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Employee or Independent Contractor? Worker Misclassification Under Heightened Scrutiny

Avoiding Liability and Penalties Amid Aggressive DOL and IRS Enforcement

THURSDAY, DECEMBER 13, 2012

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

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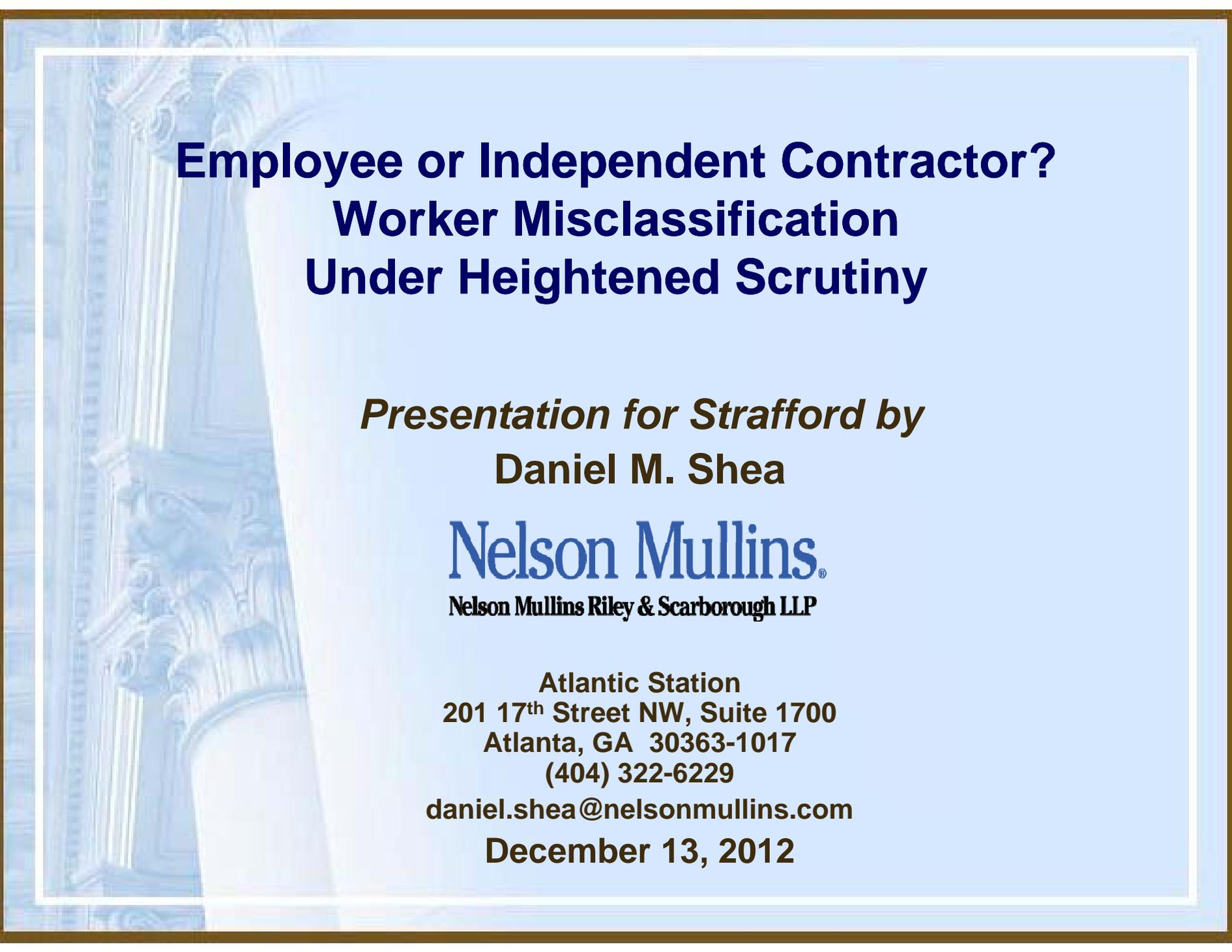
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Employee or Independent Contractor? Worker Misclassification Under Heightened Scrutiny

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December 13, 2012

Today's Presentation Will Include:

- **The current enforcement environment**
- **Various legal tests used by courts and government agencies**
- **Best practices to limit liability**
- **Hypothetical Scenario – Employee or Independent Contractor?**

Scrutiny for an Old Issue

“Few problems in the law have given greater variety of application and conflict in results than the cases arising in the borderland between what is clearly an Employer – Employee relationship and what is clearly one of independent, entrepreneurial dealing.”

(NLRB vs. Hearst Publications, Inc., 322 U.S. 111, 121 (1944))

The Government Studies

- **In 2009, the U.S. Bureau of Labor Statistics estimated that over 10.3 million workers – 7.3% of the workforce – are treated by businesses as independent contractors**
- **A 2000 Department of Labor study found that up to 30% of companies misclassified 3.4 million workers**
- **A 2009 GAO study found that 71% of IRS misclassification examinations result in changes to worker status**

Internal Revenue Service Initiatives

- **Agreements with 34 state commissioners and workforce agencies to share information and enforcement techniques**
- **Employment Tax National Research Project Auditing 6,000 Companies Over 3 Years**
- **Expected to raise \$7 billion over 10 years**

Department of Labor Initiatives

- **DOL has hired hundreds of investigators and other enforcement staff to be used in a “Misclassification Initiative” intended to recover wages and other benefits**
- **14 million in FY 2013 federal budget for grants to states, for misclassification initiatives**

- 
- **DOL and IRS partner with 37 states for information sharing and in some cases, joint investigations by federal and state compliance officers**
 - **DOL targets construction, restaurant, security guard, hospitality, landscaping, office cleaning industries**

Proposed Federal Legislation

- **Taxpayer Responsibility, Accountability and Consistency Act of 2009**
- **Employee Misclassification Prevention Act of 2010 and 2011**
- **Fair Playing Field Act of 2010 and 2012**
- **None has become law – yet**

State Legislative Developments

- **At least 20 states have passed misclassification statutes**
- **More than a dozen states have created misclassification task forces**

Legal Tests for Determining Employee Status

1. **The IRS's Right to Control Test**
2. **The Common-Law Test**
3. **The “Economic Realities” Test**
4. **The “ABC” Test**

The Internal Revenue Service's Right to Control Test

Perhaps the best-known test for employment status is the common law "right to control" analysis employed by the IRS. In general, an employer-employee relationship exists for federal tax purposes "when an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done."¹ In 1987, the IRS issued a list of twenty factors to be considered in determining whether an employer-employee relationship exists:²

¹Treas. Reg. § 31.3401(c)-1(b). This regulation explains:

Generally the relationship of employer and employee exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. That is, an employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. In this connection, it is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if he has the right to do so.

²Rev. Rul. 87-41, 1987-1 C.B. 296.

The Internal Revenue Service's Right to Control Test

1. **Instructions**: Whether the employer has the right to require the worker to comply with instructions about when, where, and how he or she is to work.
2. **Training**: Whether the worker is required to work with an experienced employee, to attend meetings, or otherwise is trained to perform the services in a particular method or manner.
3. **Integration**: Whether the worker's services are integrated into the business operations generally, in that the success or continuation of a business depends to an appreciable degree upon the performance of the services.
4. **Services rendered personally**: If the services must be rendered personally, the employer is presumably interested in the methods used to do the work as well as the results.

The Internal Revenue Service's Right to Control Test

5. **Hiring, supervising, and paying assistants:** Whether the employer or the worker hires, supervises, and pays any assistants.
6. **Continuing relationship:** A continuing relationship between the worker and employer indicates that an employer-employee relationship exists.
7. **Set hours of work:** The establishment of set hours of work by the employer indicates control.
8. **Full time required:** When the worker must devote substantially full time to the employer's business, the worker is impliedly restricted from doing other gainful work, unlike an independent contractor who is free to work when and for whom he or she chooses.

The Internal Revenue Service's Right to Control Test

9. **Doing work on employer's premises:** Work done away from the employer's premises indicates freedom of control, whereas work done on site indicates the employer's control over the worker.
10. **Order or sequence set:** A worker who must perform services according to established routines and schedules set by the employer is not free to follow his or her own pattern of work.
11. **Oral or written reports:** The requirement that a worker submit regular or written reports indicates control over the worker.
12. **Payment by hour, week, month:** Payment by the job or on straight commission generally indicates an independent contractor relationship, while payment by the hour, week, or month more likely points to an employer-employee relationship.

The Internal Revenue Service's Right to Control Test

13. **Payment of business and/or traveling expenses:** Payment of business expenses generally indicates an employer-employee relationship.
14. **Furnishing of tools and materials:** An employer's furnishing of tools, materials, and other equipment indicates an employer-employee relationship.
15. **Significant investment:** If the worker invests in facilities that are not typically maintained by employees, an independent contractor relationship is indicated. Lack of investment in facilities indicates dependence on the employer.
16. **Realization of profit or loss:** A worker who can realize a profit or suffer a loss as a result of his or her services (due to significant investment or liability for expenses) is generally an independent contractor.

The Internal Revenue Service's Right to Control Test

17. **Working for more than one firm at a time:** If a worker performs services for multiple employers at the same time, this indicates that the worker is an independent contractor.
18. **Making service available to general public:** The fact that a worker regularly makes his or her services available to the general public indicates an independent contractor relationship.
19. **Right to discharge:** The right to discharge a worker indicates an employer-employee relationship.
20. **Right to terminate:** The worker's right to quit at any time without liability indicates an employer-employee relationship.

The Internal Revenue Service's Right to Control Test

More recently, the IRS has created a three factor test so that the 20 factors are not mechanically applied in search of a magic number:

1. **Behavioral control** (facts illustrating a right to direct or control how the task is performed). Behavioral control includes instructions on when and where to work, what tools to use, where to purchase supplies or services, whether and which assistants may be utilized, whether prior approval is needed before taking action, and what routines, patterns, order, or sequence to follow. The more detailed the instructions, the more likely that an employer-employee relationship exists.
2. **Financial control** (facts illustrating a right to direct or control how the business aspects of the job are handled). Financial control factors include whether the worker has made a significant investment in the business, whether expenses are reimbursed, the opportunity for profit or loss, the method of payment, and whether the services are available to others.
3. **Relationship of the Parties** (facts showing how the parties perceive their relationship). Factors relevant to the relationship of the parties include their intent as expressed in a written contract, whether a W-2 form is filed, whether the worker is incorporated, the receipt of employee benefits, the manner in which the relationship may be terminated, and the expected duration of the relationship.

Department of the Treasury, Internal Revenue Service, *Independent Contractor or Employee?*
Training Materials, Course 3320-102 (10-96).

The Internal Revenue Service's Right to Control Test

- **Section 530 of the Revenue Act of 1978 creates a "safe harbor" permitting an employer to treat a worker as an independent contractor for employment tax purposes, regardless of the worker's actual status under the common law test, if certain requirements are met. In order to qualify for Section 530 relief, an employer must have:**
 - 1. consistently treated the workers (and similarly situated workers) as independent contractors;**
 - 2. complied with Form 1099 reporting requirements with respect to the tax years at issue; and**
 - 3. had a reasonable basis for treating the workers as independent contractors.**

National Association of Tax Reporting and Professional Management, "Section 530: Its History and Application in Light of the Federal Definition of the Employer-Employee Relationship for Federal Tax Purposes," (February 2009), at 6.

The Internal Revenue Service's Right to Control Test

- There are four categories of authority that may be relied upon as a "reasonable basis":
 1. federal judicial precedent or administrative rulings including published revenue rulings, and technical advice memoranda or private letter rulings *issued to that employer*;
 2. prior audits of the taxpayer;
 3. long-standing (at least 10 years) industry custom or practice in a significant segment (25%) of the industry; and
 4. other reasonable bases such as reliance on advice provided by an accountant or attorney when the treatment of the workers as independent contractors began.

The Common Law Test

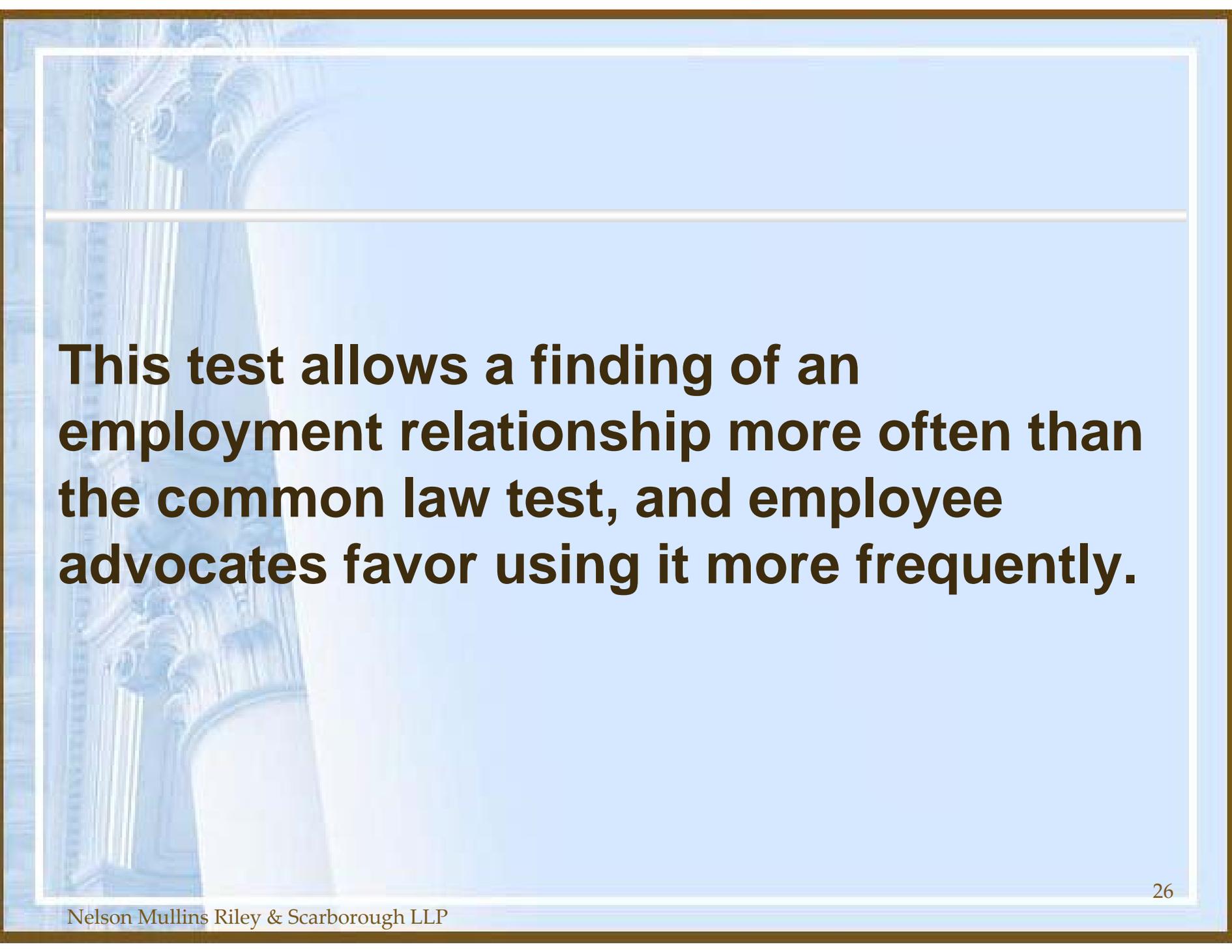
- The Supreme Court has indicated this test should be used under the NLRA, ERISA and a number of the discrimination laws. *NLRB v. United Ins. Co. of America*, 390 U.S. 254, 256 (1968). The Common Law Test draws on the following factors:
 - The Employer's contractual right to control the manner and means of performing the work.
 - Whether the worker is engaged in a “distinct occupation or business”.
 - The type of occupation.
 - Whether the occupation requires a special set of skills.
 - Whether the Employer or the Employee supplies the instrumentalities, tools, and the place of work for the person doing the work.
 - The length of time for which the individual is employed.
 - The method of compensation.
 - Whether the work is integral to the Employer's business.
 - Whether the parties intended to enter into an employment relationship.
 - Whether “the principal is or is not in business.”
- There is typically particular focus on the putative employer's control of the “manner and means of performing the work,” but no one factor is determinative.

The "Economic Realities" Test

- The test used under the FLSA, Age Discrimination in Employment Act, and Family and Medical Leave Act
- This is considered the broadest test of employee status
- This test focuses on whether the worker is "economically dependent" on the purported employer for his livelihood. An independent worker is not dependent.

Most Commonly Cited Factors

- **The degree of the company's right to control the manner in which the work is to be performed**
- **The worker's opportunity for profit or loss depending on his managerial skill**
- **The worker's investment in equipment or materials required for his task**
- **Whether the service rendered requires a special skill**
- **Whether the service rendered bears an integral relationship to the company's business**
- **The degree of permanence of the working relationship**



This test allows a finding of an employment relationship more often than the common law test, and employee advocates favor using it more frequently.

The ABC Test

- **The test used in about two thirds of the states to determine employee status under wage and hour laws and workers/unemployment compensation statutes**
- **The burden is on the company to prove that a worker is not an employee**

The ABC Test

- **This test requires the employer to show that**
 - A. The worker is, was, and will be free from control and direction in the performance of duties both contractually and in fact;**
 - B. The service is performed “either outside the usual course of the principal’s business or outside all the principal’s places of business;”**
 - C. The worker is “customarily engaged in an independently established trade, occupation, profession, or business” that is typically independent in the context of the service provided.**

The ABC Test

- **A handful of states use a test other than the ABC test to evaluate employee status. For example, the Texas Workers' Compensation Act defines an independent contractor as a person who contracts to perform a service for the benefit of another, and**
 - **Acts as the employer of any employee of the contractor by paying wages, directing activities, and performing other similar functions**
 - **Free to determine the manner in which the work is performed, including the hours of labor or method of payment**
 - **Required to furnish or to have employees, if any, furnish necessary tools, supplies or materials**
 - **Possesses the skills required for the specific work or service**

NLRB Developments

- **NLRB seeking to expand the common law test under the NLRA.**
- **Incorporating the FLSA’s “economic realities” tests – recognized to be the broadest under the employment laws is on the agenda of the NLRB through the efforts of Former Chairman Wilma Liebman.**
- **Conceding that the Board can not treat economic dependence as a determinative factor in the independent contractor analysis, the Board stated that it is “appropriate to treat economic dependence as one relevant factor among many.” Chairman Liebman, dissenting, then proceeded to apply the economic dependence test in a manner that would make it the tie breaker or outcome determinative of the common law test. *St. Joseph News-Press*, 345 NLRB 474, 484-87 (2005).**
- **After *St. Joseph News-Press*, Liebman reiterated her endorsement of the “economic dependence” test under the NLRA in *Arizona Republic*, 349 NLRB 1040, 1046 (2007).**
- **With the balance of power on the Board now shifted, another run at installing the “economic dependence” test under the Act is to be expected.**

“Entrepreneurial Opportunity” (Another Economic Consideration)

- **Courts have identified “Entrepreneurial Opportunities” as the touchstone of the common law test – whether the putative independent contractors have significant entrepreneurial opportunities for gain or loss. The focus is not upon the employer's right to exercise the means and manner of the work but instead upon whether the putative independent contractors have a “significant entrepreneurial opportunity for gain or loss.”**
- **In *FedEx Home Delivery v. NLRB*, 563 F.3d, 492 (D.C. Cir. 2009), the court set aside an NLRB decision that FedEx unlawfully failed to bargain with the Teamsters local that had been certified as bargaining agent for “single route” drivers at two FedEx Home terminals. The court reasoned that application of the common law agency test needed to evolve, and found independent contractor relationships based on a record that included the following:**

“Entrepreneurial Opportunity”

- **The drivers had signed the FedEx Home form “Operating Agreements” specifying they were not employees and retained control over the “manner and means of reaching mutual business objectives”**
- **Provided their own vehicles and bore the costs of operating/maintaining them**
- **Drivers were free to use their trucks for any personal or commercial purpose as long as they removed or covered FedEx logos**
- **Contractors could incorporate (and did)**
- **Contractors could negotiate fees with FedEx (and did)**
- **Contractors were free to serve multiple routes for FedEx Home**

“Entrepreneurial Opportunity”

- **Had authority to hire and fire their own drivers, negotiating pay and benefits directly**
- **Contractors did not have to show up at work every day, but could take time off so long as they hired another to be there**
- **Drivers can “sell, trade, give, or even bequeath their routes,” “with no FedEx involvement,” (and did)**
- **The fact that drivers performed a “regular and essential” part of FedEx Home normal operations was a “legitimate” consideration weighing against independent contractor status, but was “not determinative” in part because otherwise companies like FedEx Home could “never hire delivery drivers who are independent contractors”**

“Entrepreneurial Opportunity”

- **Other courts, citing approvingly the FedEx Home decision, nonetheless found NLRA employee status where the putative employees did not engage in any entrepreneurial activities**
- **Because “entrepreneurial opportunities” has emerged as a guiding principle to analyze the common law test, the Board could substitute this for “economic dependence” to press a change to the common law employee test**

FLSA Independent Contractor Standard in Litigation

FLSA case law has not crystallized around a fixed set of common law test factors, but more on a “totality of circumstances” including “economic realities” rather than a checklist, but courts generally continue to rely on six frequently-cited factors in analyzing independent contractor or joint employer issues under the FLSA:

- 1. The degree of control exercised by the company**
- 2. The extent of the worker's investment compared to the company's investment**
- 3. The degree to which the worker's opportunity for profit or loss is dependent on the company**
- 4. The level of skill and initiative required in performing the job**
- 5. The permanency of the relationship**
- 6. The extent to which the work performed by the worker is integral to the company's business**

Discrimination Law Issues

- **Title VII, The Americans with Disabilities Act, and the Age Discrimination in Employment Act define an employee similarly to ERISA, and courts have used the common law test, "Economic Realities" test, and a hybrid of the two**
- **Independent Contractors have been permitted to bring Section 1981 claims for race discrimination since by its terms, Section 1981 is not limited to employment contracts**
- **The Rehabilitation Act has been interpreted to cover Independent Contractors as well as employees**



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December 13, 2012

Potential Areas of Exposure

- **Tax Liability Under Federal and State Laws**
- **Wages and Overtime Under FLSA and State Laws**
- **Employee Benefit Plans**
- **National Labor Relations Act**
- **Workers Compensation Premiums**
- **Unemployment Insurance Premiums**

Tax Liability

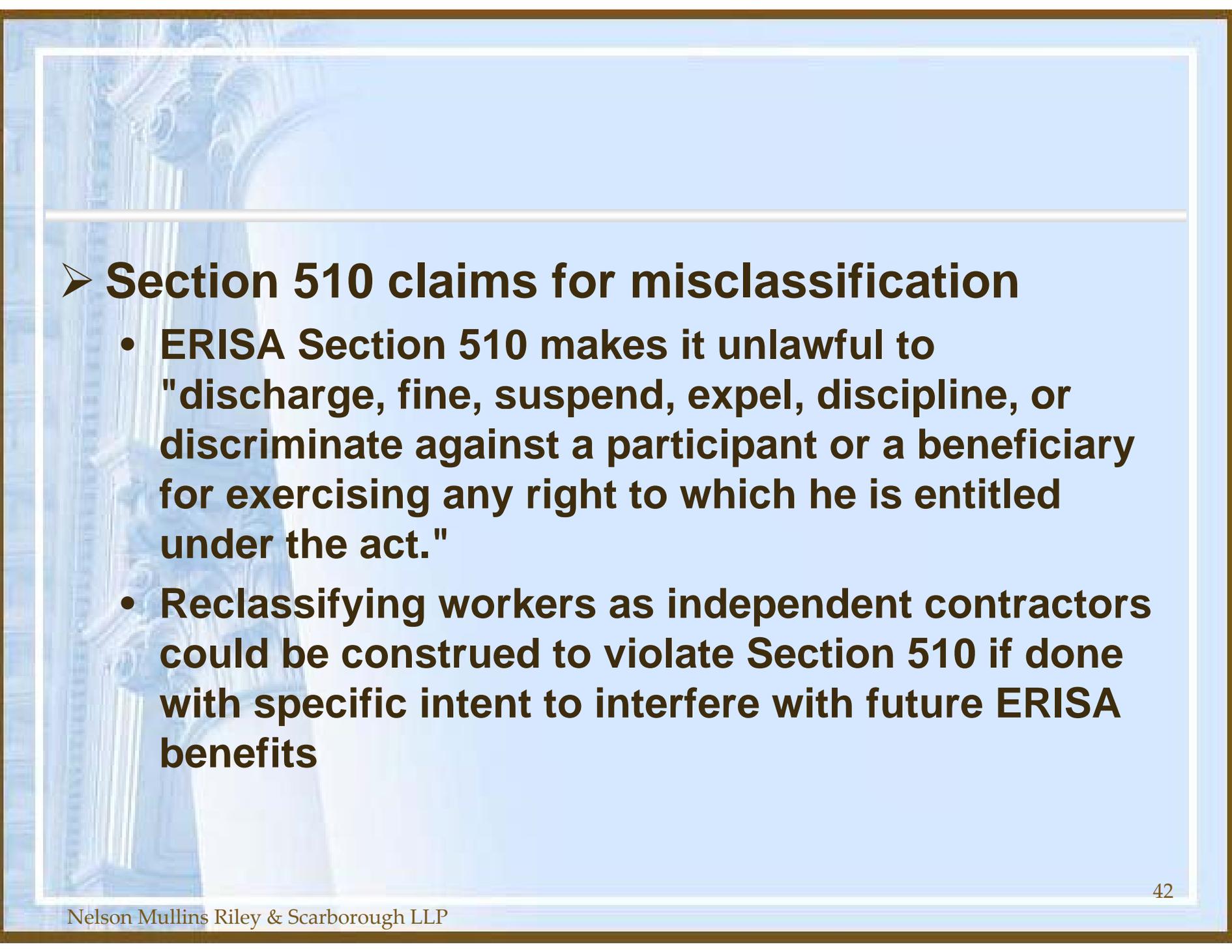
- **Income tax, FICA (social security) and FUTA (federal unemployment) taxes that should have been withheld**
- **Civil Penalties**
 1. **unintentional misclassification: 1.5% of wages paid and 20% of FICA tax, plus employer's share of FICA tax**
 2. **failure to report compensation on Form 1099: 3% of wages paid and 40% of employee's share of FICA, plus employer's share of FICA**
- **Interest compounded daily at the short-term applicable federal rate**
- **State taxes and penalties**

Minimum Wage and Overtime

- **Under FLSA, unpaid overtime of 1 ½ time regular hourly rate, plus liquidated damages in an equal amount, plus attorneys fees and costs**
- **Individual liability possible under FLSA**
- **Department of Labor may assess civil money penalties of up to \$1,100 per violation if willful or repeated**
- **Criminal prosecution is possible, with fine up to \$10,000 and imprisonment for second conviction**

Employee Benefit Plans

- **Covering workers who are not “employees” places the tax-favored status of the plan at risk**
- **Excluding workers who are eligible “employees” places the tax-favored status of the plan at risk and give rise to claims for benefits**
- **ERISA unhelpfully defines "employee" as "any individual employed by an employer"**



➤ **Section 510 claims for misclassification**

- **ERISA Section 510 makes it unlawful to "discharge, fine, suspend, expel, discipline, or discriminate against a participant or a beneficiary for exercising any right to which he is entitled under the act."**
- **Reclassifying workers as independent contractors could be construed to violate Section 510 if done with specific intent to interfere with future ERISA benefits**

How to Protect Against Benefits Claims

- **Expressly define plan terms and exclude independent contractors**
- **Contractors excluded from plan participation, even if subsequently reclassified as common-law employee**

Sample Provision

“If an individual now classified by the Company as an Employee is retroactively reclassified as such by any governmental or regulatory authority, such individual shall nonetheless be deemed to have become an Eligible Employee only prospectively on the event of such reclassification (and not retroactively to the date on which he was found to have first become an employee for any other purpose), and the only if he otherwise satisfies the requirements of this Section.”

Patient Protection and Affordable Care Act

- **By 2014, employers with 50 or more full time equivalents (FTE) must provide health insurance to employees or pay excise tax**
- **Independent contractors not included in the head count – but employers who undercount employees will be penalized**
- **If employee is misclassified and does not receive insurance, employer will face penalty**

Workers Compensation Issues

- **Variety of criteria used by various states – similar to other tests for employee status**
- **"Bright Line" Systems – specific and binding set of criteria for independent contractor status**
- **"Weight of Evidence" Systems – several criteria considered and balanced**
- **Exclusive remedy doctrine is a double-edged sword**

Unemployment Issues

- **Employers don't pay unemployment premiums for contractors**
- **If contractor files for unemployment benefits, may trigger audit or administrative proceeding regarding coverage**
- **If employment relationship found, unpaid premiums, interest and penalties may be assessed**
- **Worker may qualify for unemployment benefits under state law, but still be considered independent contractor under other laws**

National Labor Relations Act

- **Applies to employees whether or not they are union members**
- **If contractor is reclassified as member of bargaining unit, covered by collective bargaining agreement**
- **May lead to grievance or unfair labor practice charge**



Self-Audit Independent Contractor Practices to Ensure Proper Classification

Ten Questions to Help Determine Whether Contractors Are Properly Classified

- **Have all independent contractors signed written independent contractor agreements?**
- **Are the contractor's duties integrated with core business operations, or does he or she perform non-essential business activities?**

Ten Questions to Help Determine Whether Contractors Are Properly Classified

- **Does the contractor provide full-time services to you, or does he or she work for other companies also?**
- **Does the contractor receive employee benefits such as insurance coverage or paid time off?**

Ten Questions to Help Determine Whether Contractors Are Properly Classified

- **Must the contractor's services be performed on-site, or during specific hours?**
- **Must the contractor's services be performed personally?**

Ten Questions to Help Determine Whether Contractors Are Properly Classified

- **Does the contractor do the same job as or work side by side with company employees?**
- **Does the contractor have a supervisor who directs his or her work, or does the contractor supervise company employees?**

Ten Questions to Help Determine Whether Contractors Are Properly Classified

- **Is there a non-compete agreement that would prevent the contractor from providing services to other employers?**
- **Is the contractor expected to attend company meetings or periodic or ongoing training as to procedures and methods to be used?**

The Voluntary Classification Settlement Program - "VCSP"

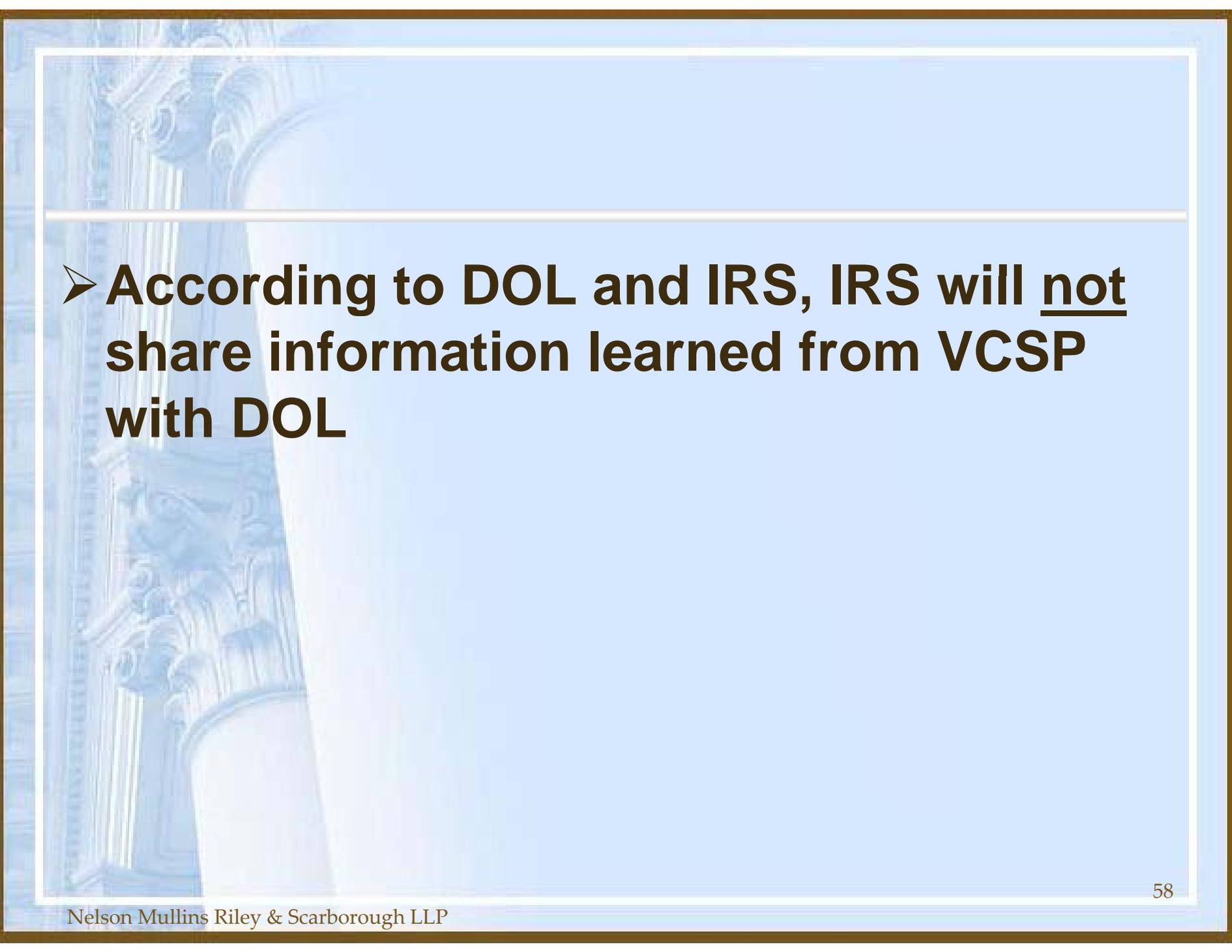
- **IRS launched on September 21, 2011**
- **Opportunity for employers to prospectively treat workers as employees, pay a small percentage of back taxes, and avoid audit**
- **625 employers have applied since program began**

VCSP Eligibility Requirements

- **Employer must have consistently treated workers as non-employees in the past**
- **Must have filed Forms 1099 for past three years**
- **Not currently be under audit by IRS, Department of Labor, or state agency concerning classification of workers**

How it Works

- **File Form 8952 at least 60 days before date workers to begin being treated as employees**
- **If accepted by IRS, pay 10% of Section 3509 tax for most recent year - 1.028% of 2011 compensation instead of 10.28%**
- **No penalties or interest for past three years, and no audit**
- **Six year statute of limitations for first three years under program instead of usual three years**

- 
- **According to DOL and IRS, IRS will not share information learned from VCSP with DOL**

Potential Risks

- **Does not resolve state tax issues**
- **Potential retroactive liability under employee benefit plans**
- **Does not resolve employee claims for overtime or minimum wages**

The background of the slide features a faded, light blue image of classical architectural columns, likely from a government building or courthouse, which adds a sense of legal authority and formality to the presentation.

Protect Your Company With a Well-Drafted Independent Contractor Agreement

Ten Essential Elements of an Independent Contractor Agreement

- **Limit agreement to a specific term or project that cannot automatically roll over**
- **Provide that contractor shall determine how, when, and where the work will be done**

Sample Provision

Method of Performing Services. Contractor will furnish all labor and equipment necessary to perform the work, and shall solely control the means, manner and method of performance; subject, however, to the terms and conditions of this agreement. The Company shall, however, be entitled to exercise general power of supervision and control over the work to assure satisfactory performance, including the right to inspect, the right to stop work, the right to make suggestions or recommendations, and the right to propose modifications.

Ten Essential Elements of an Independent Contractor Agreement

- **State that contractor may provide the same or similar services to other companies while the agreement is in effect**
- **Explicitly acknowledge that independent contractor relationship exists, and that contractor will pay his or her own taxes**

Sample Provision

Relationship Between the Parties. The relationship between the parties shall be that of independent contractors under Georgia law, and not of employer-employee. In all public records, in its relationship with others, and in any documents. Contractor shall clearly indicate the independent ownership of Contractor's business and that operations of said business are separate and apart from the operations of the Company's business. Contractor will not be treated as an employee of the Company for purposes of state or federal anti-discrimination laws, the Fair Labor Standards Act, the Federal Income Contribution Act, the Social Security Act, the Federal Unemployment Tax Act, nor Income Tax Withholding.

Sample Provision

Relationship Between the Parties (cont'd). Contractor is responsible for the payment of estimated income and self-employment taxes. Contractor further agrees to indemnify and hold harmless the Company for any liability with the Internal Revenue Service or any state tax agency, as well as local laws and regulations regarding the payment of such taxes on income from self-employment and wages paid its employees.

Ten Essential Elements of an Independent Contractor Agreement

- **If possible, require that contractor provide own tools and equipment**
- **Spell out that contractor is not covered by company's liability, health, or workers compensation insurance, and receives no other employee benefits**

Sample Provision

No Benefits. Contractor shall not be entitled to participate in health or disability insurance, retirement benefits, or other welfare or pension benefits (if any) to which employees of the Company may be entitled.

Ten Essential Elements of an Independent Contractor Agreement

- **Require that contractor be responsible for his or her own expenses**
- **If appropriate, require that contractor add company as additional insured on contractor's liability insurance policies**

Sample Provision

Insurance. Contractor agrees to purchase "occurrence" based commercial general liability insurance with a limit of liability of at least \$1,000,000 per occurrence and a general aggregate limit of at least \$2,000,000. The Company, its officers, directors, and employees shall be included as additional insureds. In addition, Contractor will maintain automobile liability insurance for all owned, non-owned, and hired vehicles with a limit of at least \$1,000,000 combined single limit for bodily injury or property damage. The Company, its officers, directors, and employees shall be named as additional insureds on such a policy.

Ten Essential Elements of an Independent Contractor Agreement

- **Pay for tasks accomplished rather than hours worked**
- **Provide for indemnification by contractor for taxes owed, workers compensation claims, discrimination claims, tort liability**

Sample Provision

Indemnification. The Contractor shall indemnify and hold harmless Company and its officers, directors, and employees, for any claims brought or liabilities imposed against the Company by Contractor or by any other party (including private parties, governmental bodies and courts) including claims related to Workers' Compensation, wage and hour laws, discrimination, employment taxes and benefits, and whether or not related to Contractor's status as an independent contractor. Indemnification shall include any and all losses, including costs and attorney fees.

Holland+Knight

INDEPENDENT CONTRACTOR OR EMPLOYEE?

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December 13, 2012

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Background

Samuel Peralta ("Sammy") Sosa (born November 12, 1968) dreamed of being a baseball player, but gave up his dream to embark on a career selling property, casualty, and life insurance like his dad. Sammy contacted Major League ("ML") Insurance Company to apply for an opportunity to open his own insurance agency in Cub County, Illinois. Sammy was hired for the position -- he told his wife Sonia that he thought he was hired because of his "winning" personality.

Independent Contractor Agreement

ML Insurance Company sent Sammy its form Independent Contractor Agreement which provides:

- **As an independent contractor, the Contractor controls its own daily activities.**
- **Either the Company or Contractor can terminate the relationship at any time for any reason.**
- **The Contractor can only sell the insurance products of the Company.**
- **The Contractor must use the Company's insurance forms, manuals, and computer network.**

Independent Contractor Agreement

- **The Contractor is subject to the Company's rules and regulations regarding the sale of insurance.**
- **The Contractor is paid exclusively by commission after the first 6 months of employment. No monies are withheld from the Contractor's paycheck and the Company issues a 1099 at the end of each calendar year.**
- **The Company provides no employment benefits.**
- **The Contractor is responsible for its own expenses, including office space open to the public.**

Training

During the first 6 months, Sammy was required to attend training classes one day per week in the Company's home office. The classes covered the operation of the Company's systems, basic insurance knowledge, sales techniques, and the Company's product line. Attendance at these training sessions was mandatory.

Compensation and Expenses

In addition, during the first 6 months Sammy received a draw of \$1,000 per month plus commissions. The draw was paid to subsidize the agency until the agency generated steady commission income. The Company recognized that the start-up costs in running an agency could be substantial -- office space, furniture, equipment, and hiring an employee to do reception and clerical work.

Work Schedule

Sammy was free to come and go as he pleased. He set his own schedule, including days off and vacations. He regularly took time off to play right field for the local semi-pro baseball team. He rarely saw or heard from the Regional Manager, Mark McGuire.

Supervision

Occasionally, McGuire would drop by and offer suggestions regarding the operation of the agency. Sometimes the "suggestions" were pointed -- McGuire directed Sammy to remove his diamond stud earring, remove the shabby cork table in the lobby, and remove the "unprofessional" Chicago Cubs cap Sammy wore around the office.

Job Performance

Sammy got off to a great start during his rookie season. He became one of the best producers in the region. His success continued. He was the only producer in the region to sell 60 or more life insurance policies in three different years. Sammy was an All-Star Selection, a Silver Slugger Award winner, and a Home Run Derby Winner, all in recognition of his prolific production statistics. Sammy even won ML Insurance Company's coveted Most Valuable Player Award for leading the region in every production category. His contacts at the Company nick-named him "Slammin' Sammy."

Job Performance

But beginning about fifteen years after the start of his career, Sammy fell into a production slump. When Sammy's production started to slip, Regional Manager McGuire was vocal in his criticisms. In particular, McGuire criticized Sammy for staying in the office and relying on walk-in traffic. Sammy was told that he needed to "play the field" if he wanted to succeed.

Contract Termination

When Sammy's production continued to lag, the Company terminated Sammy's contract. Sammy was surprised. He suspected that Regional Manager McGuire never really liked him because of his national origin (Dominican Republic). He heard that McGuire "disrespected" the years he was a "big hitter" by claiming that he must be using "performance-enhancing drugs."

Independent Contractor or Employee?

Sammy filed a lawsuit under the state employment statute, which allows an individual to bypass the state administrative agency, alleging discrimination based upon national origin, age discrimination, and perceived disability discrimination. The Company has filed a Motion to Dismiss on the ground that the state statute applies to employer-employee relationships and Sammy was an independent contractor.