MILLER CANFIELD

How Independent Are Your Contractors?

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As businesses of all sizes utilize contingent workers to maintain payroll flexibility, heightened focus by the government on employee misclassification may expose employers to legal challenges, tax liabilities, penalties, and fines.

Virtually all automotive companies are covered by the Fair Labor Standards Act (FLSA). The FLSA requires that employees receive no less than the current minimum wage and not less than one and one-half times their regular rate of pay for all hours worked in excess of 40 hours per workweek (overtime). Exempt executive, administrative, and professional employees who meet certain tests regarding their job duties and are compensated on a salary basis, are not subject to minimum wage and overtime requirements.

Because independent contractors are also exempt from coverage under wage and hour laws, many automotive companies, especially new market entrants, looking to save costs during these tough economic times turn to the common practice of classifying certain individuals as "independent contractors." However, labeling someone an independent contractor does not mean that an automotive company is not the employer.

Whether an employment relationship exists under the FLSA depends on an "economic reality" test

- whether a worker's services are an integral part of the company's business
- the permanency of the relationship
- the amount and extent of the worker's investment in facilities and equipment
- the nature and degree of a company's control over the worker
- whether the worker has an opportunity for profit and loss and
- the degree of skilled involved

The exposure arising from independent contractor relationships does not end with potential liability for past wages and employment taxes. There is also potential for liability based on a joint employment status under other employment and labor statutes and current collective bargaining agreement obligations.

Generally speaking, a direct employment relationship provides the usual basis for liability under state and federal employment discrimination statutes such as the Michigan Elliott-Larsen Civil Rights Act (ELCRA) and Title VII of the Civil Rights Act of 1964 (Title VII). Automotive companies typically would not have statutory obligations with respect to independent contractors or employees of other entities (such as engineers hired through a third party). However, state and federal courts have adopted several doctrines under which an entity that does not directly employ an individual may nevertheless still be subject to liability under one or more of those statutes. These include the "single employer" or "integrated enterprises" doctrine, the "joint employer" doctrine, and common law agency principals.

Current collective bargaining agreement obligations

Most automotive companies are well aware of obligations under existing collective bargaining agreements. Nevertheless, prudent managers should review current collective bargaining agreements covering the job classifications in which the company intends to place workers through a direct independent contractor relationship, or through a third

party, to clarify any ambiguity that might affect its ability to contract with third parties to provide services. Failure to recognize a labor agreement's limitations on contracting for services (directly or indirectly) through a third party could lead to unfair labor practice charges and/or breach of contract grievances.

What should you do if you have existing independent contractors?

Now is the time to ensure compliance with the FLSA. Employers are noticing an increase in wage and hour claims by terminated individuals. Automotive companies should consider conducting an immediate review of their current pay practices to ensure overall compliance with the FLSA and, in particular, that all employees, contractors, and third-party relationships are properly categorized.