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Employer Misclassifies Workers as Independent Contractors

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In *JKH Enterprises, Inc. v. Department of Industrial Relations* (2006) 142 Cal. App. 4th 1046, a courier service classified its drivers as independent contractors, but the Sixth District Court of Appeal held that the drivers were employees entitled to workers' compensation insurance.

Facts

JKH Enterprises, Inc., a courier company, classified its drivers as independent contractors. The drivers filled out a form entitled "Independent Contractor Profile" and an application wherein the driver acknowledged that he or she was an independent contractor. The driver provided his or her own automobile insurance information. The drivers' primary responsibility was to pick up delivery items from JKH's customers and deliver the packages to designated locations.

JKH divided its drivers into two categories -- "route" and "special." The route drivers regularly serviced the same route or territory and JKH paid them a negotiated amount per hour depending on the mileage, time, and volume of deliveries usually involved in the particular route. JKH did not require the route drivers to contact JKH's dispatcher on a regular basis because in the course of servicing the regular routes, they picked up the packages from JKH's route customers and the customers directed them where and when to deliver the packages. The route drivers decided how to cover their territories and JKH learned of the route drivers' particular deliveries the next day through their "document registers." JKH's route customers also provided the company, for billing purposes, with information about the driver's time spent on the customers' deliveries.

The special drivers made "special" deliveries which JKH's customers requested on any given day. The special drivers would call JKH on their own cell phone on a daily basis to let JKH know whether they were available to work that day. If they were available, the special drivers would receive assignments. However, they were still free to decline to perform a particular delivery even if the driver had indicated his or her availability. JKH did not require the special drivers to work on any particular schedule. They were paid their individually negotiated commissions based on the deliveries made.

Neither the special drivers nor the route drivers were governed by particular rules and they did not receive direction from JKH about how to perform the delivery task or what driving routes to take. Both special and route drivers used their own vehicles to make the deliveries. They paid for their own gas, car service and maintenance, and insurance. The drivers did not wear uniforms and the drivers' cars did not bear any JKH marking or logo. They did not receive any particular training. They set their own schedules and selected their driving routes. They were not supervised and were not required to report to JKH's location. The drivers took time off when they wanted to and they were not required to work on a given day. The drivers were paid twice a month, no withholdings were taken, and they were issued a federal tax form 1099 rather than a W2. The drivers turned in their delivery logs and JKH kept track of those in order to bill its customers. However, the drivers did not fill out or turn in any time sheets.

In 2004, a Deputy Labor Commissioner conducted an inspection of JKH. As a result of his inspection, the Deputy found that the drivers were making the deliveries for JKH, performing the actual work of JKH's day-to-day business and thereby under JKH's general control. The Deputy further found that the drivers were not actually functioning as independent contractors, but rather were employees. Consequently, the Deputy concluded that JKH was obligated to provide a policy of workers' compensation insurance for the drivers' benefit. He issued a "Stop-Order-Penalty Assessment" and fined JKH $16,000 for each of the 16 driver-employees.

JKH contested the order and requested a hearing before the Department of Industrial Relations. However, relying on the factors enumerated in *S.G. Borello & Sons, Inc. v. Department of Industrial Relations* (1989) 48 Cal. 3d 1288, the hearing officer stated:

> **Although some of the factors in this case can be indicative of the workers being independent contractors, the overriding factor is that the persons performing the work are not engaged in occupations or businesses distinct from that of [JKH]. Rather, their work is the basis for [JKH's] business. [JKH] obtains the clients who are in need of delivery services and provides the workers who conduct the service on behalf of [JKH]. In addition, even though there is an absence of control over the details, an employee-employer relationship will be found if the [principal] retains pervasive control over the operation as a whole, the worker's duties are an integral part of the operation, and the nature of the work makes detailed control unnecessary. (Citation omitted.)**

JKH petitioned the trial court for a writ of administrative mandate. The trial court held that there was substantial evidence to support the Department's determination and denied the writ. JKH appealed that decision to the Sixth District Court of Appeal.

Appellate Court's Analysis

The Appellate Court upheld the stop order. The court observed that the common law emphasis on the hirer's degree of control over the details of the work in the determination of an employment relationship remains significant. However, the court further observed that it was not the only factor to be considered in light of the history and remedial and social purposes of the

Workers' Compensation Act. The court noted that, unlike common law principles, the policies behind the Act are not concerned with "an employer's liability for injuries caused by his employee." Instead, the court noted that the policies behind the Act concern "'which injuries to the employee should be insured against by the employer. [Citations.]....' [Citations.]" *Ibid*. The court noted that the question of employment status must be decided with deference to the "purposes of the protective legislation" which is comprehensive coverage of injuries in employment. The court further noted that the Act accomplishes this goal by defining "employment" broadly in terms of "service to an employer" and by including a general presumption that any person "in service to another" is a covered "employee."

In upholding the stop order, the appellate court focused on the factors in *S.G. Borello & Sons, Inc. v. Department of Industrial Relations, supra*, which include:

> **(1) whether there is a right to fire at will without cause; (2) whether the one performing services is engaged in a distinct occupation or business; (3) the kind of occupation, with reference to whether, in the locality, the work is usually done under the direction of the principal or by a specialist without supervision; (4) the skill required in the particular occupation; (5) whether the principal or the worker supplies the instrumentalities, tools, and the place of work for the person doing the work; (6) the length of time for which the services are to be performed; (7) the method of payment, whether by the time or by the job; (8) whether or not the work is a part of the regular business of the principal; (9) whether or not the parties believe they are creating an employer-employee relationship; (10) whether the classification of independent contractor is bona fide and not a subterfuge to avoid employee status; (11) the hiree's degree of investment other than personal service in his or her own business and whether the hiree holds himself or herself out to be in business with an independent business license; (12) whether the hiree has employees; (13) the hiree's opportunity for profit or loss depending on his or her managerial skill; and (14) whether the service rendered is an integral part of the alleged employer's business. (Citation omitted).**

Upon evaluating the *Borello* factors, the appellate court concluded that the functions performed by the drivers did not require a high degree of skill and that the functions constituted the integral heart of JKH's business. The court was not persuaded by JKH's arguments focusing on its lack of control over the drivers' work.

CONCLUSION

Employers must carefully consider the *Borello* factors in determining whether to classify their workers as independent contractors because the consequences of misclassifying can be costly. Not only is the employer on the hook with workers' compensation but there are also various wage and hour requirements, including but not limited to, meal and rest period requirements and overtime, for which an employer is liable when an employee has been misclassified.