Deliberately Misclassified?
What Allstate Has In Common With FedEx

"When employers hire a work force, a fundamental preliminary decision with serious economic repercussions must be made: Are workers employees or independent contractors?" This opening statement is from a Dec. 14, 2007 Law.com article written by Carla Rozycki and Darren Mungerson entitled "Misclassification of Independent Contractors and Employees Can Be Expensive."

The focus of the Law.com article is the legal battle being waged against FedEx by its "independent contractor" Ground/Home Delivery drivers. At issue is a class action lawsuit encompassing approximately 14,000 current FedEx Ground/Home Delivery drivers and possibly as high as 10,000 former drivers. The case revolves around whether or not Ground and Home Delivery drivers are independent contractors as labeled by FedEx, or employees disguised as independent contractors. As we will see, this contentious issue has produced a seesaw battle with a final outcome yet to be determined.

With its genesis in 1999, current and former independent contractor FedEx drivers banded together to file a class action lawsuit against their parent company demanding treatment equal to that of their employee counterparts. In the ensuing years of litigation, several legal milestones have been passed, but none was more important to the drivers than the ruling in 2007. On October 15, 2007, Judge Robert Miller from the U.S. District Court of Northern Indiana finally certified the class giving FedEx its most serious legal setback concerning the case up to that point.

Subsequent to the certification of the class action lawsuit, Lynn Rossman Faris, the lead counsel representing the FedEx drivers, quickly issued the following statement, "This is a landmark decision for workers everywhere serving under sham independent contractor arrangements such as the one exploited by FedEx." FedEx responded by saying it would appeal the ruling.

Then on December 22, 2007, the U.S. Internal Revenue Service handed FedEx a second, more serious blow when it levied $319 million in fines and penalties related to FedEx's scheme of misclassifying its Ground and Home Delivery drivers as independent contractors instead of employees. The IRS audit, which concluded in late 2007, stated that "FedEx Ground's pick-up-and-delivery owner-operators should be reclassified as employees for federal employment tax purposes." FedEx's subsequent filing with the Securities and Exchange Commission (SEC) acknowledged that, although the initial ruling was related to the 2002 tax year, the IRS is looking at the next several years as well. Industry analysts close to FedEx estimate a potential IRS fine of over $1 billion. FedEx continues to state that it feels an IRS sanction will be ultimately reversed but, interestingly, began to make changes to its Ground and Home delivery operations in California.

The following is a statement posted by attorneys for the class action lawsuit on its Website: Fedexdriverslawsuit.com:

"FedEx's practice of avoiding tax liabilities and foisting its operating costs onto its drivers has been under continuous attack at the state and federal level for several years." According to the lawsuit, if you are a Ground or Home Delivery driver for FedEx, you are required to meet certain quotas for delivery of packages, you are told how to maintain your truck, you are told who you can hire to help you and even how to dress. FedEx changes quotas annually and implements changes to "Payment per stop" as well as overall "core zone settlement payments." FedEx drivers must pay for all truck operation and maintenance expenses as well as all other business operation expenses. Drivers do not have 401Ks, health insurance, pensions, and are not protected by any state or federal regulations for employees such as Workers Compensation, unemployment benefits and family medical leave. The independent contractor drivers for FedEx were initially happy with their arrangement, but became increasingly aware of the lack of difference between their operational requirements and that of their employee counterparts. When the same controls exerted on employee drivers migrated over to the independent drivers, they began their efforts to gain employee status.

In contrast to their independent contractor counterparts, FedEx employee drivers operate typically in major metropolitan areas. FedEx employee drivers receive many standard employee benefits as well as all the government protections afforded employee status. Employee drivers must meet quotas for pickup and delivery times. They are compensated hourly, but can also earn more via a "bonus" structure. By implementing both employee and independent contractor delivery methods, FedEx retains the profitability of using employee drivers in densely populated areas and the ability to cost-shift expenses to the independent rural drivers. Clearly the ability to avoid expenses like payroll taxes, employee benefits and profit sharing aids FedEx in retaining its competitive edge in areas where paying employee expenses could cause it to be uncompetitive. According to the lawsuit and the IRS ruling, the problem for FedEx is that it's reaping the benefits of treating certain drivers as independent for tax purposes but controlling these same drivers as employees.

The news got even worse for FedEx when the California Supreme Court upheld an appeal for a similar complaint in *Estrada vs. FedEx Ground*. There the court found that FedEx drivers were indeed misclassified as independent contractors stating that FedEx Ground "purposefully created controls of an employee nature" and in summary stated, "We affirm the finding that the drivers are employees." This latest ruling also buttresses decisions from Massachusetts and the National Labor Relations Board, each finding FedEx in violation for misclassification of its independent contractor drivers. In their December 14, 2007 Law.com article, Ms. Rozycki and Mr. Mungerson summarize the ruling further when they state: "Notwithstanding that FedEx drivers executed a non-negotiable Pick-up and Delivery Contractor Operating Agreement, which identified the driver as an 'independent contractor' and not as an 'employee' for any purpose, the trial court found the drivers were employees and therefore had the right to be reimbursed for their expenses." The court's ruling was intended to send the following message to FedEx: Just because you classify a worker as "independent" it doesn't make it so unless you treat them as "independent."

A Trickle Before the Flood?

On October 21, 2008, retired state Superior Court Judge William Cahill, acting as a court appointed official, awarded about 200 California FedEx drivers $14.4 million in their quest to be reimbursed for "employee style" expenses while being misclassified as independent contractors. These expenses, such as uniforms, fuel and truck maintenance, had long been reimbursable to employee drivers, but not to the independent contractor drivers. FedEx stated it would review the ruling and had initially objected to $1 million of the expenses. Cahill stated that only $32,000 of that objected amount would be denied. Then on December 5, 2008, FedEx agreed to settle the California dispute for a whopping $26.8 million. FedEx spokesman Maury Lane stated that the settlement would not affect the company's relationship with its California network of independent contractors and that FedEx was "pleased to put the matter behind us." The 203 drivers involved in the case will receive monetary damages ranging from $2,000 to $280,000.

Because this case is directly related to the larger class action case, completion of the California settlement and the resulting momentum should have a significant impact on future settlements. Interest is extraordinarily high at this point, with fewer than 150 drivers opting out of the nationwide action. This is extraordinary considering more than 27,000 current and former drivers have been notified.

IRS Changes Its Mind on FedEx Fine

On October 23, 2008, the IRS announced the withdrawal of its initial $319 million assessment for back taxes for the 2002 tax year, but is continuing to audit FedEx for years 2004 through 2006. While the withdrawal of the fine was initially thought to bolster management's claim that its drivers are indeed independent, the subsequent $26.8 million settlement in California appears to suggest otherwise. However, while the merits of the case are substantive and could affect similar lawsuits, the IRS may be disinclined to fine FedEx so long as it is working to resolve the issue. Similar IRS rulings where a fine is levied and then retracted are not uncommon. This is frequently the case with publicly traded companies so as not to affect the value of innocent shareholders' stock. In especially egregious cases, however, fines are imposed in spite of shareholder concerns.

FedEx's Slight of Hand

In light of the overwhelming evidence to the contrary, one must ask the question of why FedEx thinks it can treat independent contractors as employees and get away with it. FedEx officials contend that it previewed its independent contractor model with the IRS and received approval to implement the program. Companies often seek rulings from the IRS called "Private Letter Rulings" in order to affirm consistency with IRS

regulations. It is important to understand that while Private Letter Rulings are not filed by companies anonymously, they are reported anonymously. Although not legal rulings in the sense that they come from the government, Private Letter Rulings aid businesses in interpreting tax law as it applies to a specific situation. FedEx received what it thought was a tacit approval and implemented a mammoth change to its delivery system. Failing to realize just how "independent" its independent contractor drivers had to be treated, FedEx immediately began to implement many of the same controls it used with its employee drivers. Certainly it was important for FedEx to retain control over its delivery system, but it failed to realize that in doing so, it immediately converted its independent contractors back to employee status.

Central to FedEx's or any other company's ability to direct the outcome of its business operations, are the controls it institutes. With an employee-based business, directives (controls) are conveyed through employment contracts, memos, contract changes from corporate officers, and written or verbal orders from managers. Employees are subjected to reviews and their performances are compared to expected goals. FedEx employees submit daily delivery sheets, driver logs, fuel receipts, inspection and shipping reports and other reports as required from time to time.

With an independent contractor-based business, controls may not be used for any aspect of the worker's day including, but not limited to; processes employed to accomplish assigned tasks, tools (unless specific to the product being produced), requirements to produce reports, submission to performance reviews, when to perform tasks, where to perform tasks, and requirements to meet quotas.

FedEx's independent contractor drivers were required to submit substantially the same type and quantity of reports as employee drivers. Simply put, FedEx wanted the benefits of control without the associated costs. FedEx's eagerness to use independent contractors is also based in part by its unwillingness to recognize that it was doing something wrong. In his article of April 14, 2008, CNSNews.com commentator Chuck Muth summed it up this way: "But like an alcoholic who can't come to grips with the reality of his problem, FedEx remains in serious denial over this matter."

FedEx Ground and Home Delivery drivers initially embraced their employment model and gladly operated their businesses as independent contractors. However, the economic advantages enjoyed by the employee drivers combined with the employee-like controls that were foisted upon them, was simply too much to take for the independent contractor drivers. After all, they took all the risks, made less money, received fewer, if any, benefits and yet still weren't allowed to run their business as they saw fit. It was for these reasons the independent contractor drivers sought employee status.

The New, Improved IRS Tackles Violators

Employers reap great benefits through the classification and use of independent contractors. Direct financial benefits include savings of state and federal taxes, health insurance costs, pensions, unemployment benefits, 401Ks, operating expenses and costs associated with human resources departments and other support personnel. Other financial benefits include cost savings associated with reduction of management positions, reduction of advertising expenses, and elimination of operating expenses like rent, electricity, phones and computers. Companies who use independent contractors retain a huge financial advantage over their competitors who do not. The dangerous "flip-side" of using independent contractors is improper classification, which exposes both the company and the worker to potential state and federal fines for failure to properly file tax returns. This fact is not lost on the IRS as well as the U.S. Senate. Last year, the U.S. Senate introduced the Independent Contractor Proper Classification Act of 2007 (ICPCA). Both the U.S. Senate and the IRS recognize the severity of the problem and are working with various states to implement statutes aimed at catching companies who improperly classify independent contractors.

Misclassification of employees as independent contractors is not a new issue to the IRS. In the past, individual workers have had the ability to receive an IRS ruling on their employment status by submitting the form SS8. But the bigger problem being addressed by the FedEx ruling has to do with corporations knowingly misclassifying an entire independent contractor workforce or using an independent contractor model that violates federal and or state regulations. IRS officials acknowledge that this problem has been given new emphasis and will be a seminal issue going forward. One such example of this new thinking at the IRS is a program which began last year. In November 2007, the IRS and 29 state government agencies began implementing the Questionable Employment Tax Practice (QETP). The following quote is from the IRS Website: "The QETP initiative is a collaborative, nationwide program seeking to identify employment tax schemes and illegal practices and increase voluntary compliance with employment tax rules and regulations."

Kathy Petronchak, Commissioner for the IRS Small business/Self Employed Division, stated: "Combining resources will help the IRS and the states reduce fraudulent filings, uncover employment tax avoidance schemes and ensure proper worker classification." At hand are billions of dollars in lost tax revenues and simultaneous billions of dollars in questionable profits for the companies that misclassify their workers. Looking at either side of the equation one can easily see the IRS's motivation.

Meet FedEx's Big Brother: Allstate

Back in the year 2000 when Allstate converted the vast majority of its entire sales force from employee to independent contractor status, it did so as a result of a series of events, both external and internal. Notwithstanding an immense logistical process, Allstate apparently accomplished the transition in record time, taking only about two years from start to finish. When Allstate held countrywide meetings rolling out the conversion process, agents were barely able to catch their breath after hearing the announcement that they were going to be independent contractors. Allstate openly reminded

agents that they would be independent contractors and no longer have managers. Agents were congratulated on their new career path as agency owners and urged to immediately begin acting like the entrepreneurs Allstate knew they could be. The company even cautioned its newly-forged business owners not to rely upon their "old" managers for business decisions. Now that agents were independent, their new point of contact would be a Market Business Consultant (MBC) who could only offer "assistance" to them. Armed with this new prospective, agents returned to their offices to begin a new chapter in their careers.

At first glance, there appeared to be a sharp contrast between their former jobs as employee agents and their future as independent contractor Exclusive Agents. But the lines of demarcation faded quickly. Today, tenured agents complain that they are treated more like employees than they were before the conversion. "It's worse," said one agent, "back then we had a pension plan and, if the company wanted to fire you, there was an agent review board process in place. Now, they can fire you with or without reason. Our books of business were supposed to replace our pensions, but managers have started to interfere in the sale process, which has lowered the value of our agencies. This isn't fair because for many of us, our book of business is the most important retirement asset we have."

With the devolution of their status complete, Allstate Exclusive Agents quickly became independent contractors in name only. New production quotas were introduced and routinely increased year after year. Other quotas were introduced as well. Minimum office hours were mandated. Reports that agents previously completed and faxed to their managers were now automated and provided for management's instant review. Agents began receiving emails urging them to sell certain quantities of life insurance and financial products. Not only were these quotas bigger than ever before, they have steadily grown by leaps and bounds on a regular basis. Agents were assimilated into groups in sales territories and began to receive emails from management alternately decrying their poor performance or praising them for being "district" leaders.

When it came time for agents to have "checkpoint" meetings with their Market Business Consultants, they were surprised to learn they were required to submit to full-blown annual performance reviews. Confused by this, many agents attempted to refuse to sign the reviews, stating their refusal was because they were now independent contractors. There have been reports that agents in some markets were given a choice: either comply with the review and sign it or be fired.

In the case of the FedEx Ground and Home Delivery drivers, the key issue is that drivers are suing to regain employee status. For these drivers it is easy to see why they would so aggressively pursue attainment of employee status. Their employee counterparts receive higher overall compensation, do not have to pay out-of-pocket for business-related expenses, and enjoy all the benefits associated with being an employee. The IRS position is that FedEx maintains an illegal employment scheme by cost-shifting operational expenses to what amounts to an employee in independent contractor clothing while it avoids millions in taxes.

The situation for Allstate agents is quite different. The vast majority do not want to be employees. All they want is for Allstate to uphold its promise that they be treated as true independent contractors. Whether by design or a changing legal landscape, it was ultimately Allstate that chose to move away from an employee-based distribution system to one that promised complete freedom for its agents as independent contractors.

If it Quacks Like a Duck, It's Probably a Duck, So Says the IRS

Although not implemented until several years later, the groundwork for Allstate's conversion to an independent contractor agent model began in November of 1988 when it submitted a request for a Private Letter Ruling (PLR) from the IRS. The IRS responded via PLR 8925018, dated March 23, 1989 with James L Brokaw responding for the Office of the Assistant, Chief Counsel IRS. The entire ruling is available for review on NAPAA's Website. Readers should bear in mind that since Private Letter Rulings are reported anonymously, any language that identifies the company requesting the ruling is redacted from the document. So, while the PLR that is posted on the NAPAA Website does not specifically identify Allstate, it has been widely believed for years that Allstate initiated the request. Allstate agents who have examined the document have said there can be little doubt about which company it is. To see for yourself, visit **www.napaausa.org**.

But even skeptics should realize that, if by some small chance that the PLR was not requested by Allstate, its key points are undeniably applicable to any corporation when determining independent contractor status. After all, the IRS doesn't make up different rules for different corporations.

Listed below, starting with the opening statement and progressing to the body of the PLR, are excerpts from the IRS ruling. Note: Some of the identifying terminology has been redacted by the IRS pursuant to its rules.

"This is in response to your ruling request dated November [sic] 1988, submitted on behalf of Insurer, in which rulings were requested concerning the federal employment tax status of insurance salespersons under a new program to be instituted by Insurer."

"The Program will begin with an employee phase that will last for [illegible] full months."

"While employees, the agents will be supervised and controlled by Insurer in their daily activities and compensated in a manner that is intended to tide them over until they can be established as independent agents.

Those agents who successfully complete the employee phase of the Program and show outstanding entrepreneurial abilities will be offered the opportunity to participate in the independent contractor phase of the Program. Agents in the independent contractor phase will be free to run their agencies in virtually any manner they choose with no direction from Insurer."

"Current agents who have shown an ability to operate independently will be allowed to participate in the Program without having to complete the employee phase."

The opening statement of the ruling

was intended to address the conversion process as well as potential new hires into the Allstate Exclusive Agent Independent Contractor program. Tenured agents will recall a nearly identical statement was read to them during the conversion meetings held in 1999. This was no coincidence because, as is typical with most PLR's, the requesting company usually provides an outline of the proposed program and the IRS then reworks it into its response. Agents will remember the chief concern at that time was whether or not existing agents would be required to submit to some form of probationary period or be required to qualify in order to transition to the new contract. Subsequently, written documentation was provided to agents in their conversion packages confirming that they did not have to "qualify" to become an independent contractor agent.

Mr. Brokaw continues his opening statement by specifying in no uncertain terms, several key issues to which Allstate must adhere:

"However, the contracts will stipulate that agents in the IC phase will be free of IC's direction, supervision and control and permitted to perform their services in virtually any manner they deem appropriate. They will also be allowed to work for other companies as long as they do not sell insurance products of Insurer's competitors without Insurer's consent."

"Agents will be free to run their agencies according to their own professional judgment. They generally will have complete control over the hours they work and the hours during which their offices remain open. No reports will be required of the agents except for remittance reports used to transmit premiums and other funds they receive that belong to Insurer. Insurer will not impose minimum production requirements on the agents during the IC phase."

"In the IC phase agent contracts will not be terminable at will."

Intended to leave no doubt as to the ruling, the body of the PLR reinforces several aspects of the introduction. Each of these key issues is a benchmark test for independent contractors. Keep in mind; it is not necessary for a company to actually exert control or employ the use of all of the elements listed below. According to the IRS, it is often sufficient that only one element is present. Going further, the IRS states that even if the "possibility" of control exists, it could be grounds for an IRS challenge.

To make the following excerpts from Private Letter Ruling #8925018 easier to understand, remember to substitute the name of the insurance company each time you encounter "[redacted]" in the text.

"Hours. [redacted] Agents will have complete control over the hours which they work and the hours during which their [redacted] offices are kept open to the public for business. They will, however, be required to remain "actively involved" in the operations of their offices."

Clearly, Allstate agents do not have the freedoms described by the IRS above. Agents are required to adhere to company vacation schedules and to keep their offices open a minimum of 44 hours per week. Additionally, agents are mandated to "call forward" their office phones after 5:00 PM, thereby establishing a minimum daily work schedule. Agents who don't forward their calls are reprimanded and warned that further non-compliance could "jeopardize" their relationship with Allstate. To make matters worse, the company is now controlling the flow of information agents receive via their allstate.com email addresses by blocking certain newsletters and other correspondence from NAPAA.

*"**Supervision.** As noted above, the principal purpose of the [redacted] Agent program is to provide increased incentives to [redacted] agents by allowing them to operate as entrepreneurs. Accordingly, [redacted] Agents will be free to run their agencies according to their own professional judgment. A new management position will be established to coordinate the program. These managers will be available to the [redacted] Agents as a resource for consultation and advice during the independent contractor phase of the program, but the [redacted] Agents will not be required to follow any advice which may be given.*

***Reports.** No reports of any kind will be required or expected of [redacted] Agents during the independent contractor phase of the program, except for remittance reports used to transmit premiums and other funds received by the agents which belong to [redacted]."*

It is important to note that not only do Allstate managers give advice to their agents; they expect them to follow it. Case in point is the plethora of emails urging agents to contact customers about everything from life insurance to "Emerging Business" products. Managers in Florida and elsewhere have organized "Call-a Thons" for life insurance and have inundated agents with emails suggesting specific methods for selling financial service products. They have also gone to great lengths to force agents to attend mandatory meetings to increase sales. In some markets, agents have been grouped into "Teams," receive peer statistics and are strongly urged to perform to company-imposed standards. Agents are inundated with emails and phone calls detailing all of this and more. By definition, consultation is a process initiated by the person or company requiring input. Unsolicited verbal contact, email, regular mail, and faxes constitute supervision. Independent contractors are neither members of teams nor are they in need of supervision. These are most definitely employee controls.

In an effort to manage and control its agents, Allstate produces daily, weekly and monthly reports. And while management maintains that the primary function of these reports is to benefit agents, they are used extensively by management to evaluate agent sales performance, overall performance, progress toward quotas, adherence to compliance issues and more. Agents who don't meet certain criteria, especially when they fail to meet their quotas, are oftentimes intimidated or terminated.

"Smart Reports" provide access to the CSRP, RFG, List 60 and AGY 250 reports. Each of these reports furnishes company managers with detailed information about each agent's performance. This information is then used as a tool to compare individual results with other agents, the results of which are oftentimes used to goad agents into producing more sales or to harass or intimidate them. The company also uses a report called POSIS to determine an agent's success in meeting additional quotas related to Good Student Discounts, Alternate Bind and PQB changes submit-

ted as well as Banking Exceptions and Legal Trailing Document Compliance. The fact that Allstate produces these and other reports for agents is unimportant. Allstate may be entitled to gather all the information it wishes, it just can't use it punitively against the agent as it relates to quotas and annual reviews.

*"**Quotas.** (redacted) will not impose any minimum production requirements on (redacted) Agents during the independent contractor phase of the program."*

This area of control is perhaps not only the easiest to identify, it is also the most contentious. Allstate has implemented a quota system it calls "Expected Results." These quotas are ever-changing and have been used to terminate contracts for "failure to meet Expected Results." Allstate cannot equivocate on this violation of IRS rules any more than any of the others, and has recently embedded this quota requirement into another, more complex agent control system called RFG, or Resources for Growth.

Whereas an independent contractor provides a single purposeful service for his benefactor, and may not be directed, Allstate agents provide their services one policy at a time. The following description can be found under the heading "Independent Contractor" in the small business section on the IRS Website (**www.irs.gov**): "The general rule is that an individual is an independent contractor if you, the person for whom the services are performed, have the **right to control or direct only the result of the work and not the means and methods of accomplishing the result**."

An Allstate agent's work consists of the singular event of writing a single insurance policy. Agents must complete the sale to a level of quality "expected" by Allstate and to adhere to underwriting standards supplied by them. This means they must use Allstate approved underwriting guidelines and complete their work task in a professional and ethical manner.

An Allstate agent's work is not the accumulation of a series of events, or the compilation of a series of events, such as selling enough policies to meet a year-long quota. Therefore, Allstate only has the right to direct the quality of the sale via its underwriting guidelines, thereby instituting an "expected result" which can only be measured one policy at a time. Allstate cannot combine individual sales events into a connected work package. Each sale must stand alone. However, Allstate agents have seen firsthand how the company has capriciously ridden roughshod over the precepts that define their independent contractor status. Just in the past twelve months hundreds, if not thousands of Allstate agents have received letters warning them to make their quotas or else.

While some managers avoid talking about quotas during the year, they openly and aggressively do so during the "Fall Life Promotion." Coinciding with the terminus of the sales year, this sales contest allows managers the opportunity to send agents threatening letters that detail their performance shortcomings and reminds them that they are still "responsible" for meeting their Expected Results (quotas).

Rules for Everyone Except Allstate?

The opening of this article cites a fundamental decision that every company faces when hiring a work force. Once a company makes a decision to hire independent contractors, it forever relinquishes a defined amount of control. IRS rules, as cited in Allstate's PLR, explain what constitutes control for any company, not just Allstate. Regardless of how Allstate responds to this article, the IRS ruling applies to any and all insurance companies using independent contractors. The rules do not change just because a different name might be positioned in the header. The following excerpts from the Allstate PLR lists several factors the IRS uses to determine if a worker is an employee or independent contractor. Even a brief examination will reveal that Allstate agents are misclassified.

"Factors taken into consideration by the courts and Service when determining whether the requisite control exists which are relevant to the present situation include the following:

***Training.** The right on the part of the insurer to train the agent shows control. (MFA Mutual Insurance Company v. United States. 314 F.2d 590 (W.D. Mo. 1970))*

***Hours.** The right on the part of the insurer to require the agent to work full-time or a set number of hours shows control. (Rev. Rul. 69-287, 1969-1 C.B. 257)*

***Supervision.** The right on the part of the insurer to supervise and direct the agent as to the time, place and manner of selling insurance shows control. (Kershner v. Commissioner, 14 T.C. 168 (1950))*

***Reports.** The right on the part of the insurer to require the agent to submit detailed reports reflecting his or her sales activities shows control. (Rev. Rul. 58-176, 1958-1 C. B 349)*

***Mandatory Attendance at Meetings.** The right on the part of the insurer to require the agent to attend scheduled meetings shows control. (Ellison v. Commissioner. 55 T.C. 142 (1970))*

***Quotas.** The right on the part of the insurer to impose sales quotas on the agent shows control. (Zipser v. Ewing. 197 F. 2d 728 (2nd Cir. 1952))*

***Discharge.** The right on the part of the insurer to discharge the agent at will shows control. (Rev. Rul. 58-177, 1958-1 C.B. 351)*

Obviously the more control factors which are present in a relationship, the more likely the agent will be treated as an employee, rather than an independent contractor."

With So Many Infractions, can the IRS Be Far Behind?

Likely, some readers are incredulous over why a large corporation such as Allstate would act counter to an extremely detailed ruling in response to a PLR it sought from the IRS. Speculation would range from innocent miscommunication to outright flaunting of the law. For FedEx, it clearly centered on lowering operational costs in order to gain a competitive edge. The independent contractor drivers, on the other hand, would then be saddled with operational costs and have no benefits while the company still treated them like employees.

Either FedEx failed to recognize the severity of its control over its Ground and Home Delivery drivers or it figured it would capitalize on the drivers' naiveté. But if it thought the drivers wouldn't know any better, it was dead wrong. Indeed, the drivers did recognize it and were able to organize with legal and

union representation. For its part, the IRS makes no distinction for the reason of the activity, it simply requires adherence to the law.

It would seem that Allstate agents were never intended to be allowed to be truly independent. From the beginning of the transition process, the company incorporated an open-ended unilateral contract with a "supplement" that could be altered with little or no notice. Much like with FedEx's drivers, Allstate's motivation for its conversion from employees to independent contractor agents is multifaceted. The final impetus for Allstate converting its employee agents was likely due to a combination of potential inroads by its competition and multiple lawsuits relating to the tax status of employee agents, many of whom were filing Schedule C's with their tax returns.

Then recently hired president Ed Liddy had previewed his management style at Sears when he terminated tenured employees and hired them back as part-timers. This move alone saved Sears millions of dollars in health insurance, pensions, 401k plans and associated employee perks. Mr. Liddy chose to duplicate his prior efforts at Sears and rolled out an employee-to-independent contractor conversion just as soon as he could.

While this move assured shareholders of a leaner overhead, it left some Allstate managers with doubts about the efficacy of this new agency model. Clearly, the company did not want 13,000 newly minted independent contractor agents running amok. Ed Liddy was confident the outcome would be otherwise and for good reason. Perhaps he was cunning enough to understand that he could ultimately keep employee-like controls in place by retaining the company's huge arsenal of managers to administer the company's edicts. If that was the case, he succeeded.

Ultimately therefore, one must assume it is the overwhelming necessity for control that overcame Allstate's corporate sensibilities. Because the agent employees' controls were so deeply embedded, the company had no desire to convert its long-standing corporate culture to accommodate an independent contractor model. Also endemic to Allstate's quandary is its frighteningly short hiring process and a certain fear that a newly hired agent might not be capable of living up to its expectations. As employees, agents can be easily terminated for failure to perform. As IRS approved independent contractors, a different set of standards for expectations and termination processes precludes Allstate's previous management style. Additionally, Allstate never fully transitioned its managers away from their hands-on, controlling style of management. Simply put, Allstate was mandated to change, but it could never abandon what for them was the only thing it knew. And as of today, managers are even more brazen.

Employee vs. Independent Contractor

How much control is acceptable?

1. Quotas, also known at Allstate as Expected Results. Potential terminable offense.
2. Mandatory office hours. Monitored and reported to your manager. Potential terminable offense.
3. Mandatory call forwarding. Also monitored for non-compliance by management. Potential terminable offense.
4. Mandatory meetings and training sessions.
5. Blocking agents from receiving email from their professional trade association.
6. Ever-changing standards for approvals to purchase books of business, as well as changing criteria for mergers, or satellites.
7. Denying buyer approval without providing a reason.

Where Do Agents Go from Here?

Understanding that there is a problem is part of implementing a solution. Likely, there are members of Allstate management shaking their heads in denial over this article. And just as surely, there are agents who may doubt the extent of

the problem. Make no mistake about it; the level of control FedEx exerts over its drivers is a pale shade of gray compared to controls Allstate exerts over its agents. FedEx drivers have their issues to be certain. But virtually every aspect of an Allstate agent's job has been converted back to the days of employee status. Certainly the IRS will be evaluating many corporations in the coming months, Allstate included. Allstate agents can become involved by simply retaining emails from managers. Agents should become more informed by reviewing the IRS guidelines for independent contractors. From a non-Allstate computer, agents can do a GOOGLE search on such topics as "IRS fines FedEx", "FedEx drivers' lawsuit" and "IRS independent contractor." Such searches will yield a large amount of information. Naturally, the company would prefer that agents don't see it. But as always, knowledge is power. Use it.

Agents should demand a true independent contractor agreement like the State Farm contract. Their contract is bilateral, stapled, devoid of quotas, office hour requirements and conforms to IRS standards. Unless and until the unilateral contract is eliminated, agents will not be truly independent. Agents may also wish to contact the IRS on their own. On the state level, agents can inquire with the attorney general's office to determine if there are special rules or laws pertaining to independent contractors and if their state uses the Questionable Employment Tax Practice (QETP).

Pursuing a legal remedy is never easy, but it is a process that can be won. If enough pressure is brought to bear, if enough light is shed on this issue, if enough agents stand up for their rights, then change can occur. Above all else, agents need to communicate with one another, share experiences, share information, and document everything Allstate management sends to them.

In order to be independent, agents must act independent and be treated as independent. The next time you get a warning letter, or the next time a manager emails you about your year-to-date performance, remember that you are not independent. The next time you sit down for your annual review, or get an email reminding you that you must keep your office open the day after Thanksgiving or on Christmas Eve, or get an email reminding you to forward your phones, you are not independent.

Independent contractors do not have mandated office hours, quotas, or mandatory sales meetings. Independent contractors are not grouped into teams, and do not have to sell insurance products in order to help managers make bonuses.

In conclusion, I leave you with a final direct quote from the IRS Private Letter Ruling to Allstate:

"Part IV
Application of the Law to the (redacted) Agent Program
In contrast, (redacted) Agents in the independent contractor phase of the program will not be subject to (redacted) supervision or review, nor will they be required to follow (redacted) instructions, attend meetings or meet any quotas. Rather, the details of their daily activities will be left entirely within the scope of their own professional judgment-- a factor crucial to the finding of an independent contractor status."

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