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Brokers Beware: Wage and Hour Litigation Explodes!

Under the federal Fair Labor Standards Act (FLSA), nonexempt employees are entitled to receive time-and-a-half pay for overtime. Nonexempt employees who have not been paid for overtime work can seek redress through litigation against their employers. These types of cases—commonly referred to as wage and hour litigation—have increased exponentially over the last decade, seeing a 325% increase in both single-action and collective action wage and hour cases brought in federal courts.

The freight brokerage industry has not been exempt from the wage and hour litigation explosion. In September 2010, two former employees of a transportation broker (the Broker) brought a class action lawsuit in federal court on behalf of all current and former employees of the company alleging violation of the FLSA and Ohio overtime compensation laws. Under the FLSA, potential parties must affirmatively "opt-in" in order to obtain class relief. Since the suit was filed, over 150 individuals have filed notices with the court consenting to become parties.

These employees, termed "Logistics Account Executives" (LAE) and "Logistics Account Executive Trainees" (LAET), were paid a salary or a draw against commissions by the Broker. They argue that they should be classified as inside sales people (a nonexempt position) and that the Broker owes them, as well as all similarly situated employees, overtime pay for hundreds of hours worked in excess of 40 hours per week.

The Broker defends primarily by asserting that the employees are exempt from overtime under the administrative and highly compensated employee exemptions contained in the FLSA. The Broker carries the burden of ultimately proving the employees' exemption in order to prevail. To prove the administrative exemption, which is really the ultimate issue in the case, the Broker must show that the primary duty of the employee is servicing the Broker's business, or the business of the Broker's customers, rather than routine sales. Routine sales are considered to be more like a "production" function than an administrative function and often result in a finding that the position is nonexempt. To prove the "highly compensated employee" exemption, the Broker must show the employee is annually compensated at least $100,000 and performs any one or more of the exempt duties or responsibilities of an exempt position.

While the case has not been decided, it has certainly raised the specter of overtime exemption issues for freight brokers across the country. These lawsuits can be financially debilitating, as the FLSA allows prevailing employees to recover double damages unless an employer can show the misclassification was made in good faith. Prevailing plaintiffs are also entitled to recover their attorney fees under the FLSA. Overtime litigation has cost many U.S. employers millions of dollars in a single suit.

The good news is that there are several strategies you can implement to head off such complaints in your own workforce. At minimum, you should perform a classification review to determine the actual job duties of your own employees. Because it is the employee's *actual* job duties that guide the classification, rather than job titles or compensation schemes, it is vital that a broker's employees walk and talk like administrative employees. Their primary functions must not be sales or work incidental to sales. They should be tasked instead with promoting your services generally, negotiating rates and managing transportation arrangements, and other job duties relating to servicing and advising your customer base.

However, it is important to note that no hard and fast rules exist when it comes to the administrative exemption. Consequently, it is strongly recommended that all employers consult legal counsel to determine whether you are properly classifying employees and how to address any potential problem areas.

For more information, please contact Katie Tesner at ktesner@beneschlaw.com or (614) 223-9359.

IN THIS ISSUE:

BENESCH
Attorneys at Law

Mechanic's Liens for Motor Carriers? Consider the Option to Improve Leverage

You may not be a fan of Donald Trump. But, as the saying goes, every blind hog finds an acorn, or, er . . . a truffle. In his book *The Art of the Deal*, The Donald writes: "The best thing you can do is deal from strength, and leverage is the biggest strength you have. Leverage is having something the other guy wants."

"As a motor carrier, you may have never given a second thought to filing a mechanic's lien. You should."

As a motor carrier, you may have never given a second thought to filing a mechanic's lien. You should.

When your company has completed all deliveries or shipments on a project, leverage may include whether you have properly preserved the right to assert a mechanic's lien. A mechanic's lien is a claim created by state statute to secure payment for work performed or materials furnished in connection with the erection, improvement, alteration or repair of a building or other structure. In most cases, a properly recorded mechanic's lien attaches to the land and buildings, and can be foreclosed like a mortgage.

If final payment is delayed or disputed, mechanic's lien rights can determine whether you negotiate from a position of strength. Your customer may be strongly inclined to avoid having a lien recorded, or may make concessions to ensure a recorded lien is released. Why? Because mechanic's liens can be disruptive.

For example, a mechanic's lien could create a conflict between the property owner and its lender. A mechanic's lien could constitute a breach of a covenant in loan documents. If your customer is not the property owner, but a general contractor, a mechanic's lien could create a conflict between the project owner and the general contractor, and place the general contractor in breach of its contract with the project owner. Alternatively, a mechanic's lien could create a significant rift between a project owner leasing real estate from several landowners. While the lien would only attach to the lease interest of the project owner, the landowners may become upset by the appearance of the lien as a cloud on title. Perhaps most importantly, though, a mechanic's lienholder has the right to foreclose the lien and force a sale of the real estate to satisfy its claim.

So, to ensure that you are negotiating with leverage from a position of strength:

1. Review the mechanic's lien statute for the state in which the project is located to confirm that you have the right to assert a mechanic's lien.
2. Strictly observe any pre-lien requirements in the statute, such as a notice of furnishing or notice of intent to file a lien claim.
3. Include all information and detail in your mechanic's lien claim or affidavit that is required by the statute.
4. Be aware of applicable deadlines for filing or recording your lien, and take all necessary steps to make certain those deadlines are met.
5. Perfect your mechanic's lien claim by serving all necessary parties with the filed or recorded mechanic's lien claim pursuant to the statute.

Understanding your mechanic's lien rights and being prepared to assert them when necessary could determine whether you have what the other guy wants when it's time to meet at the deal table. Finish strong!

For more information, please contact J. Allen Jones III at ajones@beneschlaw.com or (614) 223-9323.

Welcome

Wendy Brewer

Wendy Brewer is Vice Chair of the firm's Business Reorganization Practice Group and has recently joined the Transportation & Logistics Group. She is board certified as a business bankruptcy specialist by the American Board of Certification and has represented transportation industry clients in a variety of bankruptcy matters on both the Debtor and Creditor side of bankruptcy cases, as well as in adversary proceedings related to bankruptcy cases, such as preference and fraudulent transfer actions. Wendy's clients have included trucking companies, equipment lessors, equipment seller/financers and lenders. Wendy works out of the firm's Indianapolis office.

Sarah Stafford

Sarah Stafford is an associate in the firm's Litigation Practice Group and has recently joined the Transportation & Logistics Group. Sarah's practice focuses on complex business and general commercial litigation for a variety of disputes including breaches of contracts, fiduciary duties, trade secrets and fraud. In addition, she represents clients in transportation-related matters. She has diverse litigation experience in federal and state courts with a focus on disputes before the Delaware federal and state courts, including the Delaware Court of Chancery. Prior to law school, Sarah worked for a third party logistics company in Versailles, Ohio, primarily assisting with Spanish-language interpretation and account services for the company's Mexican logistics partners. Sarah works out of the firm's Wilmington office.

Worker Misclassification Targets the Trucking Industry

Worker misclassification has become a huge issue in recent years, and 2012 looks to be a continuation of this trend. Worker misclassification is the wrongful classification of a worker as an independent contractor or owner-operator when he or she is really an employee. An employee would be entitled to certain rights and benefits from an employer, such as medical leave, overtime pay, disability or minimum wage protections, which would not be available for an independent contractor. And, of course, an employer is going to have certain responsibilities for an employee, such as taxes owed and liability for the employee's actions.

The transportation industry is a particular target of this worker misclassification auditing initiative, and such audits become an issue on several fronts. It affects motor carriers who hire drivers who are independent contractors or owner-operators using an industry-traditional independent contractor business model. These companies may get hit with massive penalties, tax burdens and unpaid wage and overtime bills, crippling them or putting them out of business. Of course, generally, it also affects any company hiring anyone in any other position who may be classified as an independent contractor, which could include third party logistics companies, brokers or freight forwarders who may hire independent contractors as sales agents or for other functions.

One big reason this has become an issue in the past few years is that both the federal government and state governments have shrinking revenues and many are fighting significant budget deficits. Reclassifying workers from independent contractors, who are responsible for their own taxes, to employees means more tax revenues from income taxes, unemployment taxes and workers' compensation premiums, which the employer is responsible for remitting to the government for its employees. These worker misclassifications are really viewed as low-hanging fruit by governmental agencies.

"A proactive evaluation of current independent contractor relationships makes prudent business sense given the current worker misclassification audit initiative."

Another big reason is the current political climate in Washington, D.C. Traditionally, the Democratic party has been favorable to unions, and the Democrats currently have control in Washington. Unions, of course, cannot organize independent contractors, because by definition they are each an individual small business. However, if independent contractors are reclassified as employees of a company, then the opportunity exists for union organization at that facility.

Many recently enacted pieces of legislation and pending bills address worker misclassification in both the federal government and state legislatures. For example, on the state side, California recently enacted a new law, S.B. 459, which penalizes companies that willfully misclassify employees as independent contractors. Fines for this can be as steep as $25,000 per violation if the employer is found to have made a pattern of such practices. In Massachusetts, the parcel delivery industry has been under attack by a law that presumes all workers are employees unless they can overcome the presumption using the "ABC Test." This ABC Test looks at whether (1) the employee is free from control and direction when performing the work, (2) the services performed are outside of the normal course of business of the company, and (3) the worker is normally engaged in an independent business performing these services. While the first and third points may be overcome, it is difficult for transportation companies to overcome the second point because the services that independent contractor drivers perform are typically deemed to be within a transportation company's normal course of business. This statute is currently being challenged in the courts by the Massachusetts Delivery Association on a federal preemption challenge.

On the federal side, a new bill was introduced in Congress in October of last year that is essentially a reintroduction of the Employee Reclassification Prevention Act from a prior session. HR 3178 would impose strict record-keeping and notice requirements on companies. Employers would have to provide written notice to all workers as to whether they are classified as an "employee" or a "non-employee." The company would also have to keep records of hours and wages for each worker. If a business fails to do this, it would be subject to fines of up to $5,000. Additionally, workers would be directed to the Department of Labor's website for a synopsis of their rights as either employees or nonemployees, which would likely include instructions on how to protest their classification if they did not agree. The bill has been referred to the House Subcommittee on Workforce Protections and will need to be watched closely to see if it progresses.

Perhaps of greater immediate concern, though, is the big push for cooperation among federal agencies and state agencies on worker misclassification. In September 2011, the Department of Labor announced that it had signed a Memorandum of Understanding with the IRS to share information and coordinate law enforcement efforts that are meant to stop worker misclassification. The GAO recently reported that the government is losing $2.72 billion to misclassification of workers, and a Department of Labor

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Worker Misclassification Targets the Trucking Industry

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report claims that up to 30% of employers misclassify workers. These reports have motivated governmental agencies to take a long, hard look at worker misclassification and cooperate among themselves to ensure that all agencies can identify the offenders. Thirteen states have also signed a Memorandum of Understanding so that information can be shared freely across federal and state agencies. Right now, California, Colorado, Connecticut, Hawaii, Illinois, Louisiana, Maryland, Massachusetts, Minnesota, Missouri, Montana, Utah and Washington are the participating states, but there could be many more coming soon. So, if a company finds itself in the crosshairs of one agency, it may well get a visit from another federal or state agency looking at the same information.

Be forewarned that any kind of tax audit from one of the aforementioned agencies does not just reclassify workers going forward but also sets up scrutiny for prior years. So, the employer may end up owing not only penalties and more taxes on a going-forward basis, but back taxes on misclassified workers such as FICA, unemployment insurance taxes and workers' compensation taxes, not to mention being on the hook for proper overtime compensation due an employee that would not be due to an independent contractor.

And, of course, in March, the Obama Administration released its proposed budget for 2013, which includes an additional $3.8 million for increasing enforcement related to misclassified workers. The Department of Labor's Wage and Hour Division hopes to hire an additional 35 full-time employees and sign additional Memoranda of Understanding with more states. The Department of Labor recently said that in 2010 it collected almost $4 million in back wages for minimum wage and overtime violations because of worker misclassification issues. Compare that to 2008, when $1.3 million was collected for the same reason, and you start to get an idea of the scope and seriousness of the government's enforcement.

The government assures everyone that these new enforcement efforts are not meant to eliminate the independent contractor business model, but to simply reduce abuses in the system. However, the transportation industry is wise to be concerned that some standard operating procedures in the industry may look like violations to the various enforcement agencies.

So what exactly are these agencies using to determine who is an independent contractor versus who is an employee? Well, the IRS claims that they look at the entire relationship between the company and the worker, and consider the extent of the company's right to direct and control the worker. There is, of course, the traditional IRS Twenty Factor Test, which has now been replaced with an Eleven Factor Test set up in three categories consisting of Behavioral Control, Financial Control and Type of Relationship.

Behavioral Control is defined as whether the company has the right to control or does control what the worker does and how he or she does it. This includes whether the worker is given instructions about when, where and how to perform the work, and whether he or she is trained to perform the work in a particular way. Financial Control means whether the business aspects of the worker's job are controlled by the company. This includes reimbursement of expenses, the worker's investment in tools and equipment, whether the worker performs services for others and how he or she is paid (hourly, weekly or on a project basis). Finally, Type of Relationship includes whether a written contract exists, the extent of benefits offered such as vacation, insurance or pensions, the permanency of the relationship and if the service is a key aspect of the company's regular business.

Each state has its own laws detailing what makes an employee for different purposes and agencies. In some cases, a worker may be an independent contractor for unemployment compensation purposes but an employee for workers' compensation coverage.

A proactive evaluation of current independent contractor relationships makes prudent business sense given the current worker misclassification audit initiative. While all the factors matter in totality, at the very heart of the evaluation is the control test or the amount of control that the company exerts over the worker. One key component for companies is to set up a foundation with the worker, where it is clear that the worker and the company intend for the worker to be independent and earn a profit or loss on his or her own merits. Companies should examine how much control they have over the worker, such as setting work hours, accepting or rejecting jobs, and instructions to the worker. It's certainly okay to require the independent contractor to comply with any customer requirements that may be communicated to the company. It is okay to set general standards which the independent contractor can meet using their own discretion. And, of course, requiring that the independent contractor comply with regulations and safety standards is fine, as long as the company does not instruct the independent contractor on how to meet the standards.

For motor carriers who often rely on the independent contractor model, having workers reclassified from independent contractors to employees can be a game changer. If targeted, some companies may not have the resources to settle with the specific governmental agency regarding their penalties, back taxes and back wages. And even if they do, they may not be able to afford to continue their business given the changes they must make to their company in order

to be compliant with audit findings. Your company's best defense against being caught up in a worker misclassification audit is to simply pay close attention to your independent contractor relationships. Establish your independent contractor program on an arm's-length vendor/vendee business relationship. Focus on the results to be accomplished and not how the work is to be completed. Allow the independent contractor reasonable latitude to make his or her own business decisions. Provide realistic entrepreneurial opportunities to the independent contractor that allow him or her to succeed (or fail) economically on his or her own terms. Carefully scrutinize and analyze any contracts between the company and independent contractors to make sure that they mirror the reality of how the worker is actually treated, and ensure that the managerial and operational conduct of the company's representatives mirrors the contract terms. By examining independent contractor relationships before becoming a target of worker misclassification initiatives, companies can put themselves in the best possible position when and if an audit occurs.

For more information, please contact Teresa Purtiman at tpurtiman@beneschlaw.com or (614) 223-9380.

Special Note

Martha Payne received a Final Determination of Eligibility from the Transportation Security Administration (TSA) and is now authorized to advise and represent Indirect Air Carriers, security screening facilities and domestic and foreign air carriers in regards to security sensitive matters.

Recent Events

Marc Blubaugh moderated a panel discussion on *Transportation and Logistics* for the **Columbus Roundtable of the Council of Supply Chain Management Professionals** in Columbus, OH, on January 13, 2012.

Eric Zalud and **Martha Payne** attended the **Conference of Freight Counsel Winter Meeting** in New Orleans, LA, on January 14–17, 2012.

Martha Payne attended the **SMC³ Jump Start 2012 Conference** in Atlanta, GA, on January 16–18, 2012.

Marc Blubaugh, Wendy Brewer, Allen Jones, Thomas Kern, Teresa Purtiman and **Eric Zalud** attended the **Transportation Lawyers Association's Regional Conference** in Chicago, IL, on January 20, 2012.

Marc Blubaugh attended the **BGSA Supply Chain Conference** in West Palm Beach, FL, on January 25–27, 2012.

Eric Zalud attended the **TIDA 2012 Advanced Seminar** in Miami, FL, on February 8–9, 2012.

Marc Blubaugh attended the **BB&T Capital Market's 27th Annual Transportation Services Conference** in Coral Gables, FL, on February 14–16, 2012.

Eric Zalud presented *The Fox is in the Henhouse. Now What?: Tactical Use of CSA 2010 as a Shield and a Sword in Litigation* at the **DRI Trucking Law Seminar 2012** in Scottsdale, AZ, on February 16–17, 2012.

Rich Plewacki and **Teresa Purtiman** attended the **Food Shippers of America Annual Transportation Conference** in Orlando, FL, on February 26–28, 2012.

Rich Plewacki presented *The IC Model: Update & Ideas* at the **Truckload Carriers Association Independent Contractor Practice & Policy Committee Meeting** in Kissimmee, FL, on March 4, 2012.

Marc Blubaugh attended the **Truckload Carriers Association Annual Conference** in Orlando, FL, on March 5–6, 2012.

Eric Zalud attended the **SCRA 2012 Specialized Transportation Symposium** in Kansas City, MO, on March 7–9, 2012.

Eric Zalud presented *To the Border, And Beyond! Freight Loss and Damage Liability For Cross Border Shipments* at the **TIDA Cargo Seminar** in Tempe, AZ, on March 9, 2012.

Marc Blubaugh and **Matt Gurbach** attended the **International Warehousing Logistics Association's Annual Convention** in San Francisco, CA, March 18–20, 2012.

Martha Payne presented *What You Need to Know to Safeguard Your Business: Legal Issues* at the **Air Cargo 2012 Annual Trade Show and Conference** in Miami, FL, on March 18–21, 2012. **Eric Zalud** also attended.

Martha Payne presented on the *Contract Basics* panel, **Teresa Purtiman** presented on the *Stop Calling It Dispatch, & Other Do's and Don'ts* panel and **Eric Zalud** presented on *Employee Due Diligence* at the **TIA 2012 Convention & Trade Show** in San Antonio, TX, on March 21–24, 2012.

Eric Zalud presented *An Insurance Walk-Through: Alarm Bells, Whistles, and Red Flags that Can Help You Win Your Next Casualty or Cargo Case or Prevent it Altogether!* at the **TLA's Webinar Series** on April 4, 2012.

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Recent Events

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Eric Zalud and **Allen Jones** attended the **Specialized Carriers & Riggers Association's Annual Conference** in Austin, TX, on April 18–20, 2012.

Marc Blubaugh Co-Chaired the **Spring Forum for the Columbus Roundtable of the Council of Supply Chain Management Professionals** in Columbus, OH, on April 20, 2012. **Martha Payne** and **Teresa Purtiman** also attended.

Marc S. Blubaugh with **Anne S. Ferro**, Administrator of the Federal Motor Carrier Safety Administration. Administrator Ferro accepted Marc's invitation, as Past President of the Columbus Roundtable of CSCMP, to serve as the keynote speaker at the Roundtable's Spring Forum on April 20, 2012.

Marc Blubaugh presented *Risk Management: What is the Exposure—Understanding Damages*, **Martha Payne** presented on *Intermediaries—Risky Business?* and **Eric Zalud** presented *Carrier Selection in the CSA 2010 Era* at the **Joint Annual Conference of the Transportation Logistics Council and the Transportation Loss Prevention and Security Association** in Orlando, FL, on April 22–24, 2012. Martha and Eric were also on the *Ask the Experts* panel.

Marc Blubaugh presented *Clowns to the Left of Me; Jokers to the Right: Top Contracting Tips for Intermediaries*, **Niki Schaefer** spoke on *The Food Safety Modernization Act, Case Law Involving Food Allegedly Contaminated in Transport, and the Impact on Food Transporters* and **Eric Zalud** moderated a panel on *International Treaties* at the **Transportation Lawyers Association's Annual Conference** in Naples, FL, on May 1–5, 2012. As incoming First Vice President and Editor of The Transportation Lawyer, Marc attended the Executive Committee Meeting on May 1, 2012. **Martha Payne** and **Rich Plewacki** also attended the Annual Conference.

Eric Zalud presented *Considerations in Buying or Selling a Tank Truck Carrier in 2012* at the **National Tank Truck Carriers 64th Annual Conference & Exhibits** in San Francisco, CA, on May 6–8, 2012.

On the Horizon

Marc Blubaugh will be presenting on the latest developments in transportation law at the **International Warehousing Logistics Association's Legal Symposium** in Chicago, IL, on June 20–21, 2012.

Martha Payne will be attending the **SMC³ Conference** in Chicago, IL, on June 26–28, 2012.

For further information and registration, please contact Megan Pajakowski, Client Services Manager at mpajakowski@beneschlaw.com or (216) 363-4639.

Help us do our part in protecting the environment.

If you would like to receive future issues of this newsletter electronically, please email Sam Daher at sdaher@beneschlaw.com.

Pass this copy of *InterConnect* on to a colleague, or email Ellen Mellott at emellott@beneschlaw.com to add someone to the mailing list.

For more information about the Transportation & Logistics Group, please contact one of the following:

Eric Zalud, *Chair* | (216) 363-4178
ezalud@beneschlaw.com

Marc Blubaugh | (614) 223-9382
mblubaugh@beneschlaw.com

Wendy Brewer | (317) 685-6160
wbrewer@beneschlaw.com

Matthew Gurbach | (216) 363-4413
mgurbach@beneschlaw.com

James Hill | (216) 363-4444
jhill@beneschlaw.com

J. Allen Jones III | (614) 223-9323
ajones@beneschlaw.com

Thomas Kern | (614) 223-9369
tkern@beneschlaw.com

Peter Kirsanow | (216) 363-4481
pkirsanow@beneschlaw.com

Andi Metzel | (317) 685-6159
ametzel@beneschlaw.com

Lianzhong Pan | (011-8621) 3222-0388
lpan@beneschlaw.com

Martha Payne | (541) 764-2859
mpayne@beneschlaw.com

Rich Plewacki | (216) 363-4159
rplewacki@beneschlaw.com

Teresa Purtiman | (614) 223-9380
tpurtiman@beneschlaw.com

Nicole Schaefer | (216) 363-4593
nschaefer@beneschlaw.com

Sarah Stafford | (302) 442-7007
sstafford@beneschlaw.com

Clare Taft | (216) 363-4435
ctaft@beneschlaw.com

Katie Tesner | (614) 223-9359
ktesner@beneschlaw.com

Yanping Wang | (216) 363-4664
ywang@beneschlaw.com

Thomas Washbush | (614) 223-9317
twashbush@beneschlaw.com

E. Mark Young | (216) 363-4518
myoung@beneschlaw.com

BENESCH
Attorneys at Law