurance carrier to ensure that you are in compliance with federal tax laws and with state workers' compensation statutes.

If after completing the worksheet you are not sure whether the worker is an independent contractor or employee, you may also contact the Employment Tax Customer Service Office (ETCSO) or request a written ruling by completing a Determination of Employment Work Status, DE 1870. The DE 1870 is designed to analyze a working relationship in detail and serves as the basis for a written determination from EDD on employment status. You may also contact the ETCSO nearest you for consultation and advice. The address of the nearest ETCSO can be found in the listing in the "State Government Offices" section of the telephone directory under Employment Development Department.

**WORKSHEET ON EMPLOYMENT STATUS**

Questions 1 through 3 are significant questions. If the answer to any of them is "Yes," it is a strong indication that the worker is an employee, and you have a high probability of risk if you classify the worker as an independent contractor.

1. Do you instruct or supervise the person while he or she is working? Yes \_\_\_\_\_ No \_\_\_\_\_

Independent contractors are free to do jobs in their own way, using specific methods they choose. A person or firm engages an independent contractor for the job's end result. When a worker is required to follow company procedure manuals and/or is given specific instructions on how to perform the work, the worker is normally an employee.

2. Can the worker quit or be discharged (fired) at any time? Yes \_\_\_\_\_ No \_\_\_\_\_

If you have the right to fire the worker without notice, it indicates that you have the right to control the worker.

Independent contractors are engaged to do specific jobs and cannot be fired before the job is complete unless they violate the terms of the contract. They are not free to quit and walk away until the job is complete. For example, if a shoe store owner hires an attorney to review his or her lease, the attorney would get paid only after satisfactory completion of the job.

3. Is the work being performed part of your regular business? Yes \_\_\_\_\_ No \_\_\_\_\_

Work which is a necessary part of the regular trade or business is normally done by employees. For example, a sales clerk is selling shoes in a shoe store. A shoe store owner could not operate without sales clerks to sell shoes. On the other hand, a plumber engaged to fix the pipes in the bathroom of the store is performing a service on a onetime or occasional basis that is not an essential part of the purpose of the business enterprise. A certified public accountant engaged to prepare tax returns and financial statements for the business would also be an example of an independent contractor.

A "No" answer to questions 4 through 6 indicates that the individual is not in a business for themselves and would therefore normally be an employee.

4. Does the worker have a separately established business? Yes \_\_\_\_\_ No \_\_\_\_\_

When individuals hold themselves out to the general public as available to perform services similar to those performed for you, it is evidence that the individuals are operating separately established businesses and would normally be independent contractors. Independent contractors are free to hire employees and assign the work to others in any way they choose. Independent contractors have the authority to fire their employees without your knowledge or consent. Independent contractors can normally advertise their services in newspapers and/or publications, yellow page listings, and/or seek new customers through the use of business cards.

5. Is the worker free to make business decisions which affect his or her ability to profit from the work? Yes \_\_\_\_\_ No \_\_\_\_\_

An individual is normally an independent contractor when he or she is free to make business decisions which impact his or her ability to profit or suffer a loss. This involves real economic risk, not just the risk of not getting paid. These decisions would normally involve the acquisition, use, and/or disposition of equipment, facilities, and stock in trade which are under his or her control. Further examples of the ability to make economic business decisions include the amount and type of advertising for the business, the priority in which assignments are worked, and selection of the types and amounts of insurance coverage for the business.

6. Does the individual have a substantial investment which would subject him or her to a financial risk of loss? Yes \_\_\_\_\_ No \_\_\_\_\_

Independent contractors furnish the tools, equipment, and supplies needed to perform the work. Independent contractors normally have an investment in the items needed to complete their tasks. To the extent necessary for the specific type of business, independent contractors provide their own business facility.

Questions 7 through 13 are additional factors that should be considered. A "Yes" answer to any of the questions is an indication the worker may be an employee, but no one factor by itself is deciding. All factors must be considered and weighed together to determine which type of relationship exists. However, the greater the number of "Yes" answers to questions 7 through 13 the greater the likelihood the worker is performing services as an employee.

7. Do you have employees who do the same type of work? Yes \_\_\_\_\_ No \_\_\_\_\_

If the work being done is basically the same as work that is normally done by your employees, it indicates that the worker is an employee. This applies even if the work is being done on a onetime basis. For instance, to handle an extra workload or replace an employee who is on vacation, a worker is hired to fill in on a temporary basis. This worker is a temporary employee, not an independent contractor.

(Note: If you contract with a temporary agency to provide you with a worker, the worker is normally an employee, but may be an employee of the temporary agency. You may wish to request EDD's Information Sheet, DE 231F, on the subject of temporary service and leasing employers.)

8. Do you furnish the tools, equipment, or supplies used to perform the work? Yes \_\_\_\_\_ No \_\_\_\_\_

Independent business people furnish the tools, equipment, and supplies needed to perform the work. Independent contractors normally have an investment in the items needed to complete their tasks.

9. Is the work considered unskilled or semi-skilled labor? Yes \_\_\_\_\_ No \_\_\_\_\_

The courts and the California Unemployment Insurance Appeals Board have held that workers who are considered unskilled or semi-skilled are the type of workers the law is meant to protect and are generally employees.

10. Do you provide training for the worker? Yes \_\_\_\_\_ No \_\_\_\_\_

In skilled or semi-skilled work, independent contractors usually do not need training. If training is required to do the task, it is an indication that the worker is an employee.

11. Is the worker paid a fixed salary, an hourly wage, or based on a piece rate basis? Yes \_\_\_\_\_ No \_\_\_\_\_

Independent contractors agree to do a job and bill for the service performed. Payments to independent contractors for labor or services are made upon the completion of the project or completion of the performance of specific portions of the project.

12. Did the worker previously perform the same or similar services for you as an employee? Yes \_\_\_\_\_ No \_\_\_\_\_

If the worker previously performed the same or similar services for you as an employee, it is an indication that the individual is still an employee.

13. Does the worker believe that he or she is an employee? Yes \_\_\_\_\_ No \_\_\_\_\_

Although belief of the parties is not controlling, intent of the parties is a factor to consider when making an employment or independent contractor determination. When both the worker and principal believe the worker is an independent contractor, an argument exists to support an independent contractor relationship between the parties.

Interpretations of Answers

Depending on the services being performed and the type of occupation, this questionnaire may produce a variety of results. There may be some factors which lean toward employment and some which lean toward independence. The answers to questions one through six provide a strong indication of the presence or absence of direction and control. The answers to questions seven through thirteen when joined with other evidence may carry greater weight when indicating the presence or absence of direction and control.

1. If all of the answers to questions one through three are "No" and all of the answers to questions four through six are "Yes," there is an indication of independence. When this is the case, there are likely to be a number of "No" answers to questions seven through thirteen which add to the support of the determination.
2. If all of the answers to questions one through three are "Yes" and all of the answers to questions four through six are "No," it is very strong indication that the worker in question is an employee. When this is the case, there are likely to be a number of "Yes" answers to questions seven through thirteen which add to the support of the determination.
3. If the answer to question one or two is "Yes" or the answer to any one of questions four through six is "No," there is a likelihood of employment. At the very least, this pattern of answers makes the determination more difficult since the responses to questions seven through thirteen will probably be mixed. In such situations, the business owner would be well advised to complete a DE 1870, giving all of the facts of the working relationship, and requesting a ruling from EDD.
4. If the answer to question three is "Yes" and the answer to question four is "No," there is a likelihood of employment. Given this pattern of answers, it is probable that the answers to questions five and six will also be "No." When this happens you may also see more "Yes" answers to the last group of questions (seven through thirteen). This scenario would support an employment determination.

These four scenarios illustrate only a few combinations of answers that could result from the use of this Employment Determination Guide, depending on the working relationship a principal may have with a worker, and the type of occupation. The more the pattern of answers vary from the above four situations, the more difficult it is to interpret them. In situations one and two, there is a greater chance that the interpretation will be accurate, and they present the least risk to the business owner of misclassifying the worker. With other combinations of answers, EDD recommends that business owners complete a form DE 1870, giving a complete description of the working relationship and requesting a ruling from the Department.

**NOTE:** Some agent or commission drivers, traveling or city salespeople, homeworkers, artists, authors, and workers in the construction industry are employees by law even if they would otherwise be considered independent contractors under common law. If you are dealing with workers in any of these fields, request the Information Sheet, DE 231SE, from the Employment Tax Customer Service Office.

**SOME EXAMPLES OF INDEPENDENT CONTRACTORS AND COMMON LAW EMPLOYEES**

Independent Contractors

An attorney or accountant who has his or her own office, advertises in the yellow pages of the phone book under "Attorneys" or "Accountants," bills clients by the hour, is engaged by the job or paid an annual retainer, and can hire a substitute to do the work is an example of an independent contractor.

An auto mechanic who has a station license, a resale license, buys the parts necessary for the repairs, sets his or her own prices, collects from the customer, sets his or her own hours and days of work, and owns or rents the shop from a third party is an example of an independent contractor.

Dance instructors who select their own dance routines to teach, locate and rent their own facilities, provide their own sound systems, music and clothing, collect fees from customers, and are free to hire assistants are examples of independent contractors.

A repairperson who owns or rents a shop, advertises the services to the public, furnishes all of the tools, equipment, and supplies necessary to make repairs, sets the price for services, and collects from the customers is an example of an independent contractor.

**NOTE:** Payroll tax audits conducted by EDD have disclosed misclassified workers in virtually every type and size of business. However, certain industries seem more prone to have a higher number of misclassified workers than others. Historically, industries at higher risk of having misclassified workers include businesses that use:

- Construction workers
- Seasonal workers
- Short-term or "casual" workers
- Outside salespersons

Employees

An attorney or accountant who is employed by a firm to handle their legal affairs or financial records, works in an office at the firm's place of business, attends meetings as needed, and the firm bills the clients and pays the attorney or accountant on a regular basis is an example of an employee.

An auto mechanic working in someone's shop who is paid a percentage of the work billed to the customer, where the owner of the shop sets the prices, hours, and days the shop is open, schedules the work, and collects from the customers is an example of an employee.

Dance instructors working in a health club where the club sets hours of work, the routines to be taught and pays the instructors from fees collected from the customers are examples of employees.

A repairperson working in a shop where the owner sets the prices, the hours and days the shop is open, and the repairperson is paid a percentage of the work done is an example of an employee.



REPORT OF INDEPENDENT CONTRACTOR(S)



05420101

See detailed instructions on page 2. Please type or print.

SERVICE-RECIPIENT (BUSINESS OR GOVERNMENT ENTITY):  
 DATE FEDERAL ID NO. CA EMPLOYER ACCOUNT NO. SOCIAL SECURITY NO. NO. OF FORMS NEEDED

SERVICE-RECIPIENT NAME/BUSINESS NAME CONTACT PERSON  
 ADDRESS TELEPHONE NO.  
 CITY STATE ZIP

SERVICE PROVIDER (INDEPENDENT CONTRACTOR):  
 FIRST NAME MI LAST NAME SOCIAL SECURITY NO. STREET NO. STREET NAME UNIT/APPT. CITY STATE ZIP  
 START DATE OF CONTRACT AMOUNT OF CONTRACT CONTRACT EXPIRATION DATE CHECK HERE IF CONTRACT IS ONGOING  
 M M D D Y Y M M D D Y Y

FIRST NAME MI LAST NAME SOCIAL SECURITY NO. STREET NO. STREET NAME UNIT/APPT. CITY STATE ZIP  
 START DATE OF CONTRACT AMOUNT OF CONTRACT CONTRACT EXPIRATION DATE CHECK HERE IF CONTRACT IS ONGOING  
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DE 542 Rev. 2 (2-04) (INTERNET) MAIL TO: Employment Development Department • P.O. Box 937350, SAC 96 • Sacramento, CA 95899-7350 or Fax to (916) 319-4410 Page 1 of 2 CU

INSTRUCTIONS FOR COMPLETING THE REPORT OF INDEPENDENT CONTRACTOR(S)

WHO MUST REPORT:

Any business or government entity (defined as a "Service-Recipient") that is required to file a Federal Form 1099-MISC for service performed by an independent contractor (defined as a "Service-Provider") must report. You must report to the Employment Development Department within twenty (20) days of EITHER making payments of \$600 or more OR entering into a contract for \$600 or more with an independent contractor in any calendar year, whichever is earlier. This information is used to assist state and county agencies in locating parents who are delinquent in their child support obligations.

An independent contractor is further defined as an individual who is not an employee of the business or government entity for California purposes and who receives compensation or executes a contract for services performed for that business or government entity either in or outside of California. For further clarification, request *Information Sheet: Employment Work Status Determination (DE 231ES)*. See below for additional information on how to obtain forms.

YOU ARE REQUIRED TO PROVIDE THE FOLLOWING INFORMATION THAT APPLIES:

Service-Recipient (Business or Government Entity):

- Federal employer identification number
- California employer account number
- Social security number
- Service-recipient name/business name, address, and telephone number

Service-Provider (Independent Contractor):

- First name, middle initial, and last name
- Social security number
- Address
- Start date of contract (if no contract, date payments equal \$800 or more)
- Amount of contract including cents (if applicable)
- Contract expiration date (if applicable)
- Ongoing contract (check box if applicable)

HOW TO COMPLETE THIS FORM:

If you use a typewriter or printer, ignore the boxes and type in UPPER CASE as shown. Do not use commas or periods.

FIRST NAME	MI	LAST NAME	STREET NO.	STREET NAME	UNIT/APPT.
IMOGENE		A SAMPLE	12345	MAIN STREET	301
SOCIAL SECURITY NO.					
123456789					

If you **handwrite** this form, print each letter or number in a separate box as shown. Do not use commas or periods.

FIRST NAME	MI	LAST NAME	STREET NO.	STREET NAME	UNIT/APPT.
I M O G E N E	A	S A M P L E	1 2 3 4 5	M A I N S T R E E T	3 0 1
SOCIAL SECURITY NO.					
1 2 3 4 5 6 7 8 9					

GENERAL INFORMATION:

If you have any questions concerning this reporting requirement, please call (916) 657-0529. You may also contact your local Employment Tax Customer Service Office listed in your telephone directory in the State Government section under "Employment Development Department." Or you may access our Internet site at [www.edd.ca.gov](http://www.edd.ca.gov).

To obtain additional DE 542 forms:

- Enter number of forms needed in upper right hand corner on front of form; or
- Visit our Internet site at [www.edd.ca.gov](http://www.edd.ca.gov); or
- For 25 or more forms, telephone (916) 322-2835
- For less than 25 forms, telephone (916) 657-0529

To obtain information for submitting *Report of Independent Contractors* on magnetic media, call (916) 651-6945.

HOW TO REPORT:

Please record the information in the spaces provided and mail to the following address or fax to (916) 319-4410.

EMPLOYMENT DEVELOPMENT DEPARTMENT  
 P. O. Box 937350, Document Management Group, MIC 96  
 Sacramento, CA 95899-7350



How Six Agencies Determine Independent Contractor-Employee Relationships

	IRS	EDD/FTB	INS	Workers' Comp.	US Dept. of Labor	CA Labor Comm.
No right to control worker	◆	◆	◆	◆	*	◆
No instructions	*					
No training	*					
Assistants can do work	*	●				
Work not hiring firm's primary business	*	*	*	*	*	*
No set work hours	*	●				
Not a continuing relationship	*	*	*	*	*	*
Control assistants	*		*	*		*
Time to work for others	*	●				
Determine job location	*	●	*	*		*
Set order of work	*					
No interim reports	*					
Paid by job	*	*	*	*		*
Work for many companies	*					
Pay own expenses	*					
Have own tools	*	*	*	*		*
Made significant investment	*		*		*	
Offer services to public	*					
Can make profit or loss	*		*		*	
Can't be fired at will	*	◆	*	*		*
Aren't paid for partial work	*					
Distinct occupation or operate separate business		*	*	*		*
Part of industry practice		*				
Skill required		*	*	*		*
Work typically non-supervised		*	*	*		*
Parties believe worker is independent contractor		*	*	*		*
Who hired the worker		*				
Amount of initiative, judgment or foresight needed to succeed					*	

Legend: ◆ Most important factor    \* Important factor    ● Lesser factor

CONTINGENT WORKERS - #311

Additional Reference Materials

TREATISES:

*Advising California Employers and Employees*, Continuing Education of the Bar, Ch. 3, Vol. 1, pp. 207-276 (2008) [Library of Congress Control No. 2005937887] [ISBN 978-0-7626-1338-0]; Go to www.CEB.com.

*Labor Law Digest*; California Chamber of Commerce, (2008); Go to www.calchamberstore.com.

*EEOC: Enforcement Guidance on Contingent Workers*, [BNA 450:7551]

LAW REVIEW ARTICLES

*Why The Law Still Can't Tell An Employee When It Sees One And How It Ought To Stop Trying*, 22 Berkeley J. Emp. & Lab. L. 295 (2001) – Discusses Darden, Viscaino & other cases.

*Legal Protection for Atypical Employees: Employment Law for Workers Without Worker places and Employees Without Employees*, 27 Berkeley J. Emp. & Lab. L. 251 (2006)

CASES

Workers' Compensation

S.G. Borello & Sons, Inc. v. WCAB; 48 Cal. 3d 341 (1989) (Share farmers were employees due to retention of control by contracting entity – established purpose of statute is a consideration along with common law and economic realities factors)

Caso v. Nimrod Productions, Inc., 163 Cal. App. 4th 881, 77 Cal Rptr. 3d 313 (2008) (stuntman deemed covered by workers' compensation notwithstanding contract agreement, "Special employee" status as work was part of contracting business activity; production company controlled work & supplied instrumentalities used to perform the work).

Kowalski v. Shell Oil Co., 23 Cal 3d 168 (1979) (Scaffold workers not special employee of refinery as no direct control over duties established.)

Assicurazioni General v. Pipeline Valve et al., 935 F. Supp. 879 (SD Tex 1996) (Insurance coverage case analyzing whether leased employee could bring an action against borrowing employer outside of workers compensation - NO).

#### Discrimination Laws

Mathieu v. Norell Corp., 115 Cal. App. 4th 1174, 10 Cal. Rptr. 3d 52 (2004) (FEHA protects both employees and special employee from harassment, discrimination and retaliation by special/joint employers)

Mitchell v. Frank Howard Memorial Hospital, et al., 853 F.2d 762 (9th Cir 1988) (Hospital radiologist established employment relationship for purposes of Title VII)

Walters v. Metropolitan Education Enterprises, 519 U.S. 202 (1997) (Special or leased employees and temporary employees count towards establishing threshold coverage of Title VII/ADEA).

Thimber v. Jack Reilly's Inc., 717 F. 2d 633 (1st Cir. 1983) (part-time employees count toward coverage threshold of ADEA/Title VII).

Zimmerman v. North American Signal Co., 704 F.2d 347 (7th Cir. 1983) (Directors, unpaid volunteers, and low inactive officers are not "employed" for prepared of Title VII.)

Moreau v. Air France, 356 F. 3d 842 (9th Cir. 2003) (joint employer status measured by totality of circumstance, i.e. an economic realities/hybrid analysis, for purposes of FMLA). See also 29 CFR 825.106(d) noting that employees of joint employers count towards FMLA thresholds and eligibility.

Amarnare v. Merrill Lynch, 611 F. Supp. 344 (SD NY 1984) (Leased employee covered by Title VII – worked two weeks then termed as unsatisfactory – race claim allowed to go forward under economic realities test but same result under Darden as Merrill exercises substantial control over Plaintiff's work.)

U.S. EEOC et al. v. Custom Companies, Inc. et al., 2007 U.S. Dist. Lexis 16691 (ND IL 2007) (leased employees count towards Title VII minimums)

#### NRLA

Todd v. Benal Concrete, 710 F.2d 581 (9th Cir. 1983) Common law that applied to conclude independent contractor status, then trust find welfare payments not req'd).

NLRB v. Browning Ferris, 691 F. 2d 1117 (3rd cir. 1982) (joint employment relationship found and therefore joint employer liable for unfair labor practices and retaliation due to protected activity)

Holyoke Visiting Nurses Assn. et al. v. NLRB, 11 F. 3d 301 (1st Cir 1993) (same)

California Oilfield Maintenance, Inc., 311 NLRB 1079 (1993) (refusal to bargain with workers subsequently found to be employees may create liability for ULP)

So. Cal. Gas Co., 302 NLRB 456, 461 (1991) (applying common law test to find joint employment)

International Shipping Ass'n, Inc., 297 N:RB 1059, 1067 (1990) (same)

#### FLSA

Real v. Driscoll, 603 F.2d 748 (9th Cir. 1979) (Strawberry harvest workers found to be independent contractor under FLSA – cited Rutherford Food Corp v. McComb, 331 US 772. 730 (1947))

But see Borello, *supra*, when opposite result reached for Workers' Compensation under expanded statutory purpose issue.

See also 29 CFR 791.2(a) noting that joint employers are jointly and severally liable for FLSA compliance.

#### Unemployment Insurance Benefits/Social Security Taxes

Santa Cruz Transportation, Inc. v. Unemployment Insurance Appeals Board (Gallegos), 235 Cal. App. 3d 1363 (1991) (Taxi driver deemed employee eligible for state disability benefits despite existence of cab leasing/independent operator agreement because cab co. exercised significant control).

Leasing employers generally responsible for UI taxes and contributions if statutory criteria met, See Cal. Un. Ins. Code § 606.5

Leasing employers primarily responsible for FWT and FICA/OASDI withholding but borrowing employer can be jointly liable. See IRC § 3121 et seq.

IRS generally determines employee status under a 20 factor test (now 3 areas and 17 subcriteria); See Rev. Rul. 87-41.

#### Copyright

Community for Creative Non-Violence v. Reid, 490 U.S. 730 (1989) (Sculptor engaged to design a sculpture under a so called 'work for hire' agreement; under

common law test and he was deemed contractor and so retained ownership of design) [sets forth common law test for employee status].

#### FLSA/Wage & Hour

Rutherford Food Corp. et al. v. McComb, 331 U.S. 722 (1947) (“Boners” working at a slaughter house under a contract basis were “employees” eligible for OT).

Reynolds v. Bemet, 36 Cal. App. 4<sup>th</sup> 1075 (2005) (Office director acting within scope of agency not individually liable for corporate failure to pay wages/OT due).

#### Fed/OSHA

Griffin and Brand of McAllen, Inc., 1978 OSAHRC Lexis 15, 6 OSHC (BNA) 1702 1978 (Melon harvesters deemed “employees” under OSHA and therefore “Shipper” employer could be cited for violations).

#### ERISA

Nationwide Mutual Insurance Co. v. Darden, 503 U.S. 318 (1992) (establishes common law test for analyzing employment status and vesting rights under ERISA covered pensions) [reiterates common law test for employee status].

Simpson v. Ernest & Young, 850 F. Supp 648 (1994) (non-equal partners deemed employee of one other).

Viscaino v. Microsoft, 120 F3d 1006 (9<sup>th</sup> Cir. 1997) (contract application developers and other computer designers are common law employees).

Burrey v. PG&E, 159 F. 3d 388 (9<sup>th</sup> Cir. 1998) (Leased clerical employees had standing to sue under certain benefit plans if they were common law employees, a determination which is to be reached first under IRC 414(n) and other provisions of ERISA)

Wolf v. Coca Cola Company, 200 F. 3d. 1337 (11<sup>th</sup> Cir. 2000) (computer programmer hired under IC agreement with third party services provider had colorable claim to common law employee status but was ineligible for benefits under definition of “employee” under the applicable plan).

Rheem Mfg. Co. v. Central States Southeast and Southwest Areas Pension Fund, 63 F. 3d 703 (1995) (Mfgr. not liable for multi employer pension withdrawal penalties associated with its use of ‘leased’ drivers for delivery of its products)