Are Your Independent Contractors Actually Your Employees?

Even workers who agree *in writing* to be "independent contractors" may be entitled to employee benefits if their work conditions do not support classifying them as independent contractors.

Just last month, the California Court of Appeal in *Estrada v. FedEx Ground Package Sys., Inc.* (2007)154 Cal.App.4th 1, held that a class comprised of FedEx truck drivers should have been reimbursed over $5 million in job-related expenses even though each driver had signed an Operating Agreement that expressly provided that he/she was being hired as "an independent contractor, and not as an employee…for any purpose."

California Labor Code § 2802 provides that "an employer shall indemnify his or her employee for all necessary expenditures or losses incurred by the employee in direct consequence of the discharge of his or her duties." But the Code does not expressly define "employee" for purposes of this section. So, the Court turned to the common law "control of details" test – which looks to whether the principal has the right to control the "manner and means" by which the worker accomplishes work – to determine whether the drivers were, in fact, employees.

The Court also looked to factors previously set forth in *S.G. Borello & Sons, Inc. v. Dept. of Industrial Relations* (1989) 48 Cal.3d 341. Those factors are: (1) whether the worker is engaged in a distinct occupation or business; (2) whether, considering the kind of occupation and locality, the work is usually done under the principal's direction or by a specialist without supervision; (3) the skill required; (4) whether the principal or worker supplies the instrumentalities, tools, and place of work; (5) the length of time for which the services are to be performed; (6) the method of payment, whether by time or by job; (7) whether the work is part of the principal's regular business; and (8) whether the parties believe they are creating an employer-employee relationship.

FedEx argued that the agreed-upon "independent contractor" classification was valid under these standards, and that the Operating Agreement's provision that "the manner and means of reaching [mutual business objectives] are within the discretion of the [drivers]" was a true statement, because, *inter alia*, the drivers purchased their own uniforms and scanners; bought, painted, operated and maintained their own trucks; and had an entrepreneurial opportunity to make more money depending on how well they performed.

The drivers, on the other hand, argued that the agreed-upon classification was in error, and that the "manner and means" provision of Operating Agreement was false, because, *inter alia*, their jobs did not require any special skills; they were paid weekly and not on a per-job basis; their customers and routes were assigned by Fed Ex; they worked exclusively for FedEx; FedEx was heavily involved in the truck purchasing

process; and while they had a nominal opportunity to profit, those opportunities could be lost at the discretion of FedEx managers for very minor rule violations.

The Court agreed with the drivers, finding that the Operating Agreement was not dispositive because "[i]n practice, . . . the work performed by the drivers is wholly integrated into FedEx's operation. The drivers look like FedEx employees, act like FedEx employees, are paid like FedEx employees, and receive many employee benefits." Thus, "FedEx's conduct spoke louder than its words," and dictated a finding that the drivers were employees notwithstanding their written agreement to the contrary.

In reaching that decision, the Court distinguished several cases in which truck drivers were held to be independent contractors because, in each of those other cases, the drivers were either paid per trip or they could select the frequency of their jobs and could haul for more than one entity.

The Court also disregarded the integration clause in the Operating Agreement, and looked both to FedEx's actual treatment of its drivers and to other documents such as a "Ground Manual" and an "Operations Management Handbook" which set forth detailed policies and procedures (*e.g.*, regarding "the color of their socks and the style of their hair") that the drivers had to follow to remain in good standing.

Finally, the Court noted that "drivers employed by FedEx's competitors (UPS, DHL, and FedEx's sister corporation, FedEx Express) are classified as employees," further supporting its conclusion that the FedEx Operating Agreement was an artifice.

In very stark terms, the *Estrada* decision cautions that employers cannot impose "constraints of an employment relationship . . . in the guise of an independent contractor model." The "independent contractor" label – even when agreed to in writing by the worker – "is *not* dispositive and will be *ignored* if their actual conduct establishes a different relationship."

And, while *Estrada* is a California decision based on a California Labor Code provision, this issue is not limited to California because ERISA and the Social Security Act (for example) similarly do not provide a helpful definition of the term "employee." *Nationwide Mutual Ins. Co. v. Darden*, (1992) 503 U.S. 318. Thus, employers in and outside of California must be certain that their "independent contractors" are not actually employees regardless of what their contracts might say.

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