KEELEY, KUENN & REID

Legal Advisory

Independent Contractor or Employee?

Worker misclassification has been a hot topic in the employment and legal arena for several years. Recently the Ninth Circuit Court of Appeals in California ruled that FedEx drivers were classified incorrectly and were employees and not independent contractors. FedEx had classified its drivers as independent contractors for about 10 years despite the fact that their routes were assigned by the Company; the drivers reported to FedEx managers; and the Company even provided their uniforms. The Court ruled that the drivers were incorrectly classified as independent contractors when they should have been employees.

In August, 2015 the IRS issued important guidance for correctly classifying independent contractors and employees. The general rule is that an individual is an independent contractor if the payer has the right to control or direct *only the result of the work and not what will be done and how it will be done. A person is not an independent contractor if he or she performs services that can be controlled by an employer (what will be done and how it will be done). This applies even if the individual is given freedom of action. What matters is that the employer has the legal right to control the details of how the services are performed.*

After the California Department of Labor ruled that Uber drivers were employees and not independent contractors, the U.S. Department of Labor weighed in on the issue and in July, 2015 published a new interpretation referred to as the "Economics Realities Test" ("ERT") to determine who is an employee and who is not. The DOL interpretation states that the ERT should be used to determine whether a worker is economically dependent on the employer in which case the individual is an employee as compared to whether the worker is in business for himself or herself and therefore an independent contractor. This determination must be made on a case by case basis with considerate given to the following factors.

1. The extent to which the work performed is an integral part of the employer's business.

2. The worker's opportunity for profit or loss depending on his or her managerial skill.

3. The extent of the relative investments of the employer and the worker.

4. Whether the work performed requires special skills and initiative.

5. The permanency of the arrangement.

6. The degree of control exercised or retained by the employer.

The guidance issued by IRS and DOL is interrelated in that IRS's takes the approach that the worker must be independent when determining what will be done and how it will be done. The DOL takes a more specific approach by enumerating the factors that employers should review in classifying a worker as an independent contractor. Needless to say, there will be a great deal of confusion until such time as the courts provide clarification.

Nevertheless there's still some good news. The Fifth Circuit Court of Court of Appeals recently held that the Department of Labor's conduct in another misclassification case was at nearly every turn a violation of the department's internal procedures and ethical litigation practices. Just prior to the Court's decision the DOL settled the employer's claim by paying $1.5 million.

US Department of Labor Proposes New Rules for Overtime

On July 6, 2015, the U.S. Department of Labor Wage and Hour Division proposed a new rule to update the regulations which govern the salary level needed for white collar workers to be exempt. The Department proposed the following:

1. Set the standard salary level at the 40th percentile of weekly earnings for full time salaried workers ($921 per week, or $47,892 annually.

2. Increase the total annual compensation requirement to exempt highly compensated employees (HCEs) to the annualized value of the 90th percentile of weekly earnings of full time salaried workers ($122,148 annually).

3. Establish a mechanism for automatically updating salary and compensation levels going forward to ensure that they will continue to provide a useful and effective test for exemption.

When the proposed rules were published in July, 2015 the Department invited comments to be submitted by September 4, 2015 thus allowing a short time for the filing of comments. Many industry groups petitioned the Department for additional time to respond but those requests were denied.

Unless the Department reverses course it is anticipated that a Final Rule may be published during the second quarter next year with an effective date 30 days after publication.

Costco Wholesale v Johnson & Johnson Vision Care

Costco Wholesale Corporation recently filed a lawsuit challenging Johnson & Johnson Vision Care's unilateral pricing policy. Since that time several more lawsuits have been filed including class actions challenging J&J Vision Care's policy. As a result the cases have been consolidated under the Federal Court Multidistrict Litigation program and transferred from the Northern District of California to the Middle District of Florida. Below you will find the original report outlining the issue in the case for your reference. As of this month Johnson & Johnson filed a motion to dismiss the case but no ruling has been issued as of this date.

Under the federal and state antitrust laws, to what extent may a supplier dictate that a reseller not advertise or sell the supplier's product below a minimum resale price? Two Fortune 500 companies are squaring off in California federal court to answer this question. (*Costco Wholesale Corp. v. Johnson & Johnson Vision Care, Inc., U.S. District Court, Northern District of Cal.*).

At issue is the "Unilateral Price Policy" implemented by Johnson & Johnson Vision Care for its branded contact lenses and enforced against contact lenses resellers – including Costco.

The Unilateral Price Policy ("UPP") provides in part:

> "The UPP establishes a minimum price below which no reseller can advertise or sell a particular product [branded contact lenses]. The intent of the policy is to reinvigorate the rich clinical dialogue that is so important to effective patient care, rather than focusing on cost."
>
> "Under this policy, Johnson & Johnson Vision Care, Inc. (J&J) and its authorized distributors will cease to supply UPP products to any reseller who advertises or sells UPP products to patients at a price below the UPP price listed below."
>
> "This policy is unilateral and does not represent an agreement between J&J and its authorized distributors or resellers. As such, this policy is non-negotiable and individual representatives are not authorized to alter, waive, modify or negotiate this policy. Resellers are free to advertise and sell any UPP product at a price of their own choosing, however, violations will result in loss of product supply."

In a FAQ sheet on the UPP, the supplier elaborates on the reseller's ability to advertise, or sell, below the UPP price:

> "Q. Am I permitted to sell UPP products above or below the UPP price?"
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> "A. You are free to sell product you have purchased at any price you choose. However, if you sell product below the UPP price, J&J and its authorized distributors will refuse to accept new orders from you. In addition, J&J will exercise its right to repurchase your current inventory of products subject to the UPP price. If you sell product at or above the UPP price, J&J does not consider this to be a violation of the UPP."

The key legal issue in this case is whether there is an agreement between Costco, J&J and its authorized distributors that the products will not be advertised or sold below the minimum price (Costco's theory); or whether J&J has simply announced a unilateral policy (i.e., no agreement) that it will not sell to any reseller who violates the supplier's minimum price policy (J&J's theory).

Costco argues there is an agreement with J&J that Costco will not advertise or sell the products below J&J's minimum price, and claims this agreement violates the federal antitrust laws and several state antitrust laws (California, New York and Maryland are cited in the complaint).

J&J is expected to argue there is no such agreement; that it has unilaterally announced a non-negotiable resale price policy and will enforce it by refusing to do business with any reseller who violate the policy; and that this unilateral conduct does not violate any federal or state antitrust laws.

Background

In 2007, the U.S. Supreme Court overruled its own 1911 decision and held that a manufacturer does not necessarily violate the antitrust laws by establishing minimum resale price for its products with its dealers and enforcing the policy by terminating dealer or other reseller who sells below the minimum price. (*Leegin Creative Products , Inc. v. PSKS, Inc. d/b/a Kay's Kloset…Kay's Shoes*, Docket No. 06-480).

The Court ruled that a supplier's "vertical agreements [with its resellers] establishing minimum resale prices can have either procompetitive or anticompetitive effects, depending upon the circumstances in which they are formed." Thus, these agreements should no longer be per se (or automatically) unlawful, as previously ruled in the 1911 case. Rather, courts should apply the "rule of reason" standard to decide, on a case-by-case basis, whether a particular vertical price restraint violates <u>*federal*</u> antitrust law. It should be noted that federal antitrust law does not preempt state antitrust laws concerning the legality of vertical minimum resale price agreements. As stated above, Costco cites California, New York and Maryland laws as holding that these agreements are illegal per se

The Costco case was filed on March 2, 2015 and obviously is a long way from resolution of the legality of the supplier's minimum pricing policy. This case does illustrate the continuing confusion and uncertainty that exists under antitrust laws as to whether—and to what extent—a supplier can dictate or influence a reseller's pricing decisions.