



*presents*

# Worker Misclassification: Recent Trends in Independent Contractor Lawsuits

## Trial and Settlement Strategies for Individual, Collective and Class Action Litigation

### A Live 90-Minute Teleconference/Webinar with Interactive Q&A

#### Today's panel features:

Jonathan A. Keselenko, Partner, **Foley Hoag**, Boston  
Douglas Weiner, Senior Trial Counsel, **Epstein Becker & Green**, New York  
Dean L. Silverberg, Member, **Epstein Becker & Green**, New York

### Tuesday, April 27, 2010

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**1 pm Eastern**

**12 pm Central**

**11 am Mountain**

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# Worker Misclassification: Recent Trends in Independent Contractor Litigation

Jonathan A. Keselenko

Foley Hoag LLP

## Classification Disputes: A Growing Problem

- Economic downturn has led many businesses to increase reliance on independent contractors.
- If done properly, this can save money on payroll taxes and employee benefits.
- But misclassification can be extremely costly:
  - Recent high-profile lawsuits brought by disgruntled workers, including class actions and multi-district litigation.
  - Employers forced to pay damage awards and settlements in the tens of millions of dollars.
  - Obama administration announced \$25 million initiative to curb misclassification by bolstering enforcement at the state and federal levels.
  - IRS will conduct 6,000 additional audits this year in effort to combat misclassification.
  - Pending legislation in Congress would increase fines and penalties for misclassification by up to a factor of ten.
- Misclassification problems can occur in any industry and affect both overtime-exempt and non-exempt workers.

## Notable Cases: UPS and FedEx Ground

### ■ UPS:

- Federal class action lawsuit brought in California.
- Plaintiffs are class of 660 UPS truck drivers alleging company misclassified them as independent contractors.
- Settled for **\$12.8 million** in December 2009, including \$1.7 million in attorneys' fees and \$325,000 in costs.

### ■ FedEx Ground:

- Ongoing litigation in 28 states over misclassification of drivers as independent contractors.
- Company faced with class actions as well as individual suits.
- Plaintiffs seek mainly compensation for denial of ERISA benefits provided to FedEx employees, plus some alleged wage and overtime violations.
- One class action settled for **\$27 million** in 2008, including \$14.5 million to the drivers themselves and \$12.5 million in attorneys' fees and court costs.
- FedEx Ground also faces investigations by several state Attorneys General and the IRS; total financial penalties could reach upwards of \$1 billion.

## Notable Cases: Microsoft

- Ongoing legal problems with misclassification stemming from IRS investigation in late 1980s, which resulted in assessment of fines and back employment taxes.
- Had hired many software engineers as “independent contractors.” IRS investigation prompted them to claim misclassification in protracted series of lawsuits.
- Agreements with some plaintiffs and the IRS during the 1990s led Microsoft to change many of its practices, including hiring some of the misclassified workers as regular employees.
- Even with changes in practices, Microsoft’s legal woes spanned nearly two decades. In 2007, entered a \$97 million settlement with eight former misclassified software engineers. The settlement compensated them for their improper exclusion from the company’s ERISA plans.

## Other Cases and Settlements in the Headlines

### ■ Grocery Chain Litigation

- Class action lawsuit brought by 2,100 allegedly misclassified janitors, many of whom were undocumented immigrants.
- Claims for FLSA overtime violations
- 2005 settlement between plaintiffs and Ralph's, Vons and Albertsons for **\$22.4 million**

### ■ Northwestern Mutual:

- \$200 million federal class action suit brought in July 2009.
- Plaintiffs are former life insurance salespeople and financial representatives.
- Alleges minimum wage violations and failure to pay overtime.
- Case is still pending.

### ■ Comcast

- Federal class action suits pending against Comcast and subcontractor TriWire.
- Plaintiffs are former cable installers
- Allege FLSA wage and overtime violations as well as violations of state labor laws.
- Plaintiffs seek actual and punitive damages; exact amount unknown but reach the tens of millions of dollars.

## Independent Contractors Under the FLSA

- The Department of Labor uses the following six-factor “economic realities” test for determining a worker’s independent contractor status:
  - The degree to which the person is independent or is controlled by the employer with respect to the way the work is done;
  - The individual's opportunities for profit or loss;
  - The individual's investment in the facilities and equipment of the business;
  - The permanency and length of the relationship between the business and the individual;
  - The degree of skill needed to do the person's work; and
  - If, and how much, the work performed by the individual is a major part of the employer's business.
  
- No one factor is determinative
  
- Language used by the parties to describe their relationship is not determinative.

## Other Tests for Independent Contractor Status

- IRS: 20-factor test, incorporating six FLSA factors plus 14 others, found at Rev. Rul. 87-41, 1987-1 CB 298.
- ERISA claims: 12-factor common-law test, incorporating elements from FLSA test and Restatement of Agency. Nationwide Mut. Ins. Co. v. Darden, 503 U.S. 318, 323-24 (1992).
- State common law
- State statutory law

# Damages and Theories of Recovery

- Wage and Hour Claims Under the FLSA
  - Misclassification of independent contractors can jeopardize FLSA compliance, particularly for workers in job classifications that would otherwise be non-exempt.
  - Typical problem scenario: Employer hires “independent contractors,” assuming then it does not need to make exemption determination or worry about hourly wage rates or overtime. Workers dissatisfied with perceived long hours, menial duties, or low pay claim misclassification.
  - Employee vs. independent contractor status determined based on six-factor FLSA test.
  
- Commonly-litigated Issues:
  - Failure to pay minimum wage.
  - Failure to pay overtime.
  - Minimum wage and overtime claims often brought simultaneously.

# Damages and Theories of Recovery

## ■ Benefits Claims

- Employers who offer benefit plans to regular employees may face liability if misclassification causes them to deny plan eligibility to purported independent contractors.
- Workers may recover the cost of benefits for which they would have been eligible had they been classified correctly.
- Per *Microsoft*, this affects workers who are performing similar or identical tasks to those performed by the employer's regular, benefits-eligible employees.
- Common claims:
  - Health plans
  - Retirement plans or pension funds
  - Profit sharing/stock options
- Employee vs. independent contractor status may be evaluated under common-law standard for ERISA claims or relevant state law, depending on nature of benefit plan at issue.

# Damages and Theories of Recovery

## ■ Attorneys' Fees

- Successful plaintiffs are commonly awarded attorneys' fees.
- Attorneys' fee awards can be very substantial, particularly in class action and/or multidistrict litigation.
- Recent fee awards have topped \$10 million.

## ■ Court Costs

- Also commonly recovered by successful plaintiffs.
- Six-figure cost awards are not unusual.
- Misclassification litigation can stretch on for a decade or more, e.g. FedEx, Microsoft, and thus, may be extremely costly even for employers who ultimately prevail.

## ■ Punitive Damages

- Intentional misclassification can theoretically result in treble damages or other punitive damage assessment.
- Lack of single “bright line” legal test for independent contractor status makes intent difficult to prove.
- In general, recent cases are not alleged to have been intentional.

## Other Misclassification Issues

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### ■ Government Investigations

- Many state Attorneys General have publicly committed to investigating and curbing misclassification.
- Investigations may generate negative publicity and can result in civil citations and hefty fines.
- In some states, the Attorney General may have the option of bringing a court action against non-complying employers.
- Criminal penalties available in some states.

## Other Misclassification Issues

### ■ Tax Consequences

- The IRS has also publicly stated it intends to step up enforcement of worker misclassification rules, in particular committing to performing additional, targeted audits in the coming year.
- If a tax violation is found, employers may be assessed fines and penalty fees and be held liable for years of back payroll taxes on misclassified workers.
- For employers who offer tax-qualified benefit plans, misclassification of workers who would otherwise be eligible for plan enrollment may jeopardize those plans' tax-qualified status.

## Projected Trends and Developments

- Worker misclassification disputes will likely continue to gain prominence in the months ahead, with several large-scale lawsuits still pending and lawmakers on the federal and state levels turning their attention to the issue.
- In many recent cases, the filing of a misclassification lawsuit by a disgruntled worker has served to “tip off” not only other, potentially similarly-situated plaintiffs, but also lawmakers and government agencies, sometimes even spurring an investigation by the latter.
- Similarly, an Attorney General or IRS investigation may alert a potential plaintiff to a possible misclassification claim.
- Given this legal and regulatory environment, employers will want to be especially cognizant of potential misclassification claims going forward.



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# Litigation and Settlement Strategies for Worker Misclassification Lawsuits

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# Litigation and Settlement Strategies for Worker Misclassification Lawsuits

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- The issue of worker misclassification is continuing to skyrocket in both public and private litigation.
- The US Department of Labor has initiated the “We Can Help” promotional campaign designed to raise public awareness of workers’ rights.
  - States have identified worker misclassification as a “major problem” in need of increased scrutiny and enforcement.

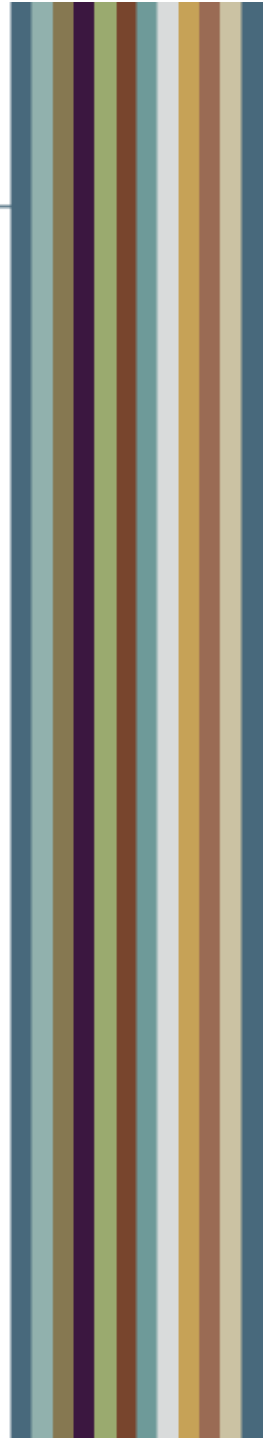


# Litigation and Settlement Strategies for Worker Misclassification Lawsuits

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Private litigation has even outpaced the fast pace of increased government activity.

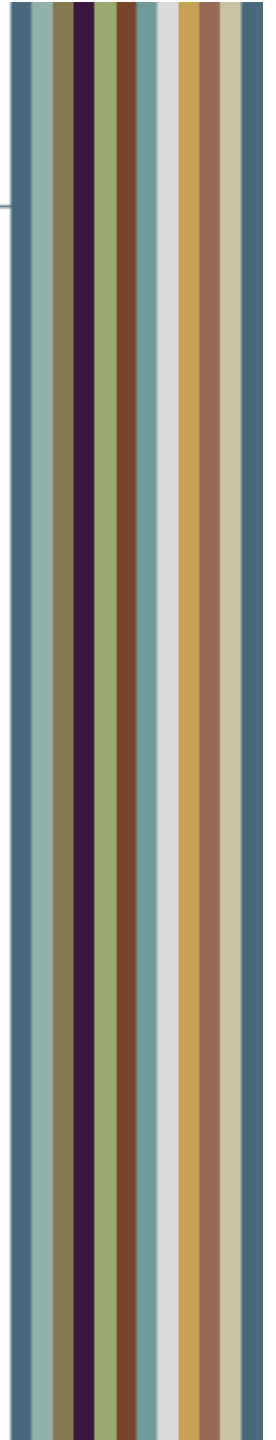
- Public awareness of the issue is at an all time high.
- Employers have relied upon established business models that were unquestioned for generations. These models may leave employers in entire industries vulnerable to current wage hour claims.



# Litigation and Settlement Strategies Work Best When They Work Together

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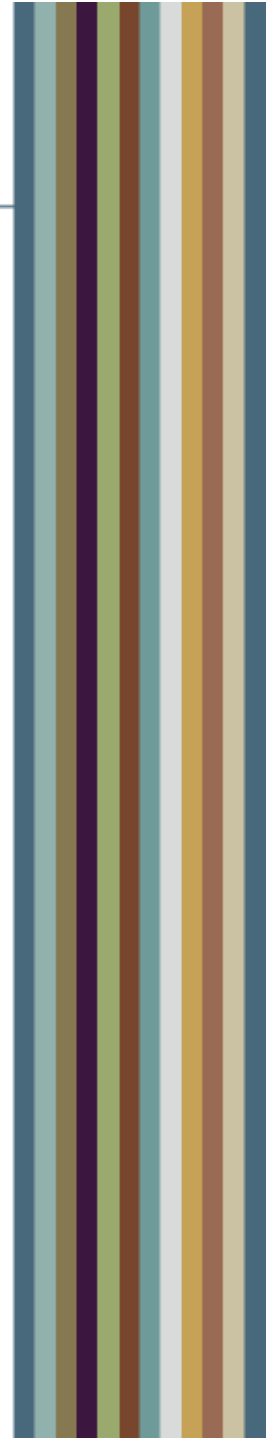
- Litigation and settlement strategies are most effective when implemented in a complementary manner designed to achieve the ultimate goal of a final resolution of the claim, and closure to the problem.
- The most effective litigation strategy uses a settlement component, and the most effective settlement strategy uses litigation to secure the best terms.



# Individual, collective or class action?

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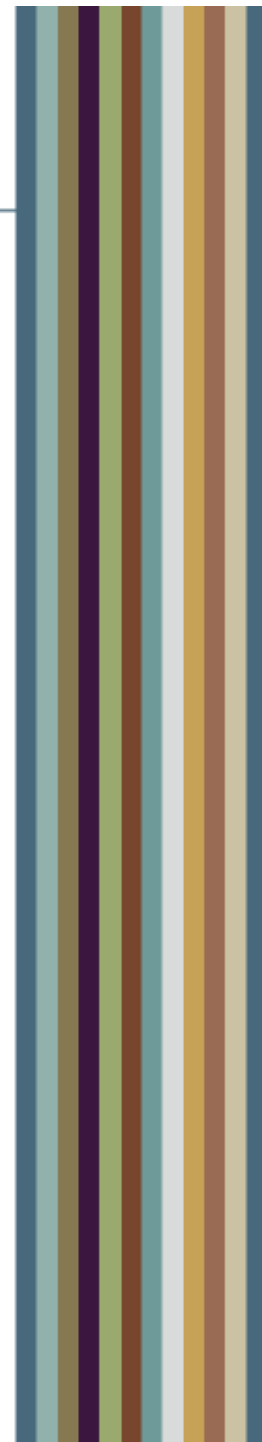
1. An individual action is a claim from a single worker.
2. A collective action is one under the federal wage-hour law, the Fair Labor Standards Act, where a worker brings an action on behalf of himself and all those “similarly situated”. Only workers who actually sign a written Consent to Sue declaration, and file it in court, may join the lawsuit.
3. A class action is one that alleges numerous workers have common questions of law and fact and should all be adjudicated together in one lawsuit as a single class.



# Class Certification Strategies.

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- Limit Exposure to Unspecified Claims
- Limit Exposure to Unidentified Claimants
- Limit Exposure



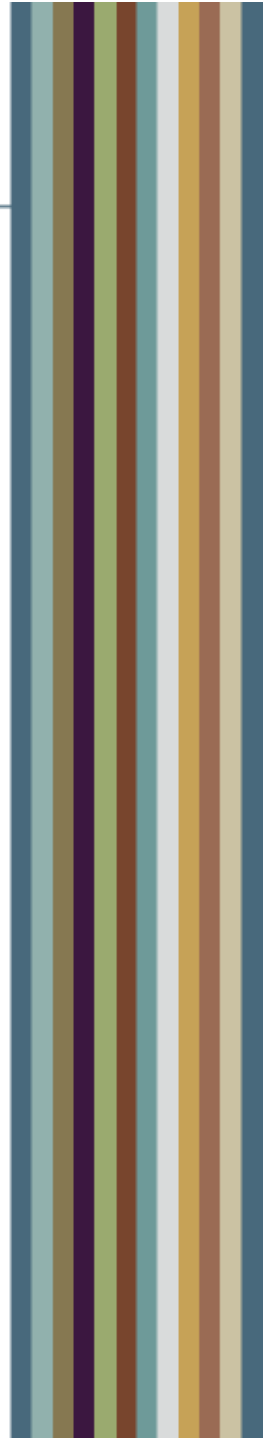
# Class Certification

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## Plaintiffs Motion For Conditional Preliminary Class Certification

The plaintiff must “make a modest showing” that:

1. there are numerous workers who have
2. common questions of law and fact, and that
3. the named plaintiff is typical of the common questions of the case
4. plaintiff and counsel are adequate to represent the class

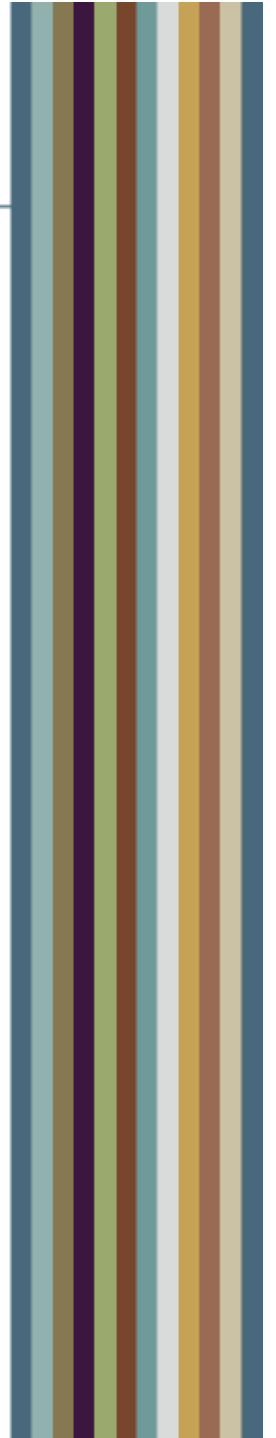


# Class Certification

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## Defendants' Motion For Class De-certification

- After mailing notice of lawsuit
- Evaluate claims of those who filed opt-in Consents to Sue
- Where claims are from dissimilar workers, move to de-certify the class

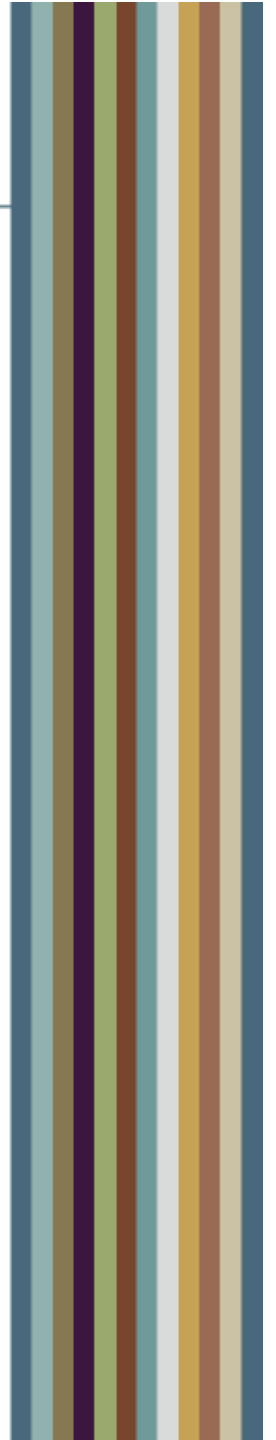


# Litigation and Settlement Strategies for Worker Misclassification Lawsuits

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## Multidistrict litigation considerations—

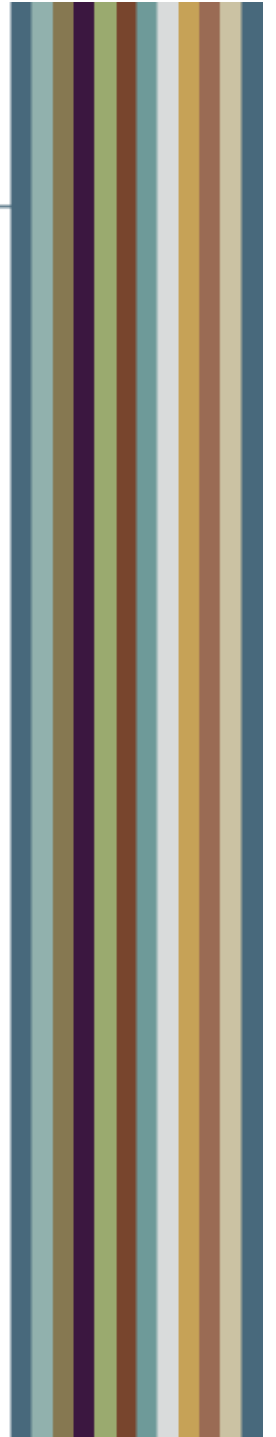
- A high profile case against a nation-wide enterprise in California may spawn copy cat cases in New York, Florida or elsewhere.



# Plaintiffs' Attorneys' Fee Awards

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- The FLSA is a cost shifting statute. A “prevailing party” may recover reasonable costs, including attorneys’ fees, from the employer.
- Accordingly, early assessment of risk with a view toward early resolution may be advisable where claims have a strong potential for merit.
- Attorneys fees need to be part of the calculation for settlement considerations.
- When an issue is resolved in a Government investigation, there are no plaintiffs’ attorneys’ fees





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**DOUGLAS WEINER** is a Senior Trial Counsel in the Labor and Employment practice in the Firm's New York office. He has 30 years of federal wage and hour litigation experience. Mr. Weiner:

- Provides compliance advice and counsel to employers to avoid litigation
- Defends class actions in federal and state courts
- Defends FLSA collective actions in arbitrations
- Defends government contract investigations involving prevailing wage requirements
- Negotiates settlements of law enforcement and class and collective actions

As Senior Trial Attorney for the New York Regional Solicitor's Office of the U.S. Department of Labor (DOL), Mr. Weiner was the lead prosecutor on the Northeast Region's most significant and difficult wage and hour and whistleblower cases, including those pursuant to Sarbanes-Oxley, OSHA and the Fair Labor Standards Act. Mr. Weiner's past experience includes:

- Litigating federal wage and hour matters, including complex FLSA actions involving misclassified employees, tip credit issues, "off the clock" working time, government contract requirements, *inter alia*
- Conducting many trials as first chair prosecutor of actions brought by the U.S. DOL in the U.S. District Courts for the Districts of New York, New Jersey and Puerto Rico
- Successfully resolving through settlement negotiations hundreds of cases involving a wide variety of wage and hour and whistleblowing issues
- Guiding Wage - Hour agency officials in their most challenging investigations
- Guiding OSHA agency officials in their most complex whistleblower investigations

**Awards and Appointments**In 2004, the Solicitor of Labor presented Mr. Weiner with the U.S. DOL's National Award for Excellence in Trial Litigation for being the DOL's "top gun" trial attorney. Additionally, during the last 13 years of Mr. Weiner's federal career, he was awarded the Secretary's Exceptional Achievement Award for excellence in Fair Labor Standards Act litigation nine times, including awards for the following: (i) FLSA litigation in the restaurant and car wash industries; (ii) guiding U.S. DOL officials in managing hundreds of cases; (iii) tip credit and overtime litigation in the catering industry; (iv) off-the-clock work in retail establishments; (v) FLSA litigation involving retaliation and overtime in manufacturing facilities; (vi) FLSA litigation in the wholesale warehouse and delivery industry (Mr. Weiner won the *Secretary of Labor v. Harold A. Levinson Associates* case after a full trial, and prevailed again in a remand proceeding involving overtime calculations. Both judgments were affirmed by the U.S. Court of Appeals for the Second Circuit. The U.S. Supreme Court denied a Petition for Writ of Certiorari in the case); (vii) Davis Bacon and Related Acts (DBRA) litigation involving prevailing wage rate issues on federally funded construction projects and (viii) FLSA litigation involving misclassified employees in the retail supermarket industry (Mr. Weiner won the *Secretary of Labor v. Waldbaum* case after a full trial. The judgment was affirmed by the U.S. Court of Appeals for the Second Circuit).

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# **Worker Misclassification: Recent Trends in Independent Contractor Lawsuits**

***Trial and Settlement Strategies for Individual,  
Collective and Class Action Litigation***

***Best Practices To Limit Liability***

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# BEST PRACTICES TO LIMIT LIABILITY

# WHERE'S THE BEEF?

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- February 18, 2010 *New York Times* front page article.
- Obama administration cracking down on employee misclassification.
- Employers who misclassify will be investigated and may be subject to penalties, higher tax assessments, periodic audits, employee benefit plan disqualification.
- Numerous state agencies have also aimed their sites at investigation and enforcement.

# CONSIDER THESE SIGNIFICANT NUMBERS

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- 3.4 million: Federal study concluded that number of workers were misclassified as independent contractors
- 30 percent: Department of Labor estimates that up to that percentage of companies misclassify workers

\* \* \*

Plaintiffs (your employees) and their attorneys are ready!

# PREVENTIVE MAINTENANCE: CONDUCT YOUR INTERNAL AUDIT

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- Assess The Workforce and Business Model
- Scrutinize The Workforce: Critical Eye and Devil's Advocate
- Check For Inconsistencies
- Research Industry Standards

# CONTRACTOR RELATIONSHIPS

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- Single Consultant
- Incorporated Consultant
- Incorporated Entity Groups
- Staffing Agencies
- Professional Employer Organizations (“PEOs”)

# Is Your House In Order: Proper Documentation

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- Incorporated Entities – (reprise)
- Agreements with Staffing Agencies and PEOs
- Independent Business Entities
  - Listing/Website
  - Address
  - Telephone Number
- Invoicing
- Payment
- Independent Contractor/Consultant Agreement (more to follow)

# Agreements With Staffing Agencies and PEOs

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- Not The Panacea
- Creates a “Distance and a Perception”
- Spell out Rights and Obligations
  - Interviewing
  - Payrolling
  - Insurance
  - Employee Benefits (Economic Scale)
  - Indemnification
- Employment vs Dual/Joint Employment
- Joint Liability

# SPECIAL IMPACT ON EMPLOYEE BENEFIT PLANS

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- Affects maintenance and operation of all types of employee benefit plans
- Covering workers who are not “employees” places the tax-favored status of the plan at risk
- Excluding from participation workers who are eligible “employees” can place the tax-favored status of the plan at risk, and give rise to claims for benefits

# SO WHAT DO YOU DO?

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- Employers not precluded from including plan language to exclude certain groups of individuals from participation
- Plan “Fail-Safe” Language
  - Expressly define terms and exclude independent contractors
  - Contractors excluded from plan participation, even if subsequently reclassified as a common-law employee

# SO WHAT DO YOU DO?

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## Example of this type of language:

- “If an individual not classified by the Company or a Participating Employer 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 then only if he otherwise satisfied the requirements of this Section.”

# IF WORKERS HAVE BEEN MISCLASSIFIED UNDER RETIREMENT PLANS

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- Rev Proc 2008-50: IRS Employee Plans Compliance Resolution System (“EPCRS”)
  1. Self Correction Program (“SCP”)
  2. Voluntary Correction Program (“VCP”)
  3. Audit Cap – Correction on audit

# RESTRUCTURING TO REDUCE OR ELIMINATE CONTROL

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- Business Models
- Operationally and Not Just In Theory

# Sample Agreement Highlights

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- Commercial Relationship
- Services vs Duties/Jobs
- Delineate Fees and Invoicing Procedure
- Confirm Status
- Fees and Tax Obligations to Contractor
- No Benefit Entitlement
  - Handbook Benefit Programs
  - Employee Benefit Plans

# SAMPLE AGREEMENT HIGHLIGHTS (CONTINUED)

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- Non Exclusivity
- Site of Services
- Control (Result rather than means, manner & method)
- Termination of Services

-BLUE-

# Reclassifying Contractors As Employees on a Prospective Basis

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- Timing of Reclassification
- Operational Issues
- Delineation of Worker Classification
- Compensating for Past Liability: A Two Edged Sword

# RED FLAGS

- Split Years
- “Active” Retirement

# PARTING WORDS

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Be Careful Out There!!

