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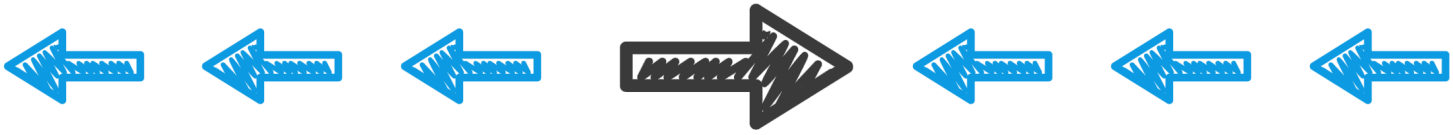

Independent & Sub-Contractors

Presenter: Maureen Gallagher

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Maureen Gallagher

Maureen Gallagher is the Michigan Managing Director and National Real Estate and Workers Compensation Brands Leader in the 13th largest US broker, AssuredPartners. Gallagher specializes in insurance placement, risk management and consulting. In addition, her passion for education inspired her — in 2003 — to establish Insurance Partners Academy, an educational company, where she serves as Director. Gallagher previously held the position of President and CEO of Acordia of Michigan (Wells Fargo), assuming that position after heading up her own agency, Gallagher Group, Inc., for more than ten years.

She has been featured and profiled in numerous publications, and was named by Crain's Detroit Business as one of the "Best and Brightest" and as one of "Detroit's Most Influential Women." Risk and Insurance recognized Gallagher as a "Power Broker" which identifies the best brokers in the country. In addition, Liberty Mutual honored Gallagher with the "Responsibility Leader Award" awarded to those insurance professionals that have demonstrated a commitment to their organization, profession and community. Business Insurance named Gallagher as one of their "Women to Watch" in 2011 and WorkCompCentral honored Gallagher with the Work Comp Laude Award in 2015. Gallagher was also the recipient of "Soaring Eagle Leadership Award" by The Executive Committee (TEC). TEC is an international association of Chief Executive Officers dedicated to increasing the effectiveness and enhancing the lives of chief executives and managing directors. The City of Louisville presented Gallagher with a key to the city for her commitment to leadership and education at the Women's Leadership conference in 2014 where she was the keynote speaker. Finally, in 2016, the Women's Leaders in Insurance and Finance awarded the Women of the Year Award to Gallagher in recognition of outstanding performance and achievement in the insurance industry.

Gallagher is a Licensed Insurance Counselor (LIC), Licensed Claims Adjuster (LCA), Certified Insurance Counselor (CIC), Certified Workers Compensation Professional (CWCP), Certified Risk Manager (CRM), Certified Workers Compensation Advisor (CWCA), Registered Professional Liability Underwriter (RPLU), Construction Risk and Insurance Specialist (CRIS) and Certified Integrated Leave Management Administrator (CILMA). A frequent lecturer and presenter, Gallagher is also on the National teaching faculty for the National Alliance for Insurance Education and Research. She is a featured writer for Insurance Thought Leadership and writes for Resource Magazine. Gallagher is a member of the American Bar Association and the Society of Trainers and Educators. She is the creator of the Property Risk and Insurance Specialist (PRIS), Certified Workers Compensation Counselors (CWCC), Certified Experience Modification Advisory (CXMA) and Real Estate – Certified Insurance Professional (RCIP) certification programs as well as Producer Peak Performance training. An avid long-distance runner, cyclist, swimmer, stair climber, certified exercise/spinning instructor, USA Cycling, Road Runners Club of American and USA Triathlon coach, Gallagher has qualified several times for the Sprint and Olympic distance USA Triathlon National Championships, has completed 70.3 Ironman and was named one of the "50 Fittest CEOs" by Crain's Detroit Business. She has raised over $260,000 for charities through her participation in endurance events.

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Indianapolis, IN

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Independent and Sub-Contractors

INSURANCE PARTNERS

Presented By
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Employer-Employee & Independent/Sub-Contractor Relationships

Common-law Criteria for Determination

Common law has evolved slowly over the centuries based upon judgments rendered by the courts on individual cases. The common law of employment, as it exists today, is the total of all court decisions related to the question of what constitutes an employment relationship. An employer-employee relationship exists when a person who hires an individual to perform services has the right to exercise control over the manner and means by which the individual performs his or her services.

The right of control, whether or not exercised, is the most important factor in determining the relationship. The right to discharge a worker at will and without cause is strong evidence of the right of direction and control. The following factors should also be taken into consideration:

Control: The right to control the individual in the performance of his or her job is most often cited as the primary test to determine if the worker is an employee or an independent contractor.

Nature of Work: This is arguably a more appropriate test and gaining acceptance. The premise is we should look at the nature of the claimant's work in relation to the regular business of the employer. If the work is an integral part of the company's business, the worker should be considered an employee.

Other Factors: that have been considered in determining whether a worker is an employee or an independent contractor include:

- Control over details of the work
- Whether the worker works for others
- Whether the worker holds himself or herself out to the general public as available to perform services
- Whether this kind of work is usually done by independent contractors
- The amount of skill involved
- Who supplies the tools
- The length of time involved
- The method of payment
- The right to fire
- What kind of arrangement the parties believed they were creating when they entered into the relationship.

Lesson of Time

Even when virtually all the criteria for independence are met, independent contractors may still be considered employees, especially where they work for a substantial block of time for only one employer. When independent contractors only work for one employer over a substantial period time, case law has ruled they are likely to morph into employees, with all the rights and considerations attached to being an employee.

It's a duck

If it looks like a duck, walks like a duck, swims like a duck and quacks like a duck, it is a duck. The FedEx class action suit won by workers in California is a good example of this. The ruling states that "in 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, therefore they are FedEx employees not independent contractors".

Written Agreements

Agreements stating the worker is an "independent contractor" is typically insufficient to qualify the worker as an independent contractor.

In 1989 and 1990, the IRS conducted audits of Microsoft Corporation and found that a number of its workers had been misclassified as independent contractors, when they were, in fact, full-fledged employees, at least for tax purposes. Despite having signed agreements stating they were independent contractors, these workers:

1. Collaborated on teams with regular Microsoft employees
2. Shared the same supervisors
3. Sometimes performed identical functions
4. Worked similar hours
5. Had admittance cards just like regular employees
6. Worked at Microsoft-owned facilities
7. Had access to the same office equipment and supplies as the company's regular employees.

When Microsoft agreed to reclassify these workers as employees, it prompted a number of the misclassified employees to file a class action lawsuit against Microsoft. The suit aimed to recover what the workers argued were wrongfully withheld benefits, including those accruing from an employee stock purchase plan and a 401(k) plan. The Ninth Circuit Court held that the signed independent contractor agreements notwithstanding, the workers were indeed "common law employees" and were thus entitled to the benefits accruing to employees in comparable positions.

Workers Compensation and Independent Contractors

Employee-employer relationships regarding workers compensation are complicated by the IRS, industrial commissions, the courts and state statutes. Each has its own definition or applies a different test to define "employee." The DOL has actually made the insurance agent/broker job easier as it is drawing a bright line between employee and independent contractor giving our clients less “wiggle” room in trying to make some or all of their employees “independent contractors”. The most important significant take-away is that even if a worker qualifies as an independent contractor under the statute, by DOL definition and case law, the workers compensation statutes may contradict and overrule the independent status at least as it applies to workers compensation insurance.

WC Statutes Definition of “independent contractor” versus Definition of “employee”

State workers compensation laws vary as to their specificity on this point. Many are completely silent, in which case the common law principles that distinguish between an employee and an independent contractor would usually govern, unless the workers compensation case law in the state in question has established exceptions to these principles.

Several States (approximately 16) contain a definition of “independent contractor” in their workers compensation statute. The problem with the definition is they are similar to the common law criteria and do not provide a clear-cut formula for determining employee versus independent status.

Most state statutes provide that if one employer contracts with another employer (sub-contractor) to do work for it - the first employer can be held liable to provide benefits to the employees of the second if the sub-contracted employer does not have workers compensation coverage.

Nearly all workers compensation laws (exceptions are Alabama, CA, DE, IA, ME, RI and WV) allow employees to collect under these circumstances. However, states vary in how broadly this principle is applied.

Special Employments

Trucking Owner/Operators

Traditionally, the trucking industry has considered owner-operators to be independent contractors who, through ownership and/or control of their power units, operated their own independent businesses. They are free to work for any one of hundreds of competing carriers and, through hard work and proper asset management can become a small business success.

The federal truth-in-leasing regulation, 49 C.F.R. 376, establishes detailed contractual requirements intended to protect owner-operators against carrier abuse. Under the independent contractor model, the owner-operator is supposed to be free to succeed or fail, unfettered by unnecessary carrier control.

As independent contractors, they are unprotected by the state law benefits extended to employees and unburdened by the attendant cost. Unlike the employer driver, the independent contractor does not receive workers compensation benefits or state unemployment compensation.

Mandatory workers compensation premiums in high-risk states, particularly for truck drivers, can be significant. Yet, when owner-operators are classified as independent contractors the owner/operator does not purchase workers compensation but occupational accident insurance coverage where premiums are lower than workers compensation. Owner-operators as a whole have fewer workers compensation claims than company drivers, are not malingerers, and on an experience-rated basis deserve cheaper premiums.

While the trucking industry likes to consider owner/operators independent contractors, - unless the driver is operating in a state that considers owner/operators independent contractors by statute, many/most carriers do not. Carriers have had to pay too many workers compensation claims on owner/operators.

Some states include specific workers compensation provisions addressing the status of truck owner-operators and taxi drivers. When such provisions are included they usually establish that these individuals are considered independent contractors. 21 states consider owner/operators as independent contractors. These states include Alabama, Colorado, Florida, Georgia, Indiana, Iowa, Kansas, Louisiana, Mississippi, Missouri, Montana, Nebraska, North Carolina, North Dakota, Oklahoma, South Carolina, Tennessee, Texas, Washington and Wyoming.

Sole Proprietors

A sole proprietorship, also known as the sole trader or simply a proprietorship, is a type of business entity that is owned and run by one person and in which there is no legal distinction between the owner and the business. A sole proprietor may use a trade name or business name other than his, her or its legal name. Sole proprietors are really a workers compensation conundrum with no uniformity among states. There are a surprising amount of sole proprietors. Below is general information:

- Most, but not all states, do not require the sole proprietor to carry workers compensation;
- Not withstanding above, the sole proprietor is usually required to provide insurance on any employees they have or employees over a certain numerical amount (e.g., 1, 2 or 3).
- While the sole proprietor may not be required to purchase insurance, many states allow a sole proprietor to elect to obtain coverage on themselves.
- Other states do not allow a sole proprietor to purchase workers compensation on themselves, only on employees. The only way to remedy this is for the sole proprietor to file as a corporation, LLC or “S” to obtain coverage for companies the sole proprietor works for that is requiring coverage.
- Typically insurance carrier auditors will pick up the payroll for the “uninsured” sole proprietor if they have no coverage or only provided coverage for their employees.
- Many states have developed forms specific to sole proprietors (e.g. MI, MT) the sole proprietor can complete. The forms have the sole proprietor verify they work for others; list others they work for among other things to establish their independence. Properly executed forms usually avoid audit issues even if the sole proprietor has no coverage on themselves. You must check with your state for sole proprietor rules.

Contractors

In the construction industry, the most pertinent question relating to independent contractors is whether a contractor is liable for the payment of workers compensation benefits to employees of its *subcontractor* in the event the subcontractor is uninsured. In most states, provisions making an employer responsible for payment of benefits to the employees of an independent contractor apply exclusively to the construction industry. The vast majority of states do hold contractors responsible for payments of benefits to subcontractors' employees, but most also allow the contractor to recover such payments from the uninsured subcontractor.

Workers compensation laws regarding general contractor-subcontractor relationships are designed to create a safety net for any injured worker – assuring benefits will be paid by somebody.

Some states stipulate that contractors who have required the subcontractor to carry workers compensation insurance, and who relied in good faith upon evidence that such coverage is in force, are not liable for injuries to uninsured subcontractors' employees. A written construction contract requiring such coverage, and a valid certificate evidencing coverage should meet these criteria.

Contractor Statutorily liable to Uninsured Subcontractor's Employees		
Alabama	Louisiana	North Dakota
Alaska	Maryland	Ohio
Arizona	Massachusetts	Oklahoma
Arkansas	Michigan	Oregon
Colorado	Minnesota	Pennsylvania
Connecticut	Mississippi	South Carolina
District of Columbia	Missouri	South Dakota
Florida	Nebraska	Tennessee
Georgia	Montana	Utah
Hawaii	Nevada	Vermont
Idaho	New Hampshire	Virginia
Illinois	New Jersey	Washington
Indiana	New Mexico	West Virginia
Kansas	New York	Wisconsin
Kentucky	North Carolina	Wyoming

Conclusion

Independent and sub-contractors create claims and audit issues. Insureds must:

- Be diligent in classifying employees correctly.
- Obtain certificates of insurance on all independent contractors and sub-contractors.
- Learn the laws of the states of operation and take advantage of protections (e.g. forms).
- Execute contracts prepared by employment attorneys to clarify any arrangements.

Examining WC Waivers of Subrogation

There is no doubt that workers' compensation waiver of subrogation requirements are extremely common in today's contracts, particularly construction contracts. What is less clear is why. Perhaps the contracting party hopes the waiver will provide immunity from a third-party claim arising out of their subcontractor's workers compensation claim. If this is the hope, it's a false one.

A waiver of subrogation does not prevent an injured subcontractor's employee from filing suit against the contractor. It only bars the subcontractor's workers compensation insurer from initiating a subrogation action and/or from enforcing its lien on a third-party claim. Possibly, the only winner from the waiver is the injured employee who might actually receive a double recovery because the workers compensation lien does not have to be repaid to the employer. The contracting party loses or at least does not win since the waiver did not have the desired effect of preventing a third-party claim. The workers compensation insurer loses because it forfeits its right of recovery. The biggest loser is the subcontractor who:

1. Pays an additional premium to add the waiver of subrogation to its workers' compensation policy.
2. Faces a premium increase because the lack of a recovery on its workers compensation lien inflates its loss experience.
3. Takes a double hit when its own general liability coverage must respond to resolve its employee's third-party claim due to a likely indemnification provision in its contract.

In theory, a waiver could eliminate a third-party exposure. Many jurisdictions give insurers an independent right to pursue subrogation if the injured employee opts not to bring a third-party claim. With a waiver, the insurer loses this independent right. As a practical matter, it is quite rare for an insurer to initiate an independent third-party claim. It faces the prospect of funding an attorney to pursue subrogation without a guarantee of a recovery. This pursuit becomes even riskier if undertaken without the cooperation of the star witness, the injured employee. The elimination of this sort of theoretical third-party claim hardly justifies a waiver of subrogation requirement. Finally, most states make another stakeholder (insurance company or employer) wait a certain amount of time (typically two years) before they can pursue the lien – if the employee did not take action.

Typical Scenario

It is far more typical for an injured employee to initiate a third party claim opposed to the workers' compensation insurer. Most often, the employee retains an attorney on a contingency basis to seek compensation beyond what he has received in workers compensation benefits from an at-fault party. In a third-party claim, the employee may be awarded damages for pain and suffering in addition to the lost wage and medical benefits that are also available through the workers compensation system. In the absence of a waiver of subrogation, the workers compensation insurer can place a lien on any third-party settlement or verdict to recover the benefits paid to the injured employee. In this circumstance, the insurer can recover up to two-thirds of his workers' compensation payments lien, conceding one-third to cover the attorney's contingency fee (assuming a one-third contingency fee arrangement). It varies by state.

In the scenario where the employee initiates the third party claim, and there is a waiver of subrogation endorsement attached to the workers' compensation policy, the contractor who required the waiver receives absolutely no benefit from the waiver. The waiver does not bind the injured employee, who initiated the claim.

The third-party award is not reduced by the workers compensation benefits that were already paid. The insurance carrier waived its right of subrogation and the carrier is not seeking reimbursement from the liable third party. In many jurisdictions, when there is a waiver, the injured employee gets to keep the full award, which essentially gives the employee a double recovery for the indemnity and medical benefits already received through the workers compensation claim. Giving a double recovery to an injured employee while providing no benefit to the contractor that included the waiver of subrogation in its contract was certainly not the intent of requiring the waiver, but in many cases, it is the reality.

Why Do It?

With such questionable value, why are subrogation waivers routinely required in contracts? There are many culprits. General liability insurers look favorably on companies that obtain waivers from their subcontractors. It is a standard question on general liability applications. In addition, the right answer can affect the insurer's appetite for the risk and the premium charged. Requesting waivers has also become a "best practice" for brokers, insurance advisers, and risk managers. Few are willing to have their competence questioned because they failed to follow an industry norm—even if the norm is largely pointless.

It is advisable for subcontractors to resist workers' compensation waiver of subrogation requirements whenever possible. The problem is sub-contractors lack the leverage necessary to force the general contractor to drop this requirement. Unless their bargaining position changes for the better, subcontractors will likely need help from state legislatures or will need to mount court challenges to rid themselves of the waiver of subrogation requirements that they now face.

State Response

New Hampshire has taken a lead in this area by amending its workers' compensation law in 2004 to make waivers of subrogation against public policy. Section 281–A:13 (VI) now prohibits any provision in any agreement that requires an employer or an employer's insurer to waive any rights of subrogation. Similarly, Kentucky and Missouri have declared waivers of subrogation contrary to public policy and therefore invalid.

The Maine courts have also weighed in favorably for subcontractors on this issue. In *Fowler v. Boise Cascade Corp.*, 948 F.2d 49 (1st Cir. 1991), the court held that a waiver of subrogation did not prevent the employer from enforcing its lien against the employee who made the third-party recovery. In a bit of an end-around, the employer could not enforce its lien against the contractor that required the waiver, but it could enforce its lien directly against the employee who received the third-party settlement. While not completely declaring waivers of subrogation contrary to public policy, Wisconsin—like Maine—allows employers to recover on their liens even when there is a waiver of subrogation endorsement.

Conclusion

While the preceding paragraphs highlight some states where subcontractors are not required to forego a third party recovery even when there is a waiver of subrogation in place, these states are very much in the minority. It is a cruel irony for subcontractors that they are forced to accept waivers of subrogation to secure work from general contractors, and, yet, the waiver does not benefit the general contractor but could cause great harm to the subcontractor's loss experience. Until universal change comes to the industry, subcontractors can only push back on waivers where they can and, of course, work as safely as possible to avoid the multiple claim hits that can come from injuries to their employees.