

BY:

**MICHAEL BEYGELMAN**  
**PRESIDENT, CEO**

IAMINDEPENDENT, INC.  
P.O. Box 187  
TENAFLY, NJ 07670

TOLL FREE  
(866) 778-2434

FAX  
(509) 756-1156

E-MAIL  
[INFO@IAMINDEPENDENT.COM](mailto:INFO@IAMINDEPENDENT.COM)

[WWW.IAMINDEPENDENT.COM](http://WWW.IAMINDEPENDENT.COM)

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## INDEPENDENT CONTRACTOR RECLASSIFICATION AND JOINT EMPLOYMENT

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# INDEPENDENT CONTRACTOR RECLASSIFICATION AND JOINT EMPLOYMENT

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## OVERVIEW

Often people ask us [iamindependent] to explain the circumstances under which a staffing source ("Supplier") would be considered a joint employer with its client ("Client") under the various labor laws<sup>1</sup>, such that both the Supplier and its Client would share employment responsibility under those laws; it is widely acknowledged that most Clients would like to develop relationships with their Suppliers wherein the Supplier's employees are not considered employees of the Client for any reason whatsoever. This research report, in two parts, will attempt to provide a holistic view of the issues surrounding independent contractor reclassification and joint employment.

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**CONTINGENT WORKFORCE** is a term that refers to a segment of the labor market often characterized as independent contractors, consultants, free lancers, 1099's, independents, temps, free agents, etc. These individuals ("contingent workers") are not permanently employed by a client for whom they provide services; the entrepreneurial ones are either incorporated or self-employed, but for the most part contingent workers are employed by staffing and consulting services providers.

In today's competitive worldwide marketplace, more and more employers are turning to "contingent workers" in an effort to reduce overhead, maintain workforce flexibility, and minimize liability for any potential violation of a worker's rights. The companies that employ these contingent workers offer their services to a variety of corporations, or "client companies<sup>2</sup>." In short, American businesses are increasingly employing people through third parties and on contract basis. This isn't a new phenomenon.

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A great portion of America's buildings, roadways, and railroads were built with non-employee labor. The new millennium continues that tradition and extends it to many categories of work previously reserved for people with "employee" status<sup>3</sup> such as Information Technology professionals, Management and Financial advisors. Why has there been such expanded use of contingent workers by U.S. businesses? It is largely one more example of the pressure on companies to slash costs and increase corporate earnings. In addition, a change in behavior on the part of corporations, that is they are no longer "paternal", has also contributed to the rise of the contingent workforce and has changed our society.

Because industry analysts such as AT Kearney, who in a recent study estimated that corporations will spend \$250 billion on their temporary workforces in 2001, many incumbents who are traditional staffing companies, professional employer outsourcing (PEO) companies and the like, as well as new entrants, have emerged to provide services into this space. This comes as no surprise. U.S. Department of Labor statistics place the current number of contingent workers at 10.3 million, and predict that this number will grow by 142% to 25 million by 2004. Gartner Group predicts that by 2004, 60% of all corporations will use independent contractors for more than half of their IT workforce alone. The Information Technology Association of America (ITAA), among others estimates that the IT Contingent Workforce in itself represents some 2 million individuals.

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Given all the recent innovation in the areas of human capital management (HCM), staffing and managing contingent workers still remains to be a complex process and very expensive, coupled with risk and exposure in the areas of compliance with EEOC, IRS, ERISA, HIPAA and myriad of joint employment and independent contractor related law. For example, the Department of Labor estimates that less than 5% of corporations are legally compliant with ERISA and contract labor laws. It is data such as this that garners attention of corporate officers, which have fiduciary responsibilities to their shareholders to not only keep their companies financially sound, but in compliance with Federal, State and local labor and employment laws as well. For these reasons, among others, executives have begun reassessing the risk and liability of their overall contingent workforce strategy.

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Because independent contractors are not generally protected under the various labor laws, such as Title VII, the ADEA, the ADA, ERISA, and the NLRA, an individual must be an “employee” of the Supplier and/or its Client before he or she may bring a claim under any of these statutes. In this respect, the label used by the parties to describe an individual in an employment contract is not determinative<sup>4</sup>. Instead, the test is whether the Supplier and/or its Client have the right to control the means and manner of the individual’s work. If the Supplier will have the ability to hire and fire; assign work; pay wages; withhold taxes and provide benefits, an employer-employee relationship will exist between the Supplier and the individual.

However, a determination as to whether the Supplier shares a joint employer relationship with its Client will depend on the facts of each assignment and the relationship among the Client, the Supplier and the individual. For example, where the Client retains the right to fire or discipline the individual, or where the Client exercises significant supervisory control over the individual, a joint employer relationship will exist. Where, however, significant supervisory control does not exist, and the individual is subject only to the general control and direction of the Client, a joint employer relationship will not exist. Depending on the nature of the assignment, it will almost always be possible to create an environment where the individual is not deemed an employee of the Client.

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Generally the Supplier maintains an employer-employee relationship with the individuals it hires. To this effect, it controls the hiring, firing, wages and benefits of its employees. In general a Supplier assigns work to some of its employees, while others may find the projects they work on by themselves. The Supplier negotiates with the Client a rate for the work performed by its employee, collects the money due from the Client, and pays the employee an internal rate established by the Supplier. Additionally, a Supplier withholds employment taxes from the employees’ wages, including Social Security, and offers its employees medical benefits, life insurance, profit sharing and 401(k) plans, etc.

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Depending on the nature of each assigned project, the Supplier offers its Client the ability to hire independent contractors [to the Client] in a context free from the legal liability normally associated with these contingent workers. Depending on the amount of supervision and control on the part of the Client, some workers will be able to work from home, while others will have to report to a Client site or some other determined location. Employees who work from home will do so with minimal supervision and will more than likely be using their own tools, i.e. laptops, computer programs, etc., while employees who work on the Client's site are more likely to be supervised by the Client, use the Client's equipment and may have to be present on-site for a set number of hours each day.

## EMPLOYEE VS. INDEPENDENT CONTRACTOR

Generally, independent contractors are not protected under Title VII, the ADEA, the ADA, the NLRA, and ERISA.<sup>5</sup> Before determining whether the Supplier will be a joint employer with its Client, the threshold question is whether the Supplier's worker is an "employee" or an "independent contractor."<sup>6</sup>

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An individual is a covered employee under the various labor laws mentioned above<sup>7</sup> where the right to control the means and manner of his or her work performance rests with the Supplier and/or its Client rather than with the worker him or her self.<sup>8</sup> The right to control test considers all aspects of the alleged employment relationship, including: (1) the alleged employer's right to control the manner and means of performance; (2) the skill required; (3) the source of the instrumentalities and tools; (4) the location of the work; (5) the duration of the relationship between the parties; (6) whether the client has the right to assign additional projects to the hired party; (7) the extent of the hired party's discretion over when and how long to work; (8) the method of payment; (9) the hired party's role in hiring and paying assistants; (10) whether the work is part of the regular business of the hiring party; (11) whether the hiring party is in business; (12) the provision of employee benefits; and (13) the tax treatment of the hired party.<sup>9</sup> The burden is on the individual claiming employee status to prove the existence of an employment relationship.<sup>10</sup>

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Additionally, the most significant factor under this test is the right to control the means and manner of the worker's performance.<sup>11</sup> Once it is established that the Supplier and/or its Client has the right to control the means and manner of the individual's performance, the remaining factors under this test are of marginal importance.<sup>12</sup>

A Supplier generally maintains an employer-employee relationship with each of its workers where the Supplier typically hires the worker, determines when and where the worker should report to work; pays the wages; is itself in business; withholds taxes and social security; provides workers' compensation coverage; and has the right to discharge the worker.<sup>13</sup> The worker usually has a continuing relationship with the Supplier, who pays his or her wages by the hour or week, rather than by the job.<sup>14</sup> Furthermore, the intent of the parties typically is to establish an employer-employee relationship.<sup>15</sup> Where the Supplier does not exercise **any** control over the worker, it will not be considered an "employer."<sup>16</sup>

In general a Supplier will qualify as an "employer" under the facts discussed above. The fact that a Supplier has the ability to hire and fire its workers, pays their wages according to an internal rate it establishes; withholds employment taxes; assigns work; is itself in business; and expects to maintain a continuing employment relationship with the majority of these individuals suggests that a Supplier falls into the general staffing source example discussed above. In the event that a Supplier wishes to avoid an employer-employee relationship with its workers, it would avoid any type of control over these workers.<sup>17</sup>

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**SUMMARY**

In this first part, of a two part series, we discussed what the contingent workforce consists of, why it is on the rise, and what has caused U.S. businesses to reexamine their risks of engaging contingent workers. We defined the relationship between the Supplier and its Client, and established that in order for an individual to bring any type of employee-related legal action, the individual must first establish that he or she is an employee and not an independent contractor, irrelevant of the label the parties place on the relationship. We have also seen that the most significant factor under this test is the right to control the means and manner of the worker's performance.

Part two of this report will cover Joint Employer liability and how to avoid a Joint Employment relationship.

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## REFERENCES

<sup>1</sup>For example, the National Labor Relations Act (“NLRA”); Title VII of the Civil Rights Act of 1964, as amended (“Title VII”); the Age Discrimination in Employment Act (“ADEA”); the Employment Retirement Security Act (“ERISA”); and the New Jersey Law Against Discrimination (“NJLAD”).

<sup>2</sup> Source: Steel Hector, and Davis, LLP – Contingent Workforce Briefing

<sup>3</sup> Source: IDC – Filling the Gap: The Contingent Workforce

<sup>4</sup> See, e.g., Vizcaino v. Microsoft, 120 F.3d 1187 (9th Cir.1997), cert. denied 118 S.Ct. 899 (1998) (agreement acknowledging that the workers at issue are independent contractors did not, by itself, determine workers’ employment status); Maynard v. Kenova Chemical Co., 626 F.2d 359 (4th Cir.1980) (agreements regarding liability for injury to employees not determinative of whether an employer-employee relationship existed under loan servant doctrine).

<sup>5</sup>See 42 U.S.C. §2000e-3(a); Kern v. City of Rochester, 93 F.3d 38 (2d Cir.1996); Spirides v. Reinhardt, 613 F.2d 826 (D.C.Cir.1979).

<sup>6</sup>See *EEOC Enforcement Guidance: Application of EEO Laws To Contingent Workers Placed By Temporary Employment Agencies And Other Staffing Firms*, EEOC Compliance Manual Section N:3319 (12/3/97).

<sup>7</sup>In addition to satisfying the right to control test, the individual must also be a “participant” under an ERISA plan before he may be entitled to benefits. See Wolf v. Coca-Cola Co., 200 F.3d 1337 (11th Cir.2000). An individual is a participant where he or she is an: (1) an employee; and (2) eligible to receive a benefit according to the language of the plan itself. See, e.g., Abraham v. Exxon Corp., 85 F.3d 1126 (5th Cir.1996) (plan excluded “leased employees”); Bronk v. Mountain States Tel. & Tel., Inc., 140 F.3d 1335 (10th Cir.1998) (plan covered only regular employees). An individual who fails on either prong lacks standing to bring a claim for benefits under an ERISA plan. See Wolf, 200 F.3d at 1340.

<sup>8</sup>See *id.* See also Zarnoski v. Hearst Business Communications, Inc., 69 Fair Empl.Prac. Cas. (BNA) 1514 (E.D.Pa.1996) (Title VII); Barnhart v. New York Life Ins. Co., 1998 WL 172785 (9th Cir. Apr. 15, 1998) (ADEA); NLRB v. Town & Country Elec., Inc., 116 S.Ct. 450, 455-56 (1995) (NLRA); National Mutual Insurance Co. v. Darden, 503 U.S. 318, 324, 112 S.Ct. 1344, 117 L.Ed.2d 581 (1992) (ERISA).

<sup>9</sup>See Darden, 503 U.S. at 324.

<sup>10</sup>See Kumar v. Temple Univ. School of Medicine, CA 95-7832, U.S. Dist. LEXIS 13576, \*17 (E.D. Pa. Aug. 29, 1997); EEOC v. Zippo Manufacturing Co., 713 F.2d 32, 35 (3d Cir.1983).

<sup>11</sup>See Amarnare v. Merrill Lynch, Pierce, Fenner & Smith, Inc., 611 F.Supp. 344 (S.D.N.Y.1984); Gutierrez v. Aero Mayflower Transit Co., 22 Fair Empl.Prac.Cas. (BNA) 447, 449 (N.D.Cal.1979).

## REFERENCES

<sup>12</sup>See Amarnare, 611 F.Supp. at 348; Maynard, 626 F.2d at 362 (“the right to exercise control and supervision is still the determinative element”).

<sup>13</sup>See, e.g., Magnuson v. Peak Technical Services, Inc., 808 F.Supp. 500, 508 (E.D.Va.1992); Amarnare, 611 F.Supp. at 349; NLRB v. Western Temporary Services, Inc., 821 F.2d 1258, 1266-67 (7th Cir.1987); Maynard, 626 F.2d at 362.

<sup>14</sup>See id.

<sup>15</sup>See id. See also EEOC Compliance Manual Volume II, Section N:3317.

<sup>16</sup>See, e.g., Astrowsky v. First Portland Mortgage Corp., Inc., 887 F.Supp. 332 (D.Me.1995) (leasing firm was not a joint employer of workers it leased back to original employer where it did not exercise any control over the employees, but merely processed pay checks and withheld taxes).

<sup>17</sup>See id.