# The Employer-Employee Relationship: Definitions and Distinctions

**Chapter Objective:**

The purpose of this chapter is to define the terms employee and employer in connection with various statutes and regulations which apply to them in order to understand the application of each regulation. First the chapter addresses why it is important to understand who is and is not an employee, then continues to explore the definition, which may vary depending on the applicable statute. The chapter explains the benefits and costs of hiring someone as an employee and as an independent contractor. Next, we will discuss how a firm is designated as an employer and what are the ramifications of that designation.

**Scenarios -** Points for discussion

***Scenario One:*** One might decide to discuss this scenario before proceeding with the discussion of the rest of the chapter in order to determine the awareness level of the students before teaching the text. Many students may have some understanding of the difference between an independent contractor and an employee, while others do not.

The benefits to hiring someone as an independent contractor include the fact that the employer in many situations may not have liability for the acts of the independent contractor while it would be liable for the acts of an employee. Second, an independent contractor is generally responsible for the completion of a project. She is hired for a specific project and is responsible for its success. Third, the employer need not pay benefits to the independent contractor. On the other hand, the employer would have no control over how the project will be completed if it hires someone as an independent contractor, merely that it is completed to certain specifications.

In addition, an employer is not responsible for withholding any amount from its payment to independent contractors. In this way, it may avoid additional bookkeeping costs.

For the second position, it is likely that the individual will be considered an independent contractor.

***Scenario Two: The*** suggestion offered by the employee may be an acceptable solution as long as it can not be inferred that the employer did this specifically to avoid paying the older worker any benefits. In this way, the older worker recognizes a benefit because he may still receive some income from specific projects for which he remains qualified, even though it was not profitable for the firm to retain him on a full-time basis.

***Scenario Three.*** Many students might consider that, because the question identifies these workers as "part-time," this would mean that the workers are independent contractors. To the contrary, part-time workers are not conclusively employees or contractors. Therefore, before turning to the statutes, ask the students what other information is necessary to reach a conclusion regarding the number of employees employed by this employer. I would argue that secretaries would generally be considered employees because they generally have little control over how they perform their work. On the other hand, depending in the type of business involved, the four consultants may be viewed as contractors or employees. The answer to this question also depends on whether the employer receives federal assistance or is a federal agency.

**Lecture Notes**

**Lecture Note:** As with the beginning of my first class session, again I try to emphasize that we are all unique individuals. My concern is that, even in a class such as this where these types of issues are "on the table," students of course retain their biases from their culturalization process. In an effort to break these molds, I play a game called Human Bingo. The purpose of this game is to make students aware that people are not always who you think they are, and that the one person in the class who appears to be the most reserved may also be the only person in the class who has jumped out of an airplane, or who speaks several languages, and so on.

Prepare a grid on a regular sheet of paper with twenty-five boxes. Fill in twenty of the boxes with qualities such as "speaks more than two languages," "has skydove before," "knows a good joke and can tell you it," "can name at least three Michael Jackson songs," "grew up in the city/suburbs," etc. Copy these sheets so that everyone has the same one and hand them out.

Tell students to write a quality that an individual may have in each of the empty squares. This can be skis downhill, reads People, lives more than thirty miles from school, can name three Michael Jackson songs, etc. The trick to listing these is that the quality must be one that you expect less than half of the class to satisfy.

The point of this exercise is to walk around the room and find people who satisfy that quality. You may only ask, do you . . . , not whether they can sign any of the boxes. If they do, have them sign that square on your sheet. Collect as many signatures as you can. At the end of the time limit, the person who has the most bingo lines on their paper wins. Ties will be broken by the total number of squares signed. And those ties will be broken by all of you voting on who of them listed the harder qualities to find.

[I usually ask who signed certain boxes, and ask the person who knows the joke to tell it, the person who knows the songs to name them, etc.]

**Lecture Note:** I would probably wait until the class has discussed the chapter to consider Box 2-1. In that way, you could discuss together the issues presented by the chapter, then go back and ask the students why each of these is actually a myth.

1. Introduction to the Issue

A. Basic Principles of Agency Law

1. *Origins in Agency Law.* The law relating to the employment relationship is based on the traditional law of master and servant, which evolved into the law of agency. It may be helpful to briefly review the fundamentals of the law of agency in order to gain a better perspective on the legal regulation of the employment relationship that follows.

2. In an agency relationship, the party for whom another acts and from whom she or he derives authority to act is known and referred to as a "principal," while the one who represents the principal is known as an "agent." The agent is like a substitute appointed by the principal with power to do certain things. The agent is considered as the representative of the principal and acts for, in the place of the principal. Similarly, an employee is the agent of the employer, the principal. The employee is the representative of the employer and acts in its place.

1. In an employment/agency relationship, the employee/agent is under a specific duty to the principal to act only as *authorized*. As a rule, if an agent exceeds her authority or places the property of the principal at risk without authority, the principal is now responsible for all loss or damage naturally resulting from the agent’s unauthorized acts. An agent is subject to a duty to properly conduct himself in the discharge of the agency transaction and he is liable for injuries resulting to the principal from his unwarranted misconduct.

4. Accordingly, if an employee acts in a way that exceeds her authority, the employer may still be liable to a third party (though the employee would then be liable back to the employer because she exceeded her authority).

1. Throughout the entire relationship, the principal has the obligation toward the agent to exercise good faith in their relationship, and the principal has to use care to prevent the agent from coming to any harm in the during the agency relationship. This requirement translates into the employer's responsibility to provide a safe and healthy working environment for the workers.

6. In addition to these implied duties for the employment relationship, the next section further answers the question of why this characterization is so important to the working relationship

**II. Why is it Important to Determine Whether A Worker is an Employee?**

A. There is not merely one definition of who constitutes an employee. The answer will vary depending on the court, the issue and the statute to be applied. The issue, however, must be determined because of the following concerns.

B. **Employee Payroll Deductions**. An employer paying an employee is subject to different payroll requirements than when paying an independent contractor.

1. In general, it is the employer's duty to pay Social Security (FICA), the FICA excise tax, Railroad Retirement Tax Act (RRTA) withholding amounts, federal unemployment compensation (FUTA), IRS federal income tax withholdings, Medicare and state taxes for each of its employees.

2. In addition, it is the employer's responsibility to withhold a certain percentage of the employee's wages for Federal income tax purposes.

3. An independent contractor must be responsible for the payment of such taxes on his or her own. The principal merely pays the fee to the contractor and the contractor then pays the taxes at a later date, usually through four estimated payments per year. Thus, the principal is able to avoid the bookkeeping costs associated with such withholdings.

C. **Employee Benefits.** In an effort to attract and retain superior personnel, employers offer employees a range of benefits which generally are not required to be offered, such as dental, medical, pension, and profit-sharing plans. Independent contractors have no access to these benefits.

1. Where a worker is considered an employee, the worker is protected by the provisions of The Employee Retirement Income Security Act of 1974 (ERISA), which was enacted to protect employee benefit plan participants from retirement plan abuses, and the Fair Labor Standards Act of 1938 (FLSA) was enacted to establish standards for minimum wages, overtime pay, employer record-keeping and child labor.

D. **Discrimination and Affirmative Action.** Title VII and other related anti-discrimination statutes only protect *employees* from discrimination by employers.

1. Additionally, the National Labor Relations Act protects only employees and not independent contractors from unfair labor practices.

2. Note, however, that independent contractors may be considered to be *employers*, so they may be subject to these regulations from the other side of the fence.

E. **Cost Reductions.**

**By hiring employees:**

1. Employees are more expensive to employ due to the above regulations which require greater expenditures on behalf of employees, as well as the fact that others must be hired to maintain records of the employees.

2. In addition, by hiring independent contractors, the cost of overtime is eliminated (the federal wage and hour laws do not apply to independent contractors) and the employer is able avoid any work related expenses such as tools, training or traveling.

3. The employer is also guaranteed satisfactory performance of the job for which the contractor was hired, as it is the contractor's contractual obligation to adequately perform the contract with the employer; while the employee is generally able to quit without incurring liability.

4. In addition, the employee may actually cause the employer to have greater liability exposure. An employer is "**vicariously liable**" if the employee causes harm to a third party while the employee is in the course of employment. While the employee may be required to indemnify or reimburse the employer for any liability incurred as a result of the negligence, generally the third party goes after the employer because the employee does not have the funds to pay the liability. The employer could sue the employee for this reimbursement, but will more likely write it off as an expense of doing business.

5. Finally, some managers contend that independent contractors are more motivated and, as a result, have a higher level of performance as a consequence of their freedom to control their own work and futures.

**By hiring independent contractors:**

1. Independent contractors may still be more expensive to hire and maintain than employees. This situation may exist where the employer finds that it is cheaper to have its employers perform certain types of work that are characteristically expensive to contract for.

F. **Failure to Appropriately Categorize Worker**

1. If a worker is found to be classified as an independent contractor, but later found to constitute an employee, the punishment by the **IRS** is harsh.

a. The employer is not only liable for the its share of FICA and FUTA, but also subject to an additional penalty equal to 20% of the FICA that should have been withheld.

b. In addition, the employer is liable for 1.5% of the wages received by the employee.

c. These penalty charges apply if there have been 1099 forms (records of payments to independent contractors) compiled for the worker. If, on the other hand, the forms have not been completed, the penalties increase to 40% and 3%.

d. Where the IRS determines that the worker was *deliberately* classified as an independent contractor in order to avoid paying taxes, the fines and penalties can easily run into six figures for even the smallest business.

2. The employer may also be liable for violations of the **National Labor Relations Act of 1935.**

a. Liability may include reinstatement and back pay to employees fired in violation of the NLRA under the mistaken belief that they were independent contractors.

3. The employer may also be liable under the **Fair Labor Standards Act of 1938** for amounts of unpaid wages or overtime compensation, attorneys' fees and costs.

a. Any person who willfully violates the FLSA is subject to a fine of $10,000 and six months imprisonment.

4. Under the **Employee Retirement Income Security Act of 1974 (ERISA),** an employer may be liable for accrued but unpaid benefits.

a. The tax advantages of a qualified retirement or fringe benefit plan to employers or employees may be lost as a result of misclassification.

5. There is possible liability under the **Social Security Act of 1935**, state worker's compensation and unemployment compensation laws.

6. So it would seem to be a lost cause? Not really; there is hope for correct classification: the 1978 Revenue Act forms a **safe harbor** for employers who have consistently classified a class of workers as independent contractors.

a. There are certain "safe harbors" established by section 530 of the Revenue Act of 1978. A safe harbor is a rule which establishes certain criteria which, if met, guarantee that a worker will be deemed an independent contractor or an employee for the purpose of the IRS classifications (not federal income tax classification). According to section 530, a worker will be considered an independent contractor provided that each of the following four criteria are met.

1) The business must have never treated the worker as an employee for the purposes of employment taxes for any period (i.e. the company has never withheld income or FICA tax from its payments, etc.).

2) All federal tax returns with respect to this worker were filed consistent with the worker being an independent contractor.

3) The company has treated all those in positions substantially similar to that of this worker as independent contractors.

4) The company has a reasonable basis for treating the worker as an independent contractor. Such a reasonable basis may include a judicial precedent or published IRS ruling, a past IRS audit of the company, or long standing industry practices.

b. Where these conditions have been satisfied, the employer is not liable for misclassification.

**Lecture Notes**

**III. How Do You Determine Whether a Worker is An Employee?**

A. Given the variety of ways in which to determine whether a worker is an employee or not, the means by which the decision is reached usually depends on the factual circumstances and issue in the case. Most statutes do not define the term, even though it is used extensively in the statute itself (assuming the term is clear), while others create new ways to reach the decision.

**Lecture Note:** The text then discusses the case, Lemmerman v. A.T. Williams Oil Co. It may be beneficial to ask the class whether they understand why the employer wanted the boy classified as an employee. (Because then he is limited to collecting damages under workers' compensation act rather than under standard tort law.) Perhaps ask the class to list those reasons why someone might classify him as an employee or not.

B. Several tests have developed and are commonly used by courts to classify employees and independent contractors. These tests included the common law test of agency, which focuses on the right of control, the Internal Revenue Service (IRS) 20 factor analysis, and the economic reality analysis. Several courts also use a hybrid approach, using one test but combining factors from other tests.

* 1. Under the common law agency test, a persuasive indicator of independent contractor status is the ability to control the manner in which the work is performed. This test was derived from the law involving domestic relations of the “master and servant.” Where the master had control over the servant, the worker was considered the master’s servant, employed by and connected to that master, more similar to common law property rights than contract rights. Today, the contract or agency principals apply rather than property principals. The element of control has persisted to today’s interpretation of who constitutes an employee and who is an independent contractor. The right to control remains the predominate factor.
     1. Under the common law agency approach, the employer need not actually control the work, but must merely *have the right or ability* to control the work for a worker to be classified an employee. Although this is a strong indication that the worker is an employee, other factors usually are considered. For example, it has been held that an employee is one who works for wages or salary and is under direct supervision. An independent contractor has benefited as one who does a job for a price, decides who the work will be done, usually hires others to do the work, and depend for their income not upon wages, but upon the difference between what they pay for goods, materials and labor and what they receive for the end result, that is upon profits.
     2. The common law test is specifically and consistently used to determine employee status in connection with FUTA and FICA taxes, in determining whether an employee is a statutory employee (discussed later in this chapter), as well as in federal income tax withholding.

**Case Example:**

***Nationwide Insurance Co. v. Darden, 112 S.Ct. 1344 (1992)***

**Issue:** Whether Darden was an employee, and therefore had rights under ERISA, or independent contractor. ERISA does not clearly define the term employee.

**Facts:** Darden worked as an agent for Nationwide Insurance Company pursuant to a contract which stated, among other terms, that Darden would sell only Nationwide policies and that he would forfeit his entitlement to retirement plan benefits if he sold insurance for Nationwide's competitors within one year of his termination and 25 miles of his previous business location. After his termination, he began working for one of those competitors and Nationwide determined that he was therefore disqualified from receiving his retirement benefits. Darden sued under the Employee Retirement Income Security Act (ERISA). The district court granted summary judgment to Nationwide as Darden was not an employee and therefore not a proper ERISA plaintiff. The court of appeals reversed the lower court's ruling, and the Supreme Court evaluated which definition of employee was most appropriate for an ERISA claim.

**Decision:** The court noted that ERISA does not adequately define the term employee. In analyzing the definition, therefore, the court discusses other instances where no definition for the term was given, and found that "where Congress uses terms that have accumulated settled meaning under the common law, a court must infer, unless the statute otherwise dictates, that Congress means to incorporate the established meaning of those terms. In the past, when Congress has used the term ‘employee’ without defining it, we have concluded that Congress intended to describe the conventional master-servant relationship as understood by the common law agency doctrine." The court consequently adopts a common law test for determining who qualifies as an "employee" under ERISA. Since the common law test contains no shorthand formula or magic phrase that can be applied to find the answer, all of the incidents of the relationship must be assessed and weighed with no one factor being decisive.

**Case Questions**

*1. If someone were to ask you to define "employee," according to the "established definition" as described by the court, how would you respond?*

The purpose of this question is to highlight the fact that, while the court appeared distressed that ERISA did not adequately define the term employee, neither did the court in the end. The court even said that "traditional agency law criteria offer no paradigm for determinacy. But their application generally turns on factual variables within an employer's knowledge." As an employer, one is still given very little direction and would have to, again, look to the twenty factors of the common law test.

*2. Do you agree that the definition offered by ERISA, "any individual employed by an employer," is circular if "employer" is clearly defined?*

One might argue that, in fact, it is not circular, merely broad. If employer is clearly defined, then anyone employed by, or used by, hired by, an employer is an employee. This would probably lead to a greater number of individuals being categorized as employees than the court envisions reasonable; however, it may be argued that it is clear.

*3. Do you think that the average employer will be clear regarding which of their workers are employees and which are not, using the criteria for the common law test described in this chapter?*

The court believes that the employer will be clear (see answer to No. 1). Ask your students about various types of positions and whether they would be an independent contractor or an employee: Referee at a hockey game? Substitute teacher? Delivery person for a grocery store? Valet parking attendant?

Under the IRS 20-factor analysis, the IRS, in training material issued in July, 1996, explained that this Twenty-Factor Test is an analytical tool and **not** the legal test used for determining worker status. The legal test is whether there is a right to direct and control the means and details of the work (emphasis in original (Dept. of Treasury, Internal Revenue Service, “Employee or Independent Contract?” Training 3320-102 (7/96)). However, the following 20 factors have been consistently and continually articulated by courts, regulatory agencies, commentators, and scholars as critical to the determination of the status of an individual worker. When these factors are satisfied, courts are more likely to find “employee” status. In addition, the IRS stated that these 20 factors are not inclusive but that “every piece of information that helps determine the extent to which the business retains the right to control the worker is important.”

a.  **Instructions:** A worker who is required to comply with other persons' instructions about when, where and how to perform the work is ordinarily considered to be an employee.

b.  **Training:** Training a worker indicates that the employer exercises control over the means by which the result is accomplished.

c.  **Integration:** When the success or continuation of a business depends on the performance of certain services, the worker performing those services is subject to a certain amount of control by the owner of the business.

d.  **Services Rendered Personally:** If the services must be rendered personally, the employer controls both the means and results of the work.

e.  **Hiring, Supervising and Paying Assistants:** Control is exercised if the employer hires, supervises and pays assistants.

f.  **Continuing Relationships:** The existence of a continuing relationship between the worker and the employer indicates an employer-employee relationship.

g.  **Set Hours of Work:** The establishment of hours of work by the employer indicates control.

h.  **Full Time Required:** If the worker must devote full time to the employers business, the employer has control over the worker's time. An independent contractor is free to work when and for whom he chooses.

1. **Doing Work on the Employer's Premises**: Control is indicated if the work is performed on the employer's premises.

j.  **Order or Sequenced Set:** Control is indicated if a worker is not free to choose his own pattern of work, but must perform services in the sequence set by the employer.

k.  **Oral or Written Reports:** Control is indicated if the worker must submit regular oral or written reports to the employer.

l.  **Furnishing Tools and Materials:** If the employer furnishes significant tools, materials and other equipment, an employer-employee relationship usually exists.

m.  **Payment by Hour, Week, or Month:** Payment by the hour, week or month points to an employer-employee relationship, provided that this method of payment is just not a convenient way of paying a lump sum agreed on as a cost of a job. An independent contractor usually is paid by the job or on a straight commission.

1. However, hourly pay may not be evidence that a worker is an employee if it is customary to pay an independent contractor by the hour.

n.  **Payment of Business and/or Traveling Expenses:** Payment of the worker's business and/or traveling expenses is indicative of an employer-employee relationship.

1. This factor is less important because companies do reimburse independent contractors

o.  **Significant Investment:** A worker is an independent contractor if he or she invests in facilities that are not typically maintained by employees (such as the maintenance of an office rented at fair value from an unrelated party). An employee depends on the employer for such facilities.

p.  **Realization of Profit or Loss:** A worker who can realize a profit or loss (in addition to the profit or loss ordinarily realized by employees) through management of resources is an independent contractor. The worker who cannot is generally an employee.

q.  **Working for more than one firm at a time:** If a worker performs more than de minimis services for a number of unrelated persons at the same time, he or she is usually considered an independent contractor.

r.  **Making service available to the general public:** A worker is usually an independent contractor if services are made available to the general public on a regular or consistent basis.

s.  **Right to Discharge:** The right of the employer to discharge a worker indicates that he or she is an employee.

t.  **Right to terminate:** A worker is an employee if the right to end the relationship with the principal is available at any time he or she wishes without incurring liability.

**Case Example:**

***Hospital Resource Personnel, Inc., v. United States, 68 F.3d 421 (11th Cir. 1995)***

**Issue:** Whether H.R.P. correctly classified its workers as independent contractors, thus exempting HRP from employment taxes under §530(a)(2)(A) & (1)(B).

**Facts:** H.R.P. is a business which provides specialized nurses to hospitals in need of temporary additional staffing. H.R.P. contracts with approximately fifteen hospitals and does not prescribe the work that the nurses are to perform at the hospitals, nor does it furnish the nurses with uniforms, transportation, journals, sick pay, vacation pay, pensions, bonuses, medical insurance, or licenses. In addition, H.R.P. permits the nurses to be employed directly by the hospitals or to register with other similar nursing agencies or registries. The nurses may choose when, where, and how often they work. H.R.P. pays the nurses according to the number of hours worked at the client hospitals, making the payments on a regular basis, daily or weekly, as the nurses complete a particular job or project. H.R.P. has never withheld federal income or social security taxes from the compensation it pays to the nurses on its registry. Instead, it has always treated the nurses as independent contractors who are not subject to withholding, and at the end of each year has furnished them with information returns on Form 1099, listing all payments made during the year. Following an audit, the IRS assessed employment taxes, plus penalties and interest, in excess of $1,144,000, against H.R.P. for all quarters of the years 1988, 1989, and 1990. The IRS disagreed with H.R.P.'s characterization of the nurses as independent contractors, declaring instead that they were employees subject to withholding.

**Decision:** The court held for the plaintiff (employer). The court found that the employer met the safe haven requirements. The court used the 20 IRS factors to analyze whether the employers were correctly classified as independent contractors. Because the employer rightfully classified the workers as independent contractors, the court held that the employer was exempt from employment taxes under § 530(a)(2)(A) & (1)(B) because of its reasonable reliance on Revenue Ruling 61‑196, judicial precedent, and common law in treating the nurses as independent contractors.

**Case Questions**

*1. What factor did the court consider the most important when determining the classification?*

Although no one factor is definitive on its own, collectively the factors define the extent of an employer's control over the time and manner in which a worker performs. This control test is fundamental in establishing a worker's status

*2. What was at stake for H.R.P. in classifying its workers as employees or independent contractors?*

The assessment of employment taxes, plus penalties and interest, in excess of $1,144,000. In many cases, the employer is looking at past taxes, fines and penalties when a misclassification has occurred. As this case demonstrates, the amounts can be quite substantial.

*3. What did H.R.P. originally rely on in classifying its workers independent contractors? Why must a court use a test, such as the I.R.S. 20 factors when determining whether an employer classified its workers correctly?*

Section 530 of the Revenue Act "safe haven" provisions. These provisions allow taxpayers to treat

workers as independent contractors, even though under the common law they might be considered

employees. An employer can rely on (1) judicial precedent, published rulings, and technical advice (2) long‑standing recognized practice of a significant segment of the industry in which the taxpayer is engaged or (3) common law (§ 530(a)(1)(B)).

When an employer relies on common law to determine the appropriate classification of a worker, the court must assess whether this classification was correct. In order to do that, the court considers the IRS 20 factors.

Under the Economic Realities Test, courts consider whether the worker is economically dependent on the business or, as a matter of economic fact, is in business for him or herself. In applying the economic relatities test, courts look to the degree of control exerted by the alleged employer over the worker, the workers opportunity for profit or loss, the workers investment in the business, the permanence of the working relationship, the degree of skills required by the worker, and the extent the worker is an integral part of the alleged employer’s business. Typically, all of these factors are considered as a whole with none of the factors being determinative.

**Case Example:**

***Baker, et. al. v. Flint Engineering & Construction Company, 137 F.3d 1436 (10th Cir. AC 1998)***

**Issue:** Using the economic reality test, whether Flint Engineering & Construction Company (Flint), correctly classified its workers as independent contractors, thus not entitling them to overtime compensation.

**Facts:** Rig welders working in natural gas pipeline construction industry brought action against general contractor, alleging violation of Fair Labor Standards Act (FLSA) overtime provisions claiming they were employees rather than independent contractors.

**Decision:** The court held for the plaintiffs. The court determined that the plaintiffs were employees of Flint, rather than independent contractors, for purposes of the FLSA. The court used the economic reality test which requires the court to consider (1) the degree of control exerted by the alleged employer over the worker; (2) the worker's opportunity for profit or loss; (3) the worker's investment in the business; (4) the permanence of the working relationship; (5) the degree of skill required to perform the work; and (6) the extent to which the work is an integral part of the alleged employer's business.

**Case Questions**

*1. Do you think the outcome of the case would have been different if the court utilized one of the other tests in determining the classification of the worker as an employee or independent contractor?*

This requires an analysis of each of the tests and depends upon the test used. It is possible, depending on the strength each factor is given with each of the different tests that another outcome would result. This shows the difficulty employers have with wrongly classifying workers.

*2. When the court is considering the factors in the economic reality test, must all factors be consistent with a classification or are the factors weighed?*

No. As with the above case, even though the court found that the workers project is only a short duration and the fact that the workers use special skills (factors considered in the economic realities test) the court weighed the factors with the others in their determination. One or two factors that may indict an independent contractor status are not dispositive of the classification.

*3. The court found dispositive the fact that the rig welders could not work for anyone other than Flint while performing their job, contrast this with the tax code which states physicians are independent contractors. Couldn’t it be argued that a doctor can only work for one hospital at a time and can not work at another simultaneously?*

A doctor is more able to work with several hospitals than a rig welder is able to work on more than one rig at a time. Doctors often contract with several hospitals at a time due to the ease of traveling to one hospital to another (if short distances away) and also their ability to set their own schedules with their patients. This ability is lacking with rig welders.

**Case Example**

## **Trayon Redd v. Summers**

**Issue:** Is a tour guide hired, trained, and paid by a personnel service an employee of the organization for which she provides tours, which jointly supervises her and retains the right to refuse her placement as a tour guide?

**Facts:** The Treasury Department’s Bureau of Engraving and Printing retained Aspen Personnel Services, Inc., to provide tour services at the Bureau. Aspen hired Trayon Redd as a tour guide. Under the contract between Aspen and the Bureau, Aspen was responsible for training, paying wages, providing benefits, and did all the hiring and firing. The Bureau and Aspen both provided on-site supervision, and the Bureau had the right to reject any tour guide.

**Decision:** The Court determined that Trayon Redd was not an employee of the Bureau but of Aspen. The Court noted that while the Bureau did join Aspen in supervising Redd, its degree of control over her work was not excessive.

**Case Questions**

1. *Although the Treasury Department was not found to be Reed’s employer for purposes of employment discrimination, in a related claim, the case was remanded for trial to determine whether Reed was unlawfully denied participation in a federal program or activity or retaliated against for protesting such a denial. What lesson may be learned by federal government agencies contracting with staffing firms?*

Student Discussion. Federal government agencies may be held liable for discrimination in denial of participation in federal programs or activities, independent of employment.

2. How could Banks have avoided this lawsuit brought against the Department of Treasury?

Student Discussion. Banks’ insensitive obesity-related comments to Redd and her mother might have helped to create an adversarial relationship with Summer. Further, the timing of Banks’ recommendation that Redd be terminated looked suspect to Redd, given that her mother had confronted Banks that morning on the phone regarding Banks’ apparent concerns with Redd’s weight. Subjecting Redd to heightened scrutiny on the job after making such obesity-related comments also created an impression of unfairness. While these instances might not in themselves create actual liability, they do foster workers’ perception that they are receiving unfair treatment for which they might seek a legal remedy.

3. *Change the facts of the case to create joint liability between Aspen and the Bureau of Engraving and Printing. Consider the factors weighed by the Court such as supervision and training.*

Student Discussion. Having students revise the facts to create joint liability helps to see where “control of work” of staffing firm workers might create liability.

**Lecture Notes**

Title VII definition of an employee is vague at best, defining an employee as one employed by an employer, with some exclusions related to public office.

a. In addition, while volunteer workers are generally not protected by Title VII, Title VII does apply to volunteer workers where the employer is otherwise subject to the statute and where the volunteer's position generally leads to paid work with the same employer, i.e. where the work is viewed as a training or apprenticeship program.

1. The Court of Appeals for the Second Circuit recently held in Pietras v. Board of Fire Commissioers that a volunteer firefighter constituted an employee for purposes of Title VII since she received a number of job-related benefits, including a retirement pension.

**Lecture Notes**

**Lecture Note:** I would do problems 1, 2 and 9 at this point.

Cash payment is not required in order to classify a worker as an employee. Be sure to point out that the payment received must only amount to consideration and may be clothes, food, and so on.

Notwithstanding all the discussion on how to categorize workers, some workers are considered **"statutory employees"** according to certain statutes and are employees whether or not they would be so categorized under the various tests.

a. For example, officers of corporations are automatically defined as employees for FUTA, FICA and income tax withholding purposes. (Note that then you might have the confusion of whether someone is an "officer" or not.)

b. Real estate agent are statutorily treated as independent contractors only where she or he satisfies two conditions:

1) first, he or she must receive all or substantially all of their real estate-related renumeration as a result of real estate *sales*, rather than on the basis of hours worked;

2) second, the agent and his or her contractor must have a written agreement which provides that the agent is not an employee for federal tax purposes.

c. Further, in the Tax Reform Act of 1978, Congress classified engineers, designers, drafters, computer programmers and systems analysts who work for technical services firms as employees.

d. Similarly, the tax code states that physicians, lawyers, veterinarians, public stenographers, auctioneers and others who follow an independent trade, business, or profession in which they offer their services to the public constitute employees.

**Contingent or Temporary Workers**

1. When utilizing contingent and temporary workers, the advantages and disadvantages must be considered. Although contingency or temporary workers provide a cost savings as a short-term benefit, depending on their classification, they could be entitled to protection under the employment laws. Also, the IRS is really looking at the way employers classify its employees. It’s important to be sure the classification given is the true classification.

**Employment Probation**

1. There are certain circumstances where an individual is considered an employee under the Common Law Test, but still may not be granted the full rights and benefits of an employee. These individuals are called **probationary employees**. There are three situations where probation may occur:
2. initial employment or rehire probation,
3. promotion or transfer probation,
4. and disciplinary probation.

In these situations, the probationary employee, though called an "employee" is not treated the same as a "regular" employee.

The most common form of probation is initial employment or rehire probation. Sometimes, a firm's policies, employment contract, or established workplace practice limit the benefits to which a probationary hire has access, including the denial of medical benefits, lower pay, or the inability to use a grievance procedure in challenging a management decision. During the probationary period, the employee might also be required to demonstrate the ability to do the job for which they were hired. Upon successful completion of the probationary period, the probationary employee is entitled to have all rights and benefits allowed by company policy.

Promotion or transfer probation is similar to initial employment probation in that the promoted employee must demonstrate the ability to perform the new job adequately during the probationary period before they are considered to be in that position on a regular basis. However, promotion/transfer probation differs from initial probation because these employees are already considered regular non-probationary employees, may not be denied certain benefits such as health care, and may not be immediately dismissed for the inability to perform the new job.

Disciplinary probation is a period of conditional employment during which a regular employee has restricted rights due to a disciplinary problem such as insubordination, harassment, and chronic lateness and absenteeism, for example. Typically, disciplinary probation is one of the stages in a progressive discipline policy. Under disciplinary probation, the employee is informed of specific terms and conditions for continued employment; if she or he fails to satisfy those terms, they are terminated.

Probationary periods can vary in duration from 30 days to the discretion of the employer, although typically periods last from 60-90 days. Probationary periods can also be extended at the discretion of the employer; however, reasons for the extension and the terms and conditions of the extension period should be clearly stated.

1. Unionized and government employers, who are not covered under the employment at will doctrine due to their employment contract with their workers, may use probation as a means to screen employees and reserve the right to fire them if they cannot do the job for which they were hired. Piggy-backing off of unionized and government employers, private employers are using probationary employment to maintain some degree of management prerogative in an at-will relationship. The courts have granted employers broad authority to administer probation programs; however, courts do curtail probation programs where an employer is shown to have behaved in a capricious, arbitrary, or discriminatory manner.

Even though employers do not need just cause for terminating a probationary employee, it does not mean these employees have no rights whatsoever. Probationary employees are still protected by Title VII and are also covered under the Age Discrimination in Employment Act and the Americans with Disabilities Act. The Equal Employment Opportunity Commission considers probation simply another form of a selection test; consequently, organizations are held accountable by the EEOC for protecting probationary employees under any legislation affecting the employee selection process.

In order to ensure that a probation system is not considered to be discriminatory or unfairly applied, employers should

1. ensure that the terms and conditions differentiating probationary from regular employees are clear and communicated to the employees,
2. have an accurate and legal performance evaluation system for all employees and document all evaluations, and
3. apply all rules, policies, and procedures in a fair and consistent manner and in compliance with current employment law.

**V. Who Constitutes an Employer?**

1. Depending on the applicable statute or provision, an employer is one who employs or uses others to do his work, or to work on her behalf.

1. Most statutes specifically include in this definition employment agencies, labor organizations and joint labor-management committees.

B. **The Civil Rights Act of 1866**

1. An employer under the CRA of 1866 is one with fifteen or more employees.

C. **Title VII of The Civil Rights Act of 1964**

1. Title VII applies to all firms or their agents engaged in an industry affecting commerce which employ 15 or more employees for each working day in each of 20 or more weeks in the current or preceding calendar year.

2. Title VII exempts from its regulation government-owned corporations, Indian tribes, and bona fide private membership clubs.

3. "Commerce", in this context, is defined as trade, traffic, transportation, transmission, or communication among the states, between a state and any other place, within the District of Columbia or within a possession of the United States.

4. "Industry affecting commerce" means any activity, business, or industry in commerce or in which a labor dispute would hinder or obstruct commerce or the free flow of commerce. Lack of *intent* to affect commerce is no defense to coverage.

5. How are employees counted where the statute applies only to employers with a minimum number of employees?

a. For example, Title VII provides that an employer is covered by the proscriptions of the statute if it employs 15 or more employees for each working day in each of 20 or more calendar weeks in the current or preceding calendar year.

1) But what is a "working day"? It is generally computed by counting the number of employees maintained on the payroll in a given week, as opposed to the number of employees who work on any one day.

2) However, this form of calculation is merely the majority approach; other courts have found that part-time employees who work for any part of each day of the work week should be counted, while part-time employees who work full days for only a portion of the work week should not be counted.

D. **Title VI of the Civil Rights Act of 1964**

1. Title VI applies the race, color and national origin proscriptions of Title VII to any program or activity which receives federal financial assistance. States and state agencies are also covered under the Civil Rights Restoration Act of 1987.

2. Title VI applies where the financial assistance to the program or activity has as its primary objective the provision of employment.

3. The Department of Education, one of the larger federal funding agencies, cites four categories of programs that will be covered by Title VI:

a. Projects under the Public Works Acceleration Act,

b. Work-study programs under the Vocational Education Act of 1963,

c. Programs under other funding statutes that are limited to, or in which a preference is given to students or others training for employment, and

d. Assistance to rehabilitation facilities under the Vocational Rehabilitation Act

4. Unless it falls within one of the five exemptions, a government contractor is also prohibited from discriminating on the bases of race, color, religion, gender or national origin by Executive order 11246. The Order exempts

a. Employers with contracts of less than $10,000.00 from the requirement to include an equal employment opportunity clause in each of their contracts,

b. Contracts for work performed outside the United States by employees not recruited within the United States,

c. Contracts with state and local governments by providing that the EEO requirements do not apply to any agency of that government that is not participating in the work of the contract,

d. Religious educational institutions who hire only people of that religion,

e. Preferences offered to Indians living on or near and Indian reservation in connection with employment on or near the reservation,

1. Certain contracts on the basis of national interest or security reasons.

E. **Age Discrimination in Employment Act of 1967**

1. The ADEA applies to all entities or their agents which employ 20 or more employees on each working day for 20 or more weeks during the current or preceding calendar year.

2. In addition to an exemption similar to that of Title VII for government-owned corporations, the ADEA also exempts American employers who control foreign firms where compliance with the ADEA in connection with an American employee would cause the foreign firm to violate the laws of the country in which it is located.

3. The ADEA does *not* exempt Indian tribes nor private membership clubs, like Title VII.

F. **Rehabilitation Act of 1973**

1. The Rehabilitation Act provides that covered agencies may not discriminate against otherwise qualified disabled individuals and applies not only to all entities, programs and activities which receive federal funds, and government contractors, but also to all programs and activities of any Executive agency as well as the U.S. Postal Service.

a. Federal funding may include grants, loans, contracts, provision of personnel, or real or personal property.

b. A covered federal contractor is one who maintains a contract with the federal government in excess of $2,500.00 for the provision of personal property or nonpersonal services.

c. A contract may include any agreement between any department, agency, establishment, or instrumentality of the federal government and any person. It does not include employment contracts where the parties to the agreement are employer and employee.

2. There is no requirement similar to that of Title VI that the assistance must be for the provision of employment.

**Chapter-End Questions**

*1. Holtzman began working for World Book as a part-times sales representative in 1983. Her position required selling World Book’s educational products. Until 1995, she worked as a part-times sales representative and then a district manager for World Book. In 1995, World Book decided to separate the parent division from the school and library division and reorganize its sales force by “outsourcing:” contracting with individual “regional directors” who would in turn contract with individual sales representatives. The same people who had worked for World Book under the previous arrangement filled many of the positions under the new structure, in which branch managers became separately incorporated regional directors and district managers while sales representatives took positions with the newly formed companies.*

*Holtzman signed a contract with Lee, a former World Book branch manager who had formed her own corporation and gathered a sales force comprised largely of former World Book sales representatives. Holtzman eventually became a territory coordinator, a position slightly above sales representative but still reporting to Lee. In 1998, Holtzman was told that she was losing her territory and would no longer be selling World Book products. Holtzman sued World Book, claiming that the loss of her territory was effectively a termination. What is the result of her lawsuit?*

*Holtzman v. The World Book Company, Inc,* 2001 U.S. Dist. LEXIS 18531 (E.D.Pa. November 13, 2001).

[The Court found that Ms. Holtzman was an independent contractor under the following Darden (1) the lack of reliance by plaintiff upon any instrumentalities or tools provided by World Book; (2) the fact that plaintiff worked from home; (3) the complete discretion by sales representatives like plaintiff over the time and manner of work and general management of their workload; (4) the payment to plaintiff by commission rather than salary; (5) the lack of health or retirement benefits from World Book or Leer Services to plaintiff after 1996; and (6) the admission by plaintiff of self-employment status on her tax records since 1996. ]

*2. A staffing firm provides landscaping services for clients on an ongoing basis. The staffing firm selects and pays the workers, provides health insurance and withholds taxes. The firm provides the equipment and supplies necessary to do the work. It also supervises the workers on the clients’ premises. Client A reserves the right to direct the staffing firm workers to perform particular tasks at particular times or in a specified manner, although it does not generally exercise that authority. Client A evaluates the quality of the workers’ performance and regularly reports its findings to the firm. It can require the firm to remove the worker from the job assignment it if is dissatisfied. Who is the employer of the workers?*

[Student discussion. Students should recognize *Summers* in these facts].

*3. Iowa Pedigree, a partnership owned by Ron and Judy Kirk, is in the business of assisting dog breeders and brokers to comply with American Kennel Club (AKC) and United States Department of Agriculture (USDA) licensing and registration requirements. Iowa Pedigree sought to develop computer software that would aid its customers in conforming to these regulations. Ron Kirk learned that Harter had written a computer program that allowed kennel owners to track information on the dogs bred and sold by the kennel. Kirk asked Harter to develop a computer program for Iowa Pedigree to assist dog brokers with AKC and USDA regulations. Harter agreed and eventually helped Iowa Pedigree develop the software.*

*For the next six years, Harter worked on a variety of projects for Iowa Pedigree. He developed several computer programs, maintained the computers at Iowa Pedigree, and serviced the software of Iowa Pedigree's clients. In 1996, several customers terminated their relationship with Iowa Pedigree and began receiving services directly from Harter. Iowa Pedigree [\*1007] then sued Harter for copyright infringement, misappropriation of trade secrets, and tortuous interference with business expectancies.*

*The Copyright Act provides that an employer is the author when an item is considered a work made for hire. Was Iowa Pedigree the employer of Harter? Kirk v. Harter 188 F.3d 1005 (8th Cir. 1999).*

[The Court used the *Darden* test to determine that Harter was an independent contractor. Throughout his six-year relationship with Iowa Pedigree, Harter continued to engage in computer consulting with other companies, a factor suggesting to the court that he was an independent contractor.]

*4. Julianne Eisenberg was hired by Peter White and Mike Ewing to work on a “permanent, full-time” basis loading and unloading furniture at an Advance Warehouse in 1998. She worked on an hourly schedule, and was paid an hourly wage and received her “orders” from White. However, she did not receive benefits nor was she treated as an employee for tax purposes. On occasion, White would send employees home if there was little to do, or direct them to work on weekends if needed. Sometimes, Eisenberg and other workers would be told to go to another location, where a supervisor would direct their loading and unloading of material.*

*Shortly after starting at Advance, Eisenberg complained about sexual harassment on the job to Joan Isaacson, the company’s office manager. The warehouse was closed down the day after Eisenberg made her complaint. Later, Isaacson told Eisenberg that she would not be asked to return to work if she filed a complaint or hired an attorney to pursue allegations of sexual harassment. Eisenberg retained a lawyer and filed a sexual harassment complaint under Title VII and a state anti-discrimination statute. She was not asked to return to work. Was Eisenberg an employee of Advance, or an independent contractor?*

*Eisenberg v. Advance Relocation & Storage Inc., 237 F.3d 111 (2nd Cir. 2000).*

[The Court held that in determining whether a worker is a covered employee within the meaning of anti-discrimination statutes, special weight should ordinarily be placed on the extent to which the hiring party controls the "manner and means" by which the worker completes her assigned tasks, rather than on how she is treated for tax purposes or whether she receives benefits.]

*5. Franklin Privette hired Jim Krause Roofing, Inc. to install a new tar and gravel roof on his duplex. Using a kettle and pumping device parked in a driveway next to the duplex, the roofing crew transported hot tar to the roof. When the gravel truck arrived, the crew moved the kettle and pumping device to make room for the truck. After the gravel was deposited on the roof, crew members realized they needed 50 more gallons of tar to complete the job. The foreman then directed employee Jesus Contreras to carry 10 five-gallon buckets of hot tar up a ladder to the roof. While performing this task, Contreras fell off the ladder and was burned by hot tar.*

*Contreras sought workers' compensation benefits for his injuries. He also sued Privette, the owner of the duplex, alleging two theories of recovery: that Privette had been negligent in selecting Krause as a roofer; and that, because of the inherent danger of working with hot tar, Privette should, under the doctrine of peculiar risk, be liable for injuries to Contreras that resulted from Krause's negligence. Is Privette liable for the injuries suffered by Contreras?*

*Privette v. Superior Court, 5 Cal. 4th 689 (1993).*

[The Court held that when “ the injuries resulting from an independent contractor's performance of inherently dangerous work are to an employee of the contractor, and thus subject to workers' compensation coverage, the doctrine of peculiar risk affords no basis for the employee to seek recovery of tort damages from the person who hired the contractor but did not cause the injuries. Thus, in this case, roofing employee Contreras is precluded from suing duplex owner Privette for injuries compensable under the workers' compensation system.”]

*6. Paul Hooker was a crane operator. He was employed by a general contractor hired by the California Department of Transportation (Caltrans) to construct an overpass. The overpass was 25 feet wide and the crane with the outriggers extended was 18 feet wide, so Hooker would retract the outriggers to allow other construction vehicles or Caltrans vehicles to pass. Hooker retracted the outriggers and left the crane. When Hooker returned, he attempted, without first re-extending the outriggers, to swing the boom. Because the outriggers were retracted, the weight of the boom caused the crane to tip over. Hooker was thrown to the pavement and killed. Caltrans arguably retained control over safety conditions at the worksite. Assuming that Caltrans negligently retained control over the worksite, is Caltrans liable for Hooker’s death based on negligent exercise of retained control?*

*Hooker v. California Department of Transportation, No. S091601 Supreme Court of California January 31, 2002).*

[The Court held that a hirer of an independent contractor is not liable to an employee of the contractor merely because the hirer retained control over safety conditions at a worksite, but that a hirer is liable to an employee of a contractor insofar as a hirer's exercise of retained control affirmatively contributed to the employee's injuries.]

*7. Alberto Camargo was killed when his tractor rolled over as he was driving over a large mound of manure in a corral belonging to Tjaarda Dairy. Camargo was an employee of Golden Cal Trucking, and Golden Cal Trucking was an independent contractor Tjaarda Dairy had hired to scrape the manure out of its corrals and to haul it away in exchange for the right to purchase the manure at a discount. Plaintiffs, Camargo's wife and five children, sued defendants Tjaarda Dairy and Perry Tjaarda on the theory, among others, that they were* negligent in hiring *Golden Cal Trucking because they failed to determine whether Camargo was qualified to operate the tractor safely. Is Tjaarda Diary liable for Camargo’s death?*

*Camargo v. Tjaarda Diary, 25 Cal.4th 1235 (2001).*

[The Court held that an employee of an independent contractor is barred from bringing a negligent hiring action against the hirer of the contractor. The Court’s reasoned that, as determined in prior cases, the hirer should not have to pay for injuries caused by the contractor's negligent performance because the workers' compensation system already covers those injuries.]

*8. Spivey was a retired carpenter who occasionally drove automobiles from one location to another for automobile dealers. Generally, the dealership would contact Spivey to drive various automobiles to locations designated by the dealerships. Spivey was hired by an Acura dealer to drive a car from Raleigh to Fayetteville. As several cars needed to get to Fayetteville at the same time, several of Spivey's friends were also hired. Spivey was unaware of the route to Fayetteville and planned to follow one of the dealer's employees who was driving a van at the head of the motorcade. The van was intended to bring the drivers home from Fayetteville. As Spivey was driving the car out of the lot, he ran into Brewer, a pedestrian. Brewer filed suit against Acura, which defended itself claiming that Spivey was not its employee. Are they correct? Brewer v. Spivey, 423 S.E.2d 95 (N.C. 1992)*

[The court held that Spivey was an employee of Acura because Acura owned the automobile (giving rise to a presumption of agency) and because Acura could have terminated his employment at any time.]

*9. Christine began working for Pinkerton Security as a security guard in October 1995 when she was 18 years old. Pinkerton Security is a subsidiary of the Exxon Corporation. Christine brought a sexual harassment claim that alleged she had been harassed by an employee of the Exxon facility where she was assigned to work. In her complaint, Christine alleged that she worked at “Exxon/Pinkerton.” She asserted that Exxon employee Daryl was her supervisor on a daily basis and that Pinkerton guards working at Exxon received enhanced benefits from Exxon. Is Exxon liable to Christine if she proves that Daryl sexually harassed her?*

*Kurdyla v. Pinkerton Security, 197 F.R.D. 128 (D.C.N.J. 2000).*

[Kurdyla’s complaint withstood the defendants’ motion to dismiss because, given that a person may be an employee of multiple employers, it is possible for Christine Kurdyla to have been an employee of both Exxon Research and Pinkerton.]

*10. Farlow graduated from law school in 1988 and was employed by Wachovia Bank of North Carolina to represent it. In 1993, Wachovia discussed the possibility of Farlow working as in-house counsel for Wachovia to handle recovery and bankruptcy cases. On her employment application, Farlow disclosed that she had been convicted of two counts of misdemeanor larceny in 1982. Those convictions made it unlawful for her to become an employee of Wachovia without FDIC approval. Wachovia proceeded with its working relationship with Farlow, who closed her private practice and moved on-site with Wachovia. The parties executed a written contract under which Farlow would provide legal services as an independent contractor. Both parties intended that Farlow would not be considered an employee unless the FDIC waiver was obtained. Such a waiver was never sought for Farlow.*

*Farlow was considered an independent contractor for tax purposes and was never paid a salary by Wachovia but instead was paid for the bills she submitted. She received no benefits or compensation for business travel. She used letterhead that designated her simply as an attorney-at-law and did not receive business cards. However, she was provided with on-site office space, support, staff, equipment, and the use of company vehicles. She was paid for continuing education. Wachovia exercised control over the hours in which she had access to her office.*

*After complaining about a sexually and racially hostile work environment, Farlow was terminated. She filed several claims under Title VII. Was Wachovia Farlow’s employer?*

*Farlow v. Wachovia Bank of North Carolina, 259 F.3d 309 (4th Cir. 2001).*

[The Court determined that Farlow was an independent contractor. The Court placed greater weight on the following factors: 1) the financial relationship between the parties in which she was paid not a salary but only in response to her bills, for services actually rendered; 2) the financial relationship between the parties in which Wachovia did not withhold or pay any taxes that are incident to an employment relationship; 3) the financial relationship between the parties in which Farlow did not receive employee benefits such as medical and life insurance; 4) Farlow's filing of income tax returns under a self-employed status; 5) the express intent of the parties as indicated in the contract Farlow signed labeling her as an independent contractor; 6) that Farlow did not work exclusively for Wachovia during her working relationship with it; and (7) that Wachovia exercised no control over the manner of her work.]