Legal Requirements That Influence Control of Independent Contractors and Employees

By Robert W. Wood

Is a worker an independent contractor or an employee? The distinction is important under federal, state and local tax laws. It affects contract and tort liability exposure, and raises federal and state labor law compliance issues. Plus, it can impact insurance, employee benefits and myriad other issues.

Worker classification is not determined merely by labels. Various government agencies and the courts can make their own assessment of who is an employee. In appropriate cases, the government can retroactively recharacterize workers, so the stakes can be huge. The courts have long been divided on how to define and interpret these rules. Even today, there is no single test for determining worker status.

The Internal Revenue Service and a variety of state and federal agencies make determinations as to worker status, so a worker may be classified as an employee for one purpose and as an independent contractor for another. Quite apart from tax status, workers classified as employees have rights under federal labor and employment laws. Consequently, issues of statutory coverage and liability may turn on whether a person is found to be an employee.

Gradients of Control

Although tests for assessing worker status have differing formulations, the tighter the company's right to control the worker, the more likely the worker will be considered an employee. Most of the classification methodologies also evaluate the degree to which the worker is integrated into the company's operations, the worker's special skills, the longevity of the relationship, the company's ability to terminate the relationship, and so on. These and other factors are used as earmarks of employment.

A court or agency must determine the worker's true status by evaluating the governing contract and business records. If the worker is micro-managed and subject to the employer's unfettered control, an "independent contractor" label in a contract will probably not save the worker from being recast as an employee.

Legal Requirements

Worker classification is a fact-intensive determination. Because virtually everything is relevant in making the determination, legal and regulatory requirements impacting the working relationship must also be considered.

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For example: a trucking company mandates that its drivers may drive only up to a maximum of eight consecutive hours before taking a required rest. This rule may appear to indicate employer control, which, along with myriad other contract provisions, rules and practices, is relevant in assessing whether the putative employer has exercised (or reserved the *right* to exercise) sufficient control to dictate employee status. If, however, the eight-hour driving maximum emanates from federal or state transportation rules, can this requirement fairly be seen as indicative of company control? In the few cases to consider such a point, the answer appears to be no.

Of course, employers may subject their workers to requirements *exceeding* prescribed regulations. For example, suppose an employer requires workers to check in with the company not less than once every 24 hours because federal or state law imposes such a requirement. Suppose, then, that the applicable law changes to require workers to check in only once every 48 hours. If the employer is ignorant of this change and continues to require 24-hour check in, should this enhanced level of "control" be considered in assessing the worker relationship?

Further, does it matter if the employer exercised due diligence in attempting to keep itself abreast of such legal and regulatory changes? Does it matter if the worker's status is being examined two weeks or five years after the pertinent legal change was made? The answers to these questions are important and, to some degree, subjective. A degree of employer rule-making beyond bare legal requirements should not necessarily constitute sufficient control to characterize the worker as an employee. Nuance is important.

Case Law and Legal Control

Although one may think first of IRS involvement in worker status controversies, it does not appear that the "legal control" issue has been expressly discussed in tax cases. It has, however, come up in federal labor and employment law decisions. For example, in *National Labor Relations Board v. Associated Diamond Cabs, Inc.*,[1] the court was asked to determine whether Miami taxi drivers were independent contractors or employees. The issue hinged on city of Miami regulations that required taxi drivers to fill out "trip sheets" to record all trips, their origins and destinations, fares charged and the time of each trip. At the end of each day, drivers submitted their trip sheets to the company, which were retained for city inspection. The court found that such trip sheets did not evidence control by the company. In fact, the regulations constituted supervision not by the employer, but by the city. The *law* controlled the driver, not the *employer*. As a result, the court found that the regulations failed to evidence control by the company.

Similarly, in *K&D Auto Body, Inc. v. Division of Employment Security*,[2] the court considered federal drug-testing laws and worker classification. K&D required its drivers to sign agreements affirming their independent contractor status, but Missouri found the drivers to be employees, because K&D could require drivers to take random drug tests. Addressing the issue of the drug tests, the appellate court ruled that the company had not required more from its workers than the law required. Thus, the drug tests could not be considered employer control. However, as the *remaining* factors demonstrated an employer/employee relationship, the court held the truck drivers to be employees.

In *Air Transit v. National Labor Relations Board*,[3] a cab company sought reversal of an NLRB decision ruling its cab drivers to be employees. Air Transit was a Virginia corporation; the Federal Aviation Administration (FAA) gave Air Transit the exclusive right to operate taxicab services at Dulles Airport. Air Transit used the services of approximately 100 taxicab drivers who provided their own vehicles and picked up passengers from a designated cab line. It put a uniformed dispatcher at the head of the line to direct passengers and help with their luggage. Air Transit charged drivers $72 a week for participation in the feed line but received no share of the drivers' earnings.

The drivers did not report their earnings to Air Transit; did not keep trip sheets, manifests or other accounts of their earnings; and had control over their own schedules. Drivers received no benefits, vacation time, sick leave, workers' compensation or unemployment insurance from Air Transit. All drivers were personally responsible for their own accounting and self-employment taxes, and received no training.

Air Transit drivers were subject to many rules, however, some of which were mandated by Air Transit's contract with the FAA and some required by Virginia law. Drivers had to use a radio dispatch system, wear name tags, maintain taxicabs in safe operating condition, display the words "Airport Cab" and Air Transit's telephone number on the taxicab, display rate information, possess a valid chauffeur's license and license their vehicles for use in Louden County, Virginia. Air Transit also enforced rules that were not provided by the FAA contract or Virginia law, including requirements that drivers charge a flat rate for certain customers, post a notice in their vehicles about how to file a passenger complaint and purchase greater insurance coverage than required by Virginia law.

While the NLRB claimed that such controls meant that the cab drivers were employees, the appeals court ruled the drivers were independent contractors. The few employee-like factors were grossly outweighed by factors suggesting the drivers were independent contractors. Although Air Transit exercised *some* control over the drivers, beyond the legal regulations, it was insufficient to find the drivers to be employees. Most of the "controls" were mandated by the FAA contract or by Virginia law.

More Case Law on Legal Controls

Taxicab companies seem to feature prominently in the "legal control" cases. For example, *Local 777, Democratic Union Organizing Committee v. NLRB*[4] involved two cab companies providing taxicab service in Chicago. The NLRB ruled the cab drivers were employees.[5] The court reversed, finding the facts insufficient to support employee status.

Each cab driver signed a lease under which the driver paid a fixed fee ($22 for a day lease and $15 for a night lease), in addition to an hourly fee for late returns. The driver leased the cab for two days at a time, or three days on weekends. The driver agreed to be the sole driver, not to sublease the cab, to inspect it at the beginning of the lease and report defects, and to return the cab in good condition with a full tank of gas. The company provided the taxicab, the cab license, liability insurance, antifreeze, oil, towing service, tires, and maintenance. The lease said the drivers were not required to operate taxicabs in a prescribed manner, accept calls or dispatches, report their location, buy gas from the company or keep the cab in a designated location.

The drivers were required to comply with all applicable laws, ordinances, rules and regulations. Chicago municipal regulations and state law governing taxicab drivers required that taxicabs be operated regularly to meet public demand for service, the meter flag be kept down when the cab was carrying passengers and everyone requesting a ride be picked up unless the cab was occupied. The municipal code established fare rates, prohibited passengers in the front seat and prohibited refusing to transport passengers from the airport to the suburbs. Municipal regulations set rules for courtesy to passengers, driver appearance and attire, and driver conduct at cab lines. Drivers could not use drugs, carry weapons, loiter in public outside their cabs, leave their cabs unattended or violate traffic laws.

Driver conduct was never controlled by the cab companies. Drivers were on their own once they left the garage and were free to prospect for fares in any manner. The only requirements the cab company enforced were the daily rate for the cab, care and skill in driving, and compliance with applicable laws and regulations. The court found that compliance with the law could not be deemed control by the employer and ruled the drivers to be independent contractors.

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In *SIDA of Hawaii, Inc. v. NLRB*,[6] a company of independent taxicab owner-operators argued that its members were independent contractors. SIDA was a self-governing trade association, providing a collective body of independent drivers to compete with larger taxi companies in bidding for the right to operate at Honolulu airport. SIDA had an exclusive contract to provide taxi service at the airport. An applicant qualified to be a member of SIDA by owning a suitable vehicle, having a valid license, and having an acceptable personal appearance. If the applicant was approved, he or she signed a Standard Independent Drivers Contract with SIDA.

The court found an absence of actual control by SIDA for the following reasons: (1) drivers made substantial personal investments in their taxicab activities, purchasing and maintaining their own vehicles; (2) drivers obtained all necessary city and state permits; (3) drivers paid their own income taxes, health insurance, Social Security, unemployment benefits and auto insurance; (4) drivers paid a monthly stall rental fee to SIDA, along with a $0.50 trip fee for each trip made out of the airport; (5) drivers were substantially independent in their operations and were free to work independent of SIDA; (6) drivers could work for other cab companies, could make their own arrangements with clients and were not limited to operate in a particular area; (7) fares were not determined by SIDA but by local ordinances, and were collected and retained by the drivers; (8) SIDA did not pay compensation to the drivers, did not withhold taxes and kept no income tax records for them; and (9) drivers' contracts specifically provided for an independent contractor relationship.

The NLRB argued that SIDA's rules, regulations and enforcement were strong evidence of the company's control over the drivers. The court disagreed. Many of SIDA's regulations merely incorporated requirements imposed by its commercial contracts and state and local ordinances. Thus, the court found the owner-operators to be independent contractors.

Legal and Community Standards

Meyer Dairy, Inc. v. NLRB,[7] which involved the status of milk distributors as independent contractors or employees, puts a particular spin on the existence of compliance with laws. Meyer Dairy Distributors Association (the "Association") was a group of milk distributors who peti-

tioned the NLRB to bargain with its putative employer, Meyer Dairy Company (the "Company").[8] The Company countered that Association members were independent contractors. The NLRB found the Association members (the "Distributors") to be employees, and the Company appealed to the Tenth Circuit.

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The Meyer Dairy Company contracted with retail distributors who agreed to purchase the Company's dairy products at fixed prices and sell the products to customers in specified areas. The Distributors, or "milk men," delivered dairy products to customers over fixed routes. They provided their own trucks for delivery, paid all costs and expenses of operation, and could hire helpers if needed. The Company provided Distributors with suggested retail prices, but they were not required to adhere to them. The Distributors' contract required that they comply with regulations and policies of public health authorities, and meet standards established by the Company, consistent with similar dairy businesses in the Greater Kansas City area.

Distributors had no other obligations to the Company except to pay for the products they purchased. They had complete control over their sales and decisions regarding credit, were responsible for losses from retail sales, paid their own income and Social Security taxes, controlled their vacations, and provided their own self-retirement plans or medical and liability insurance. The Distributors were essentially holders of franchises to sell Meyer Dairy products within a specified area. They were not controlled by the Company except to maintain certain standards required by state law; thus the court found they were independent contractors.

Similar issues arose in *Global Home Care, Inc. v. State, Department of Labor & Employment Security*,[9] which concerned the status of live-in health care aides. The Florida Department of Labor and Employment Security ruled that the aides were employees, and Global appealed. The Florida Court of Appeal reversed, saying that Global's lack of control over the aides rendered them independent contractors. Notably, the court held Global's insistence on compliance with state regulations did not constitute supervision of the aides.

The aides were independent contractors because they worked for other agencies and at sites away from company supervision, and the clients provided materials and a work place. The aides were engaged only as needed on a temporary, per-job basis, and both parties intended an independent contractor relationship. Moreover, the majority of the control Global exercised over its aides was to assure compliance with state requirements for home health care. Other aspects of control were deemed too minimal to be significant.

Control in Excess of Regulations

In *Associated Diamond*, *Air Transit, Local 777*, *SIDA of Hawaii*, *Meyer Dairy*, and *Global Home Care*, the employers did not wield control significantly in excess of pertinent regulations. They merely imposed standards following federal or municipal regulations. In contrast, in *K&D Auto Body* the control went well beyond compliance with law. The results suggest that for workers to be reclassified as employees, an employer must wield pervasive control exceeding to a significant degree the scope of the government-imposed control.

The courts in these cases recognized that compliance with laws adds complexity to the worker status mix. They take a reasoned, realistic view of the amount by which a putative employer must exceed legal requirements. An employer's imposition of rules only slightly stronger than legal requirements presumably will not be fatal to a claim of independent contractor status. Conversely, there should be no special latitude, no special allowance for employer controls, just because there is also a legal framework. The legal or regulatory environment should be entirely neutral to the employee vs. independent contractor characterization question, at least if the employer's regimen of rules exactly tracks the legal requirements.

Evaluating Extra Controls

Employers who subject workers to requirements and standards in *excess* of legal requirements should be scrutinized. In *National Labor Relations Board v. Deaton, Inc.*,[10] the court considered the status of interstate courier drivers in the context of Interstate Commerce Commission (ICC) and Department of Transportation (DOT) regulations. Each truck traveling in interstate commerce must be certified. The goal of such registration is to promote safe operation of trucks and to ensure continuous financial responsibility so that truck-related losses receive compensation.[11]

The court found it unnecessary to decide whether ICC-mandated controls would alone be sufficient to establish employee status. The court analyzed the substantial nexus of control required by federal regulations and found that the facts established the existence of "additional control" voluntarily reserved by the employer. For

example, although ICC regulations required Deaton to make certain inquiries, Deaton more thoroughly checked out all drivers, including work references, police records, and driving records.

Moreover, although ICC regulations forbade any disqualified person from driving, Deaton's practice of assessing whether a driver was a "good risk" involved a subjective, employer-like inquiry. This inquiry was qualitatively different from merely ensuring that drivers were not barred from commercial driving. Based on these controls, the court found the drivers to be employees.

Conclusions

The cases discussed illustrate that an overlay of legal controls on work performance can make tougher still the already tough task of determining whether a worker is an employee or an independent contractor. At minimum, the analysis requires reference to applicable law and evaluation of whether the putative employer merely tracks the law or goes beyond it. The problem is exacerbated where legal or regulatory standards are amorphous.

How, for example, should one evaluate a requirement that salespeople receive training that is "thorough and adequate"?[12] Although rules from regulatory bodies ought not to bespeak employment,[13] exactly what is *required* by the government's rules may not be clear. It may be particularly difficult to determine fairly whether the employer is merely trying to duplicate legal requirements or inject its own standards.

In theory, rules imposed by law should be neutral to contractor-employee determinations. At least in the context of labor and employment law decisions, the courts have consistently held that governmental regulations do not evidence control by the employer.[14] Rules imposed by the government constitute supervision not by the employer but, rather, by the state.[15] However, even such a seemingly sensible rule may be very difficult to apply in practice. Suppose a multi-state employer requires independent contractor and employee painters alike to wear protective gear when spraying. Further, what if such protection is not required in two of the 15 states in which the employer operates, but uniformity and ease of administration explain the company's uniform policy?

Technically, this may place the employer's safety rules outside the protective umbrella of legal requirements in the two nonconforming states. But perhaps this kind of discrepancy should not be held against the company in a worker classification dispute. Alternatively, perhaps it should be held against the company only in these two states. The answer is unclear. At the very least, where worker status issues are examined, the presence of laws and regulations affecting that relationship must be considered. The case law (at least in the labor and employment law field) demonstrates that applying a legal regimen should not be treated as employer control, but rather as control by the pertinent legal authority. The applicability in federal and state tax law, tort cases, and so on, however, is also unclear.

Although such legal controls should generally be discounted in making worker status determinations, what is the extent to which variations between an employer's rules and legal requirements should be examined? And, particularly, should any such variations be strictly construed against the employer? Again, the answers are largely unclear. The authorities have thus far examined this issue in the context of federal labor and employment laws; but, the same issues may be expected to arise in federal and state tax cases, state tort law cases, and in legal disputes between the workers themselves and the company over their true status as either independent contractors or employees.

As with so much else in the field of employee-independent contractor classification, the presence of laws regulating worker and/or company conduct in a particular industry or location will require careful thought and attention. One must consider the factual setting, the specifics of the relevant laws and the manner in which the employer incorporates legal compliance into its operations, as well as into its relationship with its workers. ■

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1. 702 F.2d 912 (11th Cir. 1983).
2. 171 S.W.3d 100 (Mo. App. W.D. 2005).
3. 679 F.2d 1095 (4th Cir.1982).
4. 603 F.2d 862 (D.C. Cir. 1978).
5. *Yellow Cab Co.*, 229 N.L.R.B. 1329 (1977).
6. 512 F.2d 354 (9th Cir. 1975).
7. 429 F.2d 697 (10th Cir. 1970).
8. *Meyer Dairy, Inc., subsidiary of Milgram Food Stores, Inc.*, 178 N.L.R.B. 454 (1969), *vacated by* 429 F.2d 697 (10th Cir. 1970).
9. 521 So. 2d 220 (Fla. Dist. Ct. App. 2d Dist. 1988).
10. 502 F.2d 1221 (5th Cir. 1974), *cert. denied*, 422 U.S. 1047 (1975).
11. *Id.* at 1224.
12. Cal. Code Regs., tit. 10, § 2695.6 (2003) (applying to insurance salespersons).
13. *See K&D Auto Body, Inc.*, 171 S.W.3d 100.
14. *Nat'l Labor Relations Bd. v. Associated Diamond Cabs, Inc.*, 702 F.2d 912, 922 (11th Cir. 1983).
15. *Local 777, Democratic Union Org. Comm.*, 603 F.2d at 875; *Global Home Care, Inc.*, 521 So. 2d 220.