Latest Thinking

New Challenges to Independent Contractor Classifications

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The use of independent contractors has been a staple of many companies' staffing models for years. These workplace arrangements are facing renewed scrutiny from government agencies and the courts.[1] Two recent decisions involving the transportation industry highlight the perils of these tenuous classifications, which offer a cautionary tale that extends beyond this particular industry.

Businesses in the transportation industry frequently engage drivers whom they consider to be independent contractors to provide trucking or livery services. By using drivers who own their vehicles and operate their own companies, transportation businesses often lower their capital requirements. Furthermore, independent contractors frequently provide their services at a cost lower than the cost the wages and benefits of an employee workforce. Such businesses also avoid the regulatory and litigation burdens that come with coverage of workers under employment statutes.

Transportation businesses also face certain risks from using drivers who are independent contractors. For example, such drivers typically have the ability to work for multiple customers in the same industry, to accept or decline work requests at will and to choose their own hours. Different businesses may come to different conclusions in weighing these risks against the rewards described above.

In this month's column, we analyze two recent cases where transportation businesses suffered unexpected losses when groups of drivers asserted that they were misclassified as independent contractors. First, in *O'Connor v. Uber Technologies, Inc.*, 2015 WL 5138097, at *1 (N.D. Cal. Sept. 1, 2015) a proposed class of drivers claimed that they were employees and owed gratuities and expenses under the California Labor Code. The court certified the case as a class action. Second, in *Fedex Home Delivery & Int'l Bhd. of Teamsters, Local Union No. 671,* 361 NLRB No. 55, at *1 (Sept. 30, 2014) a group of FedEx drivers argued to the National Labor Relations Board ("NLRB") that that they were employees under the National Labor Relations Act ("NLRA") with the right to unionize. The NLRB accepted the drivers' argument and departed from the D.C. Circuit's opinion in a prior case that reached the opposite result. *Id.* at *22.

After we analyze these decisions, we will then propose several prophylactic measures businesses may consider in an effort to avoid the misclassification of drivers thought to be independent contractors.

Background

Various federal and state laws apply to workers considered "employees" but not to workers classified as "independent contractors." In responding to a continuing stream of misclassification cases over many decades, courts and administrative agencies have devised a

series of legal tests they use to determine whether particular workers are “employees” under the law.

Courts and agencies emphasize various factors in implementing these legal tests under different employment statutes. We do not attempt to summarize all of these legal tests here. However, one common theme of these tests is the significant emphasis placed on the putative employer’s control over terms and conditions of the workers’ engagement. Courts and agencies have often looked to the Restatement (Second) of Agency § 220 (1958) to identify the factors relevant to assessing the putative employer’s control over the terms and conditions of the workers’ engagement. The Restatement identifies inquiries such as whether payment is by time or task, whether the job requires skill, the duration of the working relationship, who supplies the equipment, tools, and location, whether the worker operates a distinct business, if that business is the employer’s regular business, and how the parties view their relationship.

We will refer to the factors enumerated in the Restatement as the “control” factors. State courts, federal courts, and administrative agencies use various formulations of the control factors to assess the classification of workers under the various employment laws.

Uber Drivers

The *Uber* case illustrates how courts in California applying state law will conduct a two-part inquiry in determining whether workers are employees or independent contractors. First, they will focus on the employer’s “right to control work details.” *Id.* at *5. Then, they will assess “secondary indicia of control,” such as “the skill required” for the position, “the length of time employed,” whether the work is usually performed by a specialist without supervision in that locality, and the other factors articulated in the Restatement. *Id.* at *6.

The court's application of this test to Uber's drivers first requires an understanding of Uber's business. Uber allows customers to log into a software application on their smartphone and request rides from available drivers, whom Uber considers to be independent contractors. Individual drivers sued Uber, claiming that Uber owed them and a class of similarly situated drivers gratuities and work-related expenses under California Labor Code § 351 and § 2208. *See id.* at *1. They alleged that Uber failed to reimburse their expenditures and losses incurred directly in performing work duties.[2] *See id.* They also alleged that though Uber advertised to customers that a tip is included in the cost of the fare, it failed to remit the entire amount of tips or gratuities that patrons left for drivers. *Id.*

In determining whether the misclassification issue was suitable for class treatment, the court analyzed each of the California control factors. The court first inquired into whether an employer uniformly retained *"rights* to control with regard to [an employer's] various hires," and not whether it exercised that control uniformly. *See id.* at *16. Consequently, the court rejected Uber's arguments that its training requirements or "suggestions" to drivers varied sufficiently to preclude class certification, because the *right* to control remained consistent. *Id.* at *19. The court also found that Uber's right to terminate drivers without cause could be ascertained on a class-wide basis despite seventeen different versions of driver contracts, because all provided that drivers were employees at will, a factor weighing in favor of employee status. *Id.* at *20. Moreover, Uber's statements that it exercised no control over any driver's schedules or routes meant that those issues uniformly applied to the proposed class. *Id.* at *17. The court also noted that Uber's position that its treatment of drivers varied was inconsistent with its argument on the merits that it properly classified "*every single driver*" as an independent contractor. *Id.* at *2.

Uber put forth other arguments on the secondary indicia of control required under the California law, but the court similarly found that whether they weighed for or against an independent

contractor relationship, they were suitable for class certification. For example, all drivers worked for an indefinite duration, supplied their own cars, had the same opportunity to maximize profits based on managerial skill, all favoring a classification of independent contractor. *Id.* at *22-*28. But the court found that uniformity enabled it to analyze the merits with respect to the entire class. *Id.* The court also rejected Uber's argument that mandating higher prices at times of high demand to entice more drivers to accept jobs was "negotiation," rather than a unilateral decision regarding compensation applicable to all drivers. *Id.* at *17. After considering the relevant control factors, the court certified for class adjudication the question of independent contractor misclassification. *Id.* at *37.

The court next determined whether plaintiffs' tips claim under California Labor Code § 351 could be adjudicated on a class-wide basis. *Id.* at *30. California Labor Code § 351 requires an employer who "collect[s], take[s], or receive[s] any gratuity or [] part thereof" to remit that amount to the employee. Uber represented to customers that a tip is included in the price of the fare, but of its own admission, never remitted that amount to drivers. *Uber,* 2015 WL 5138097, at *31. The court found that if the drivers are employees, then Uber would be liable for unremitted gratuities. *Id.* at *32. Therefore, the court certified the tips claim as a class action as well. *Id.*

FedEx Drivers

By contrast to *Uber*, when the NLRB applied the control factors under the NLRA, it applied all the factors with equal weight. *See Fedex Home Delivery,* 361 NLRB No. 55, at *14 (Sept. 30, 2014). In *Fedex,* the NLRB brought a claim against FedEx for refusing to collectively bargain with its drivers' certified elected representative under NLRA § 8(a)(1) and (5). *Id.* at *1. FedEx argued that the drivers were independent contractors, not employees, and consequently it was not obligated to collectively bargain with the union under the NLRA. *Id*. To decide whether

FedEx's classification was correct, the NLRB applied the common law control factors as articulated in the Restatement. *Id.* at *2.

The NLRB analyzed all of the control factors in Restatement of Agency and concluded that the employer controlled the drivers' work conditions. *Id.* The NLRB explained that FedEx determined work hours, routes, and number of packages delivered. *Id.* at *18. It also found that the drivers' FedEx uniforms, the mandatory logo on their vehicles, and their use of FedEx's scanner system to log and track package deliveries meant that the drivers "[did] business in the name of FedEx rather than their own." *Id.* Other indicia of employer control included audits to ensure that drivers complied with FedEx policy "governing dress, appearance, safety, and the details of package delivery," and the use of contracts with automatic renewal, creating indefinite terms of employment. *Id.*

In analyzing whether the evidence showed that the drivers render services as an independent business, the NLRB stated that though drivers could theoretically sell their routes, hire helpers and employ additional drivers, any "possibility for meaningful economic gain" was limited, because FedEx "retain[ed] the right to curtail or reconfigure" routes, and "exercise[d] considerable control over whether a driver may sell [routes] at all, to whom, and under what circumstances." *Id.* at *19-*20. The NLRB noted that the driver's scheduling arrangement "effectively prevent[ed] them from working for other employers," and found no evidence that any employee had used their vehicle for other commercial purposes. *Id.* at *21.

The NLRB rejected the D.C. Circuit's opinion in *FedEx Home Delivery v. N.L.R.B.,* 563 F.3d 492, 497 (D.C. Cir. 2009), a case involving the status of drivers "performing the same job at two FedEx Home Delivery facilities" in another location. 361 NLRB No. 55, at *1. In that case, the D.C. Circuit found that FedEx drivers were independent contractors by applying the control factors differently. *FedEx,* 563 F.3d at 497. The D.C. Circuit distanced itself from the "unwieldy

control factors," and emphasized just one: "whether the position presents the opportunities and risks inherent in entrepreneurism," or "entrepreneurial opportunity." *Id.* It noted that FedEx did not "prescribe hours or work, whether or when the contractors take breaks, what routes they follow or other details of performance," and that the drivers provided their own vehicles. *Id.* at 498. The court found that drivers had "entrepreneurial opportunity" because they could theoretically, "remove or mask all FedEx logos or markings" to work for another company, "assign at law their contractual rights to their routes without FedEx's permission," or hire their own subcontractors to perform their duties. *Id.* at 498-99, 500.

In analyzing the "entrepreneurial opportunity" factor, the D.C. Circuit focused on "opportunity," not whether drivers actually engaged in entrepreneurial activity. *Id.* Even "one instance" of a driver using an opportunity to engage in entrepreneurial pursuits would be sufficient to classify similarly situated drivers as independent contractors, according to the D.C. Circuit. *Id.* at 502.

Practice Pointers

To avoid the pitfalls experienced by Uber and Fedex, transportation businesses that wish to engage drivers as independent contractors should consider taking steps to minimize the risk of liability under the federal or state employment laws as follows:

- Perform an internal review of the classification of drivers as independent contractors to ensure that the terms and conditions of the engagement would withstand scrutiny under the applicable state or federal employment laws;
- Consider allowing drivers flexibility over their schedules, routes, and which jobs to take.
- Consider allowing drivers to work for other businesses or customers, and to use their vehicles for other jobs, so as to establish that the drivers are faced with the "risks and opportunities inherent in entrepreneurism."

To the extent possible, negotiate contracts individually with each driver and avoid “one-size-fits all” contracts which drivers may argue gives them the right to litigate their employment status as a class.

Consider including arbitration clauses which specify that all litigation by the driver will be asserted individually, and not in connection with any class action.

[1] *See e.g. Misclassification Initiative,* Dep’t of Labor, *http://www.dol.gov/whd/workers/misclassification* (last visited Sep. 29, 2015); Robert W. Wood, *FedEx Settles Independent Contractor Mislabeling Case For $228 Million*, Forbes, (Jun. 16, 2015, 8:39 A.M.), http://www.forbes.com/sites/robertwood/2015/06/16/fedex-settles-driver-mislabeling-case-for-228-million/

[2] The court found that the class representative was inadequate with regard to expense reimbursement claims, and did not certify that claim for class treatment. We will not discuss that claim here.