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Is Your Independent Contractor Truly Independent?

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In the trucking industry the use of independent contractors, also known as owner-operators, is very common. These independent contractors own their own trucks and enter into a relationship with a carrier in which their truck is operated under the carrier's name, authorities and insurance. These relationships are usually governed by a written agreement which, for the most part, has not been drafted or reviewed by a lawyer, or which is based on an old precedent which has not been updated in years.

The owner-operator agreement almost always includes a term by which the parties agree that the owner-operator will provide trucking services as an independent contractor, and that the contract does not create an employer/employee relationship. However, when the relationship breaks down there is often a fight over the true status of the owner-operator, as this party attempts to demonstrate that an employment relationship exists so as to be able to claim a number of benefits from the carrier including the application of employment standards legislation, reasonable notice upon termination and vicarious liability. The courts have developed tests to apply to the facts in order to determine whether one is an employee or an independent contractor. The recent Ontario Court of Appeal decision in *McKee* v. *Reid's Heritage Homes Ltd.* 2009 ONCA ("*McKee*") confirms that there is a third category to be considered in assessing these relationships, that of dependent contractor.

Before turning to the *McKee* decision, it is useful to review the tests the courts rely on to assess the true nature of these relationships. While a full analysis of the tests the courts have applied in order to determine whether one is an independent contractor or an employee is beyond the scope of this paper, these tests were summarized by the Supreme Court of Canada in *671122 Ontario Ltd.* v *Sagaz Industries Canada Inc.* [2001] 2 S.C.R. 983 ("*Sagaz*"). The court in *Sagaz* suggested that there is no one universal test that is applicable in all circumstances, and that the court must consider the total relationship between the parties, as well as the purpose of the classification (i.e., a finding of vicarious liability, or entitlement to notice upon termination) in order to determine which factors should be considered more important. In *Sagaz*, the purpose of classification was a finding of vicarious liability, and the court considered the following factors:

1. whether the worker provided his or her own equipment;
2. whether the worker hired his or her own helpers;
3. the degree of financial risk taken by the worker;
4. the degree of responsibility for investment and management needed by the worker; and
5. the worker's opportunity for profit.

The court framed the central question as whether the person performing services is doing so as a person on his or her own account and stated that in answering this question, the level of control over the person is always a factor.

The *McKee* Decision

On January 8, 1987, Orin Reid, owner of Reid's Heritage Homes Ltd. ("RHH") and Elizabeth McKee ("McKee"), through her business style, Nu Home Consultant Services ("Nu Home") signed a Sales and Advertising Agreement which provided that RHH supply 69 homes for McKee to advertise and sell, and that she would charge $2,500 for each home she sold. The Agreement also provided that RHH had the sole use of Nu Home, unless RHH agreed to let Nu Home sell for another company controlled by Reid. Finally, the Agreement provided that it could be terminated by either party, for any reason, on 30 days notice.

After the first 69 homes sold, RHH continued to provide McKee with homes to sell, but not advertise, at a fee of $1,500 per home sold. RHH gave McKee stationery and forms for the sales, and the title Sales Manager. McKee was paid through her corporation which in 1988 was changed to Bibet Holdings Inc. ("Bibet").

McKee eventually hired, trained and managed sub-agents. She split her commission with the sub-agents. McKee invoiced RHH through Bibet, and paid her sub-agents through Bibet.

In 2005, Reid's successor told McKee that she and her sub-agents would have to work for RHH as direct employees. RHH offered only

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a standard form employment contract with a 14-day notice period. McKee and RHH were unable to negotiate a satisfactory employment agreement and McKee sued RHH for wrongful dismissal. The trial judge found that the original 1987 Agreement was "spent" after the sale of the initial 69 homes, and that McKee was an employee, not an independent contractor, because McKee's activity, selling homes, was an integral part of RHH's business.

On appeal, RHH argued that the law provides for an intermediate category of dependent contractor, defined by economic dependency in the work relationship. After reviewing the case law, the Court of Appeal concluded that:

> "...an intermediate category exists, which consists, at least, of those non-employment work relationships that exhibit a certain minimum economic dependency, which may be demonstrated by complete or near-complete exclusivity. Workers in this category are known as 'dependent contractors' and they are owed reasonable notice upon termination."[1]

The Court of Appeal went on to state that the legal principles applicable to distinguishing between an employee and an independent contractor apply equally to the distinction between an employee and a dependent contractor. In other words, the dependent contractor category is a "carve-out" from the non-employment category. The first step is for the court to determine whether the worker is a contractor or an employee, based on the analysis in *Sagaz*, and other decisions, in which exclusivity is but only one factor. Once a court has determined that the worker is not an employee, but a contractor, the next step is to determine whether he or she is independent or dependent. In this part of the analysis, a worker's exclusivity is determinative, as it demonstrates economic dependence. The Court of Appeal stated that a dependent contractor, because of its economic dependence, would be entitled to reasonable notice upon the termination of the contract.

The Court of Appeal did not provide any guidance as to how reasonable notice should be calculated in the case of a dependent contractor, and whether or not it should be based on the same factors used for employees, which include character of the work, length of service, age, availability of other opportunities. The Court of Appeal also did not refer to any other benefits (or consequences) that flow from being classified as a dependent contractor.

While the Court of Appeal agreed that the dependent contractor category exists, it went on to uphold the trial judge's finding that McKee was an employee.

Impact on Trucking Industry

In the trucking industry, owner-operator agreements often contain a non-exclusivity clause. Such a term may not be enough to ensure that the owner-operator is found to be an independent contractor, as a court will consider a number of factors in order to determine the true nature of the relationship. Given that the owner-operator uses the carrier's insurance, the carrier's authorities, and must display the carrier's name on its trucks, the practical reality is that the owner-operator is not usually free to use its truck to provide trucking services for others. This results in exclusivity and, accordingly, economic dependence on the carrier, which would lead to a finding that the owner-operator is a dependent contractor.

While the *McKee* decision may be of assistance for carriers in ensuring that in the contest between employee and contractor, contractor wins the day, the *McKee* decision may also lead to a finding that the owner-operator is not an independent contractor but is a dependent contractor, thus exposing the carrier to having to provide reasonable notice upon termination of the contract, which notice may very well exceed what the parties have provided for in their written agreement. It remains to be seen whether additional benefits may also be available to the dependent contractor.

All parties to these types of arrangements are reminded of the importance of carefully drafted agreements which accurately reflect the true nature of their relationship.

Endnote

1. McKee's at para 30.