CALIFORNIA UNEMPLOYMENT INSURANCE APPEALS BOARD
P O Box 944275
SACRAMENTO CA 94244-2750

NCM DIRECT DELIVERY
Petitioner

Precedent Tax Decison No.: P-T-495
OA Decision No.: 972570

EMPLOYMENT DEVELOPMENT DEPARTMENT
Respondent

DECISION

Attached is the Appeals Board decision in the above-captioned case issued by Board Panel members:

ANN M. RICHARDSON

TERRI M. CARBAUGH

JACK D. COX

LIZ FIGUEROA

FRED AGUIAR

CINDY MONTANEZ

Pursuant to section 409 of the California Unemployment Insurance Code, AO-110555 is hereby designated as Precedent Decision No. P-T-495.

Adopted as Precedent: May 8, 2007

Case No.: AO-110555
Petitioner: NCM DIRECT DELIVERY, INC.

ISSUE STATEMENT

Petitioner appealed from those portions of the decision of the administrative law judge denying the petition for reassessment of an assessment made on February 13, 2003, for the period April 1, 2001 through September 30, 2002, on the basis that petitioner's delivery drivers were employees.

The issues on appeal are:

1. Whether petitioner's delivery drivers were common law employees, rather than independent contractors, under section 621(b) of the Unemployment Insurance Code[1] and

2. Whether petitioner is liable for a ten percent penalty under code section 1127.

STATEMENT OF FACTS

NCM Direct Delivery, Inc. (hereafter "NCM") is a courier company in the delivery business. During the period of assessment, its major customer was Kaiser Permanente. The bulk of its business was performed under a "hub and spoke" system in which drivers picked up packages from customers and brought them to a warehouse where they were sorted and sent out for delivery. A portion of its business involved route drivers who delivered pharmaceutical products on a regular basis according to the routes selected by its customers. Another portion involved on-demand deliveries, which arose on an irregular basis. The manner of delivery was dictated by NCM's customers. The drivers were directed by NCM's dispatcher.

[1] All references are to the Unemployment Insurance Code unless otherwise indicated.

NCM had conducted its business using delivery drivers that it hired and treated as employees, until its principal attended an industry association conference. After attending the conference, the chief executive officer decided to convert NCM's employee drivers to independent contractors because he believed this would help him remain competitive in the courier industry. He chose the National Independent Contractors Association (hereafter "NICA") to assist in the conversion and handling of independent contractors.[2]

NCM and NICA entered into a written agreement. At NICA's suggestion, NCM referred to itself as a broker that "brokered communication of delivery jobs to independent contractors." NICA offered to instruct the delivery drivers on what it meant to be an independent contractor. It described a system by which it would write the compensation checks to the drivers, based upon data sent to it by NCM, and to offer the drivers advice and other services. Later, NICA appeared on behalf of NCM in these proceedings.

NCM notified all of its delivery drivers that they were required to attend a meeting on April 13, 2001. NICA also attended the meeting. The drivers learned that they must become independent contractors if they wanted to continue to work for NCM. NCM required them to sign an agreement with NICA. All of its drivers were to be "run through NICA." There was no written agreement between NCM and any of the drivers.

The agreements between NICA and the drivers were preprinted. They provided that the drivers were independent contractors. The drivers were required to pay fees to set up the NICA account and to agree that a weekly "affiliation fee" would be deducted from the drivers' compensation. Under the new arrangement, NCM was to pay the drivers commissions, which were to be sent as lump sums to NICA. NICA would then give the drivers "settlement checks." Checks were to issue on a regular basis, usually every two weeks. NICA advised the drivers to create business names, obtain business licenses, business cards, motor carrier permits, and other such indications that they were independent business owners. Preprinted enrollment forms, application forms for accident insurance and W-9 tax forms were provided. NICA offered accident insurance, disability insurance, and tax preparation services.

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[2] We note that this decision is based on what NCM did, and not what NICA did. Although NICA aided in the conversion of NCM employees to "independent contractors," an employer who took the same actions as NCM, but did so without using an intermediary such as NICA, would be subject to the same analysis.

NICA deducted the NICA fees, NCM expenses and any insurance premiums from the settlement checks. Under the agreement, the drivers acknowledged that their rights to unemployment insurance, state disability insurance and workers' compensation were relinquished. The drivers gave up health benefits, vacation pay, reimbursement for driving expenses, and all employee protections under wage-and-hour and anti-discrimination laws. The drivers agreed to obtain certain business-related licenses.[3] Some of the drivers did so. The agreements were of indefinite duration and ended when the drivers ceased performing services "for the NICA-affiliated company."

In actuality, most drivers did not obtain any licenses. The drivers were generally unfamiliar with the terms of the agreements they had signed. The terms of the agreements gave substantial benefit to NCM by reducing its employment-related costs and taxes while providing limited financial benefit to the delivery drivers.

The work of the drivers did not change after they signed the agreements. The drivers were in daily communication with NCM, but had little, if any, contact with NICA. The drivers reported regularly to dispatchers employed by NCM. The work was performed under the direction of the dispatcher and the drivers were dependent on the dispatcher for their livelihoods. Most drivers owned their own vehicles; others used NCM vehicles. They were required to use pagers so as to remain in regular communication with the dispatcher. They leased these devices from NCM. The delivery times were arranged by NCM according to the customers' demands. The drivers could choose their hours of work but were expected to work the shifts they selected. Some drivers believed they had the right to refuse an assignment. They understood that they risked the loss of future work if they turned down a job. The drivers followed a route, obtained a customer signature, wrote down the delivery times and items delivered on paperwork provided by NCM and submitted these "run sheets" in order to obtain payment. The drivers had not owned their own businesses before the conversion and did not have their own customers. The deliveries were to and from the customers of NCM and the drivers were required to make these deliveries at the times required by these customers. The drivers' services were continuous. The parties believed that the work relationship with NCM was terminable at any time without cause.

[3] Before the conversion, the drivers had operated under the petitioner's motor carrier permit. After the conversion, a number of drivers did not obtain motor carrier permits as required by the California Vehicle Code. (Cal. Veh. Code, § 34601, et seq.) The failure to obtain such a permit was a misdemeanor. (Cal. Veh. Code, § 34661.)

The skills required of the drivers were simple - to follow the instructions of the dispatcher and customers, drive a vehicle and find a destination. NCM conceded that the work of a delivery driver did not require any particular expertise. NCM decided what would be delivered, what to charge the customer, the destination and time of delivery. At most, the drivers' discretion was limited to their choice of the route.

At the hearing, NCM agreed that the delivery drivers were an integral part of the business of NCM. The business of NCM was delivery and this business was carried out by the delivery drivers. There would be no business without them. The drivers had no investment or ownership interest in NCM. The drivers bore no risk of loss. They were paid by NCM (through NICA) whether or not the customers paid for the deliveries. They were, however, liable for damage to packages they delivered.

In sum, the petitioner made a decision to utilize drivers whom it would call independent contractors for the identical work that had previously been performed by employees. The work itself did not change. The employer decided to change the external attributes of the work without altering its essential character. Further, it accomplished all changes by dictating to workers, who only had experience as employees, how they must conduct themselves in order to create the appearance that they owned their own businesses. The changes were made by the workers under threat of loss of their employment.

The Employment Development Department (hereafter "the Department") conducted an audit of NCM. It investigated the practices of NCM to determine whether its delivery drivers were performing work as the employees of petitioner. Based upon a review of NCM's records and interviews of drivers and management, the Department concluded that the drivers were the employees of NCM. A ten percent penalty under code section 1127 was imposed.

NCM had treated all of its delivery drivers as employees, had paid their payroll taxes and reported them as required by the taxing authorities. It then required the same employees to agree to the status of independent contractor. However, it accomplished this conversion without sufficient investigation into the legal consequences of doing so. It did not seek guidance or legal advice from the Department about the conversion. Rather than changing the nature of work it provided the drivers to true independent contractor status, NCM merely changed the title by which it classified the drivers, based on the result it desired.

REASONS FOR DECISION

If the Department is not satisfied with any return or report made by any employing unit of the amount of employer or wage earner contributions, it may compute the amount required to be paid upon the basis of facts contained in the return or reports or may make an estimate upon the basis of any information in its possession and make an assessment of the amount of the deficiency. (Unemp. Ins. Code, § 1127.)

California unemployment insurance taxes accrue only on amounts paid as remuneration for services rendered by employees. The relationships of employer and employee and of principal and independent contractor have long been recognized to be mutually exclusive. They cannot exist simultaneously with respect to the same transaction. The proof of the one status automatically precludes the existence of the other. Accordingly, the services of an independent contractor are not "employment" within the meaning of Unemployment Insurance Code, section 601, and the remuneration paid for such services is not taxable. (Precedent Decision P-T-2.)[4]

The burden of proof generally is on the party attacking the employment relationship. (*Isenberg v. Calif. Emp. Stabilization Comm*. (1947) 30 CaI.2d 34.)

The petitioner's appeal turns on the question whether the delivery drivers performing work on its behalf were employees or independent contractors.

"Employment" means service, including service in interstate commerce, performed by an employee for wages or under any contract of hire, written or oral, express, or implied. (Unemp. Ins. Code, § 601.) "Employee" includes any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee. (Unemp. Ins. Code, § 621(b).)

[4] Employer contributions to the California Unemployment Fund shall accrue and become payable by employers "with respect to wages paid for employment." (§ 976.) Contributions are due the department from employers with respect to wages paid in employment for unemployment insurance (§ 976), disability insurance (§ 984), employment training (§ 976.6), and personal income taxes (§ 13020).

In determining whether service was rendered in employment, the primary test is the right of the alleged employer to control the manner and means of accomplishing the desired result. (*Empire Star Mines Company, Ltd. v. California Employment Commission* (1946) 28 Cal.2d 33, overruled on other grounds in *People v. Sims* (1982) 32 Cal. 3d 468, 479-480, fn. 8 ["If the employer has the authority to exercise complete control, whether or not that right is exercised with respect to all details, an employer-employee relationship exists." (*Empire Star Mines Company, Ltd. v. California Employment Commission*, *supra*, 28 Cal.2d 33, 43.)].) "[I]t is the existence of the right of control and not its use or lack of use" that is critical. (*Robinson v. George* (1940) 16 Cal.2d 238, 244.)

According to the California Supreme Court, the principal's supervisory power is critical in determining employee status because the extent to which the employer has a right to control the details of the work done is highly relevant to the question of whether the employer ought to be legally liable for them. Thus, the 'control of details' test is the principal measure of the servant's status for common law purposes. (See *S.G.Borello & Sons, Inc. v. Dept. of Indust. Rel*. (1989) 48 Cal.3d 341, 350, regarding law of workers' compensation, approved as applied to unemployment insurance law in *Santa Cruz Transportation, Inc. v. Unemp. Ins. Appeals Bd*. (1991) 235 Cal.App.3d 1363, 1370-1.)[5]

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[5] We take this opportunity to resolve an ambiguity created in the *Borrello* decision. In that case, the *Borello* court left open the question whether its reasoning applied to California unemployment law. (*S.G. Borello & Sons v. Depart. of Indust. Rel.*, supra, 48 Cal.3d 341, 359, fn. 16.) The court placed erroneous reliance on a panel decision of this Board that had no precedential value. The decision of "Dino J. Orsetti (Apr. 11, 1985) No. T-85-53" was not a precedent decision and neither this Board nor any other entity is bound by the holding of that case. (The rules regarding precedent decisions of this agency are contained in code section 409 and section 5109, Title 22, California Code of Regulations. We take official notice under section 5009(a) of these regulations that Case No. T-85-53 was not designated a precedent decision by the Appeals Board and was not published as such. It is not listed in the index of said decisions.) While recognizing the differences between worker's compensation and unemployment insurance laws, we find that the *Borello* case has strong applicability to cases arising under the Unemployment Insurance Code and that the reasoning of that decision provides important guidance, as may be seen by its application to the decisions of *Santa Cruz Transportation, Inc. v. Cal. Unemp. Ins. Appeals Bd*, *supra*, 235 Cal.App.3d 1363, 1370-1371 and *Metric Man, Inc. v. Cal. Unemp. Ins. Appeals Bd*. (1997) 59 Cal.App. 4th 1041, 1049.)

In this case, NCM required its drivers to sign contracts that gave them the attributes of independent contractors. The contract terms were unilateral. The delivery drivers were presented with an ultimatum: call yourselves independent contractors or lose the opportunity to work for us. The ultimatum itself may be the best indicator of control.

Having tried to establish that the drivers were independent contractors, NCM then proceeded to control the details of their services as if they were employees. Primary evidence of this control is found in the fact that work would only be given to the drivers who followed the petitioner's requirements as to the time and method of delivery. The drivers had to meet the requirements of the customers by delivering according to those demands. Therefore, the delivery requirements of customers, such as the method and time of conveying the delivery to its destination, operated as if they were commands. (*See, e.g. Tieberg v. California Unemp. Ins. Appeals Bd. (1970)* 2 Cal.3d 943.) The drivers were in daily communication with NCM. They were required to utilize a pager for this purpose. They reported to NCM's dispatcher throughout the day. They were required to record each delivery on a company-provided run sheet. Implicit in the arrangement was the understanding that a failure to comply might result in not being called for another delivery. "The belief of the [workers], however, that they would not be rehired if they failed to follow instructions is relevant to show their submission to control." (I*senberg v. Calif Emp. Stabilization Comm*., *supra*, 30 Cal.2d 34, 40.)

With the help of NICA, NCM attempted to create the impression that its relationship with the delivery drivers was at arm's length. It was no more than an illusion. NCM required the drivers to "join" NICA, a company that did not represent the drivers' interests.[6] The drivers signed preprinted contracts that were in major part one-sided. The contracts provided tangible benefit to NCM and gave little to the drivers.

This conclusion that the drivers remained the employees of NCM is supported by the application of the facts to the test for employee status as articulated in *Tieberg v. California Unemp. Ins. Appeals Bd.*, *supra*, 2 Cal.3d 943, 950.).[7]

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[6] The interests of NICA became apparent when the Employment Development Department challenged the contention that the drivers were independent. NICA appeared on behalf of NCM and took a position contrary to the interests of the drivers.

[7] The secondary factors listed in *Tieberg* are similar to those set forth in the Restatement Second of Agency, §220 (1958).

The drivers were not engaged in distinct occupations or businesses of their own. The work was the kind generally done under the direction of the courier company's dispatcher and had been performed by its employees until the conversion. When supervision was not exercised, it was because the work was simple or such supervision was impractical. The work required no experience or specialized skill. The services were continuously performed over a period of months or years. The work was integral to NCM's business. The drivers were terminable at will.

Certain of the *Tieberg* factors, looked at in isolation, point to independence. For example, some of the drivers provided their own delivery vehicle. All drivers paid their own expenses. They were paid by the job. Many drivers believed that they were independent contractors. The overall picture, nevertheless, was one of control by NCM, and status is determined by the evidence taken as a whole, not by counting factors and using a total to decide the score for determining which status "wins."

Next, we look at the nature of the independent contractor agreements with NCM. In this respect, the decisions in *S.G.Borello & Sons, Inc. v. Dept. of Indust. Rel*., *supra*, 48 Cal.3d 341 and *Santa Cruz Transportation v. Unemp. Ins. Appeals Bd.*, *supra*, 235 Cal.App.3d 1363 are instructive. In *Borello*, a grower designed the business of its cucumber "sharefarmers" in order to give the impression that they were separate business owners. The court rejected the grower's "subterfuge."[8] Likewise, In *Santa Cruz Transportation Inc. v. Unemp. Ins. Appeals Bd*., *supra*, 235 Cal.App.3d 1363, a taxicab company converted its employee drivers to lease drivers by requiring them to sign leasing agreements. The court of appeal found that the cab drivers were not independent. As in those cases, the drivers here had no real choice about signing the contracts or working under the title "independent contractor."

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[8] This Appeals Board came to the same conclusion when it disregarded a purported lease because it failed to accurately characterize the employment relationship. (*Precedent Tax Decision P-T-403*; *see also Precedent Tax Decision P-T-99*.) We distinguish the facts of this case from Precedent Tax Decision P-T104 because, unlike the drivers here, the interviewers in that case provided work on an intermittent basis, were particularly skilled in their trade and were engaged in a distinct occupation. Reliance would be better placed on *Smith v. Dept. of Emp*. (1976) 62 Cal.App.3d 206.

Also instructive to this case because of the similarity of tasks is the finding of the court in *Toyota Motor Sales U.S.A, Inc. v. Superior Court* (1990) 220 Cal.App.3d 864. There, the court found that a pizza delivery driver was an employee even though there was a written contract designating him as an independent contractor. The driver delivered to the employer's customers. The employer set the price and told the driver when and where to deliver. The court held that it did not matter that the driver selected the route because the employer retained general supervision and control. Further, the fact that the driver paid his own payroll taxes and worker's compensation did not provide evidence of independence. Rather, these actions were the legal consequences of signing the independent contractor agreement. The court observed that "attempts to conceal employment by formal documents purporting to create other relationships have led the courts to disregard such terms whenever the acts and declarations of the parties are inconsistent therewith." (*Id*. at p. 877.) The court went further: "An employer cannot change the status of an employee to one of independent contractor by illegally requiring him to assume burdens which the law imposes directly on the employer." (*Ibid*.)

In *Santa Cruz Transportation Inc. v. Unemp. Ins. Appeals Bd*, *supra*, 235 Cal.App.3d 1363, the taxicab company set the hours of work, required the drivers to complete trip sheets and take charge slips and maintained a dress code. The court looked beyond the form agreements. The substance of the relationship looked exactly like employment. It found that the company controlled the behavior of the drivers by retaining an implicit threat that it would make less work available if the drivers refused work too often and concluded that the drivers' freedoms were illusory.

We find the above reasoning applies equally in this case. The stated provisions of the NICA contracts failed to accurately reflect the true nature of the work relationship and dictated to the drivers, at least on paper, how the work was to be described in order to create the impression that it had the character of independence when, in fact, it did not.

On balance, the evidence established that the petitioner controlled the means by which the work relationship was described. It presented the delivery drivers with a *fait accompli* by requiring signatures to agreements that described the work so as to parrot the language of the Restatement Second of Agency. In so doing, the petitioner controlled the description of the manner and means of the work. This practice established that it was NCM, and not the drivers, who created the appearance of independence and was evidence that NCM also controlled the manner and means of accomplishing the work.

We conclude that, overall, the drivers performed an essential function that was integral to the business of NCM and did so in a dependent role. As in *Borello* and *Santa Cruz*, the drivers had no real choice about becoming "independent contractors." As in *Santa Cruz*, there was no practical difference between the function of the employee drivers and that performed by drivers who had signed independent contractor agreements. They did not operate distinct and independent businesses and their livelihoods depended exclusively on NCM. We cannot say that the delivery drivers were really carrying on "a distinct business of [their] own." (Precedent Tax Decision P-T-2.) For all of these reasons, we find that the delivery drivers performed their work in the capacity of employees.[9] Relying on *Borello* and the other authorities cited above,

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[9] The Illinois Supreme Court reached the same conclusion under similar facts in *AFM Messenger Service, Inc. v. Department of Employment Security* (Ill. 2001) 763 N.E.2d 272. In that case, among other things, the petitioner procured customers, set prices, provided delivery tickets, billed customers, and set the drivers' pay rate. The court concluded that the evidence did not establish that the drivers ran " 'delivery businesses' " independently from the petitioner: "Thus, a driver's 'business' was not established 'independently' of AFM. Rather, a driver's business existed only by reason of the driver's employment with AFM, which was subject to termination, at which time the driver would be unemployed." (*Id*. at p. 285.)

A number of other state courts have also held that delivery drivers were employees. (*Speedy Messenger & Delivery Service v. Indust. Claim App*. (Colo. Ct.App. 2005) 2005 Colo. App. LEXIS 2140 [couriers; unemp. ins.]; *Chicago Messenger Service v. Jordan* (Ill. Ct.App. 2005) 825 N.E.2d 315 [couriers; unemp. ins.]; *Boston Bicycle Couriers, Inc. v. Deputy Dir. of Emp*. (Mass. Ct.App. 2002) 778 N.E.2d 964 [messengers; unemp. ins.]; *Stover Delivery Systems, Inc. v. Div. of Emp. Security* (Mo. Ct.App. 1999) 11 S.W.3d 685 [delivery drivers; unemp. ins.]; *In Re CDK Delivery Service, Inc*. (N.Y., App. Div. 1989) 151 A.D. 2d 932 [messenger drivers; unemp. ins.]; *Central Management Co. v. Indust. Comm*. (Ariz. Ct.App. 1989) 781 P.2d 1374 [cab driver; workers' comp.]; *In Re Webley* (N.Y. App.Div.) 133 A.D.2d 885 [driver; unemp. Ins.]; *RX Delivery Service, Inc. v. Labor & Indust. Rel. Comm*. (Mo. Ct.App. 1984) 677 S.W.2d 936 [delivery drivers; unemp. ins.]; *Koontz Aviation, Inc. v. Lab. & Indus. Rel. Comm.* (Mo. Ct.App. 1983) 650 S.W.2d 331 [baggage delivery drivers & limousine drivers; unemp. ins.); *Zelney v. Murphy* (Ill. 1944) 56 N.E.2d 754 [motorcycle drivers; unemp. ins.]; *ACME Messenger Service Co. v. Unemp. Comp. Comm*. (Mich. 1943) 11 N.W.2d 296 [truck drivers and messengers; unemp. ins.]. *But see, Dial-A-Messenger, Inc. v. Ariz. Dept. of Econ. Sec.* (Ariz. 1982) 648 P.2d 1053 [drivers; unemployment insurance] for opposite result.

Some federal courts have reached similar conclusions. (*Hathcock v. Acme Truck Lines, Inc*. (5th Cir. 2001) 262 Fed.3d 522 [truck driver; fraud; breach of

we therefore affirm the ultimate conclusion of the administrative law judge that the drivers were employees, not independent contractors. The evidence established under the primary test that NCM controlled the manner and means of the drivers' performance in delivering packages, exercising total control over the work and the drivers. In doing so, NCM also controlled the factors generally utilized to evaluate employment, such as requiring the drivers to sign independent contractor agreements and agree that they owned their own businesses before they could deliver for NCM. NCM could not avoid its obligations by merely changing the form of the relationship without changing any of its real substance. Under the secondary factors of *Tieberg* and the Restatement Second of Agency, NCM controlled the delivery drivers' work.

If any part of a deficiency assessed under section 1127 of the Unemployment Insurance Code is due to negligence or intentional disregard of the law, a penalty of 10 percent of the deficiency shall be added to the assessment.

We also affirm the administrative law judge's conclusion that penalties were required to be paid under code section 1127 because NCM acted negligently when it converted its acknowledged employees to purported independent contractors without first inquiring with the Department or an appropriate and disinterested professional as to the propriety of this action.

DECISION

The appealed portions of the decision of the administrative law judge are affirmed. The petition for reassessment is denied. Petitioner is liable for the payment of all taxes and penalties under the assessments.

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contract]; *Corporate Express Delivery Syst. v. NLRB* (D.C. Cir. 2002) 292 Fed.3d 777 [owner-operators; N.L.R.A.]; *Gustafson v. Bell Atlantic Corp*. (S.D.N.Y.) 171 F. Supp. 2d 311 [limousine driver; F.L.S.A.]; *In Re Brown* (1984 9th Cir.) 743 Fed.2d 664 [truck drivers; unemp. ins.]; *Holiday v. Vacationland Federal Credit Union* (N.D. Ohio 2004) 2004 U.S. Dist. LEXIS 5655 [courier; F.M.L.A.].) *But see, Herman v. United States* (5th Cir. 1998) 161 Fed.3d 299 [delivery drivers; F.L.S.A.] for opposite result.