

WILLIAM H. BRADLEY
DIRECT LINE: 212.389.5020
Internet: bill.bradley@sablaw.com

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California Unemployment Insurance Appeals Board
Sacramento Office of Appeals
2400 Ventura Oaks Way, Suite 100
Sacramento, CA 95833

Re: Jerrett W. Henderson ("Claimant")
SSN: 572-61-0834
Case No. 1504106
Decision Mailed: May 4, 2005
Board Appeal of FedEx Ground Package System, Inc. ("FedEx Ground")
Employer Account #356 2864-3

Ladies and Gentlemen:

We represent FedEx Ground in connection with the following request that the Board review the decision rendered in the above-referenced appeal, a copy of which is attached hereto as Exhibit "A." FedEx Ground submits that the question of the Claimant's status as an employee for the purpose of the California Unemployment Insurance Code was wrongly decided because, *inter alia*, FedEx Ground was denied the opportunity to participate and submit evidence at the appeal hearing. FedEx Ground requests that it be permitted to submit evidence to the Board¹ or, in the alternative, that the matter be remanded to an Administrative Law Judge for the taking of new and additional evidence.

I. Procedural Background.

The Claimant's Operating Agreement with the FedEx Ground, a copy of which is attached as Exhibit "B," was terminated because Claimant repeatedly failed to perform the services called for under that Agreement. The Claimant did not seek arbitration of the question

¹ FedEx Ground respectfully suggests that the Board can alternatively treat this appeal as a request that the Board remove the proceedings to itself for review and decision pursuant to the provisions of Section 413 of the California Unemployment Insurance Code. This letter will summarize evidence that FedEx Ground would introduce if it is permitted to intervene.

of whether the FedEx Ground was entitled to terminate his Operating Agreement, notwithstanding his contractual right to do so. Instead, on November 24, 2004, Claimant filed a claim for unemployment benefits. The California Employment Development Department (the "Department") denied his claim, finding that Claimant performed services as an independent contractor, and hence that compensation paid to Claimant under the Operating Agreement did not constitute wages for personal services payable to an employee. Claimant appealed that determination.

On February 4, 2005, the Agency mailed a Notice of Hearing in the Claimant's appeal, setting a hearing for March 2, 2005. A copy of the Notice of Hearing was provided to FedEx Ground by a representative of the Department on February 10, 2005, with the suggestion that because of the direct interest FedEx Ground had in the matter, it might wish to intervene. On that date, FedEx Ground requested that it be recognized as a party to the matter and be given an opportunity to present evidence at the hearing, through both documents and live testimony. A copy of the FedEx Ground's request is attached as Exhibit "C."

On February 11, 2005, the Agency issued an "Amended" Notice of Hearing that listed the FedEx Ground as a party to the proceeding. A copy of the Amended Notice of Hearing is attached as Exhibit "D." Six days later, on February 17, 2005, Chief Administrative Law Judge Garcia notified the FedEx Ground that the "Amended" Notice of Hearing was "sent out due to clerical error" and that "[t]he employer should not have been added as a party." A copy of Judge Garcia's February 17, 2005 letter is attached as Exhibit "E."

Judge Garcia's February 17, 2005 letter was misaddressed and, as a result, was not received by a representative of FedEx Ground until February 23, 2005. On February 25, 2005, FedEx Ground requested that Judge Garcia reconsider his decision and reinstate the FedEx Ground as a party to the proceeding. In the letter making that request, FedEx Ground summarized the evidence it would present, if it were permitted to participate in the appeal hearing. A copy of the FedEx Ground's letter to Judge Garcia dated February 25, 2005 is attached as Exhibit "F." On February 28, 2005, FedEx Ground's representative was informed telephonically that Judge Garcia had denied FedEx Ground's request that it be reinstated as a party in the case.

The appeal hearing was conducted on March 2, 2005, without any participation by FedEx Ground, and Administrative Law Judge Garcia did not, therefore, have an opportunity to consider evidence that bears directly on the questions of the Claimant's employment status and the grounds for termination of his Operating Agreement. On May 4, 2005, Administrative Law Judge Garcia issued his decision, in which he determined that the Claimant was an employee of the FedEx Ground and is, therefore, entitled to unemployment insurance benefits on account of the termination of his Operating Agreement. A copy of Judge Garcia's decision is attached as Exhibit "A."

II. Evidence That Was Excluded.

Had FedEx Ground been permitted to participate in the appeal hearing, it would have presented documentary evidence and testimony to show the following facts.

Claimant entered into a contract (the "Operating Agreement") with the FedEx Ground pursuant to which he agreed to provide delivery services as an independent contractor in 2001. Claimant furnished his own vehicle. In the Operating Agreement, Claimant promised to provide delivery services in a defined area. As his business became more profitable, Claimant added a second territory, and engaged a driver, whom he employed and paid, to provide delivery services in that area. Claimant bore the expenses of his operations, including the cost of vehicles, fuel, insurance and compensation to drivers he employed.

Over time, the package volume in the territories Claimant agreed to service became too great for the small size equipment he was using, and FedEx Ground proposed that Claimant either up-grade his vehicles or operate in territories that could be serviced with the smaller vans that he owned. Claimant was unwilling to accept either option, and frequently failed to deliver all packages in the territories where he had agreed to provide service. In addition, FedEx Ground's records show that Claimant and the driver he employed mis-coded a number of packages to indicate that they had attempted delivery of the package, but the customer was not at home to accept delivery, when in fact neither Claimant nor his driver had attempted delivery. FedEx Ground's personnel discussed these and other issues directly with Claimant, and advised him that he was responsible for his own conduct and for the conduct of the driver he employed, and that his Operating Agreement would be in jeopardy if he failed to service his agreed-upon territories or if he mis-informed the FedEx Ground as to why packages provided to him or to his employed driver were not delivered .

When Claimant continued to be unable or unwilling to provide the services he had contracted to provide and his service failures continued to mount, his Operating Agreement was terminated pursuant to its terms. Claimant's Operating Agreement specifically provided for arbitration by the American Arbitration Association of disputes concerning FedEx Ground's decision to terminate the contract. At that arbitration, of course, both sides would have been entitled to submit evidence relating to the termination. Nevertheless, Claimant chose not to arbitrate and, instead, filed the claim for benefits that the Department denied.

III. FedEx Ground Should Have Been Permitted To Participate In The Appeal Hearing.

Judge Garcia's stated reason for refusing to allow FedEx Ground to participate and present evidence at the Appeal Hearing was, "[t]he employer's interests are protected under unemployment insurance taxation law." Although it is true that FedEx Ground has the right to appeal assessments made by the Department for unpaid employment taxes, Judge Garcia overlooked the fact that FedEx Ground has a direct pecuniary interest in Claimant's appeal

because the outcome of the appeal will affect the amount of tax it will be required to pay. *cf. Chrysler Corp v. California Emp. Stab. Comm.*, 116 Cal. App. 2d 8, 14, 253 P.2d 68 (1953).

Moreover, in the FedEx Ground's absence, Claimant's appeal was decided on the basis of an incomplete record, a fact that is amply demonstrated by Judge Garcia's reliance on the plainly mistaken premise that Claimant's Operating Agreement was terminable at will by the FedEx Ground.

IV. The Decision of the Administrative Law Judge In Claimant's Appeal Was In Error.

If given the opportunity, FedEx Ground will show that Claimant should not be classified as employees.

A. Owner-Operators of Trucking Equipment as Independent Contractors

1. History and Background.

The issue raised by the Claimant's appeal is not new. The appeal must be viewed in the context of litigation over the issue over the last 60 years. This litigation has established, as a settled proposition, that owner-operators, such as Claimant and other FedEx Ground Contractors, are independent contractors pursuing a recognized line of business, both under the traditional common law rules, and under the broader "economic reality" test adopted by the United States Supreme Court when it first considered the issue, and concluded that truckers engaged in a local, residential delivery service were independent contractors.

The issue of the status of owner-operators of trucking equipment first arose in the 1940s, shortly after the passage of the Social Security Act.² The Act, which provided coverage only to employees, did not initially specify what definition was to be used to determine employment status, but instead left that determination to the courts. *United States v. Mutual Trucking*, 141 F.2d 655 (6th Cir. 1944) was the first appellate case to consider the issue, and there the court found that the owner-operators were independent contractors. The owner-operators were paid a flat rate for each trip based on a printed schedule. Each owner-operator was responsible for hiring and paying his own drivers (or for driving himself). In addition to the cost of the vehicle, the owner-operators bore the other costs of operation, including vehicle maintenance and repairs. The IRS, which was responsible for enforcing the Social Security Act, took the position that the elements of "control" that were imposed by Interstate Commerce Commission ("I.C.C.") regulations, including, specifically, the requirement that the company represent to the I.C.C. that the vehicles were under its direction and control, established that the

² The Board has recognized that the federal Social Security Act and the California Unemployment Insurance Code should be given similar construction in determining the employment status of workers. *See, In the Matter of: So. Calif Interviewing Service, Herman and Ruth Levine, d/b/a, Precedent Tax Decision No. P-T-104* (1971). As shown below, the IRS, in interpreting the Social Security Act, has determined that the Contractors are independent contractors.

owner-operators were employees. The court disagreed, and found the owner-operators were employees.

The issue reached the United States Supreme Court in 1947 in the companion cases of *Harrison v. Greyvan Lines* and *United States v. Silk*, 331 U.S. 704 (1947). In *Greyvan Lines*, the government argued that the fact that the owner-operators could be required to follow a manual of instructions and to wear a uniform established that they were employees. They were required to haul exclusively for the company, and to paint the designation "Greyvan Lines" on the sides of their vehicles. Owner-operators were required to follow all rules, regulations and instructions of the company, and to take a short course in the company's method of doing business.

Silk, the companion case to *Greyvan Lines*, involved both owner-operators of coal trucks that were used for local deliveries of coal from a central coal-yard to households and the status of coal "unloaders"—that is, laborers who unloaded coal from the rail cars. The putative employer claimed these individuals were independent because they furnished their own shovels, worked largely on their own schedules, and were free from direction and control.

The Supreme Court found that the owner-operators in both cases were independent contractors. Their investment in equipment, and opportunity for profit and loss, outweighed the alleged control features. The Court did not distinguish between the over-the-road contractors involved in *Greyvan Lines* and the local, residential delivery contractors involved in *Silk*, and treated both as independent. The Court, however, came to a different result with respect to the unloaders. Its opinion took into account the purpose of the Social Security Act, and found that Congress had intended to provide coverage for those workers who were employees "as a matter of economic reality". Significantly, the Court respected the status of the owner-operators as independent contractors even under the broader "economic reality" test.

The continuing validity of these decisions is demonstrated in recent cases, including those involving California companies. *Merchants Home Delivery Service, Inc. v. NLRB*, 580 F2d 966 (9th Cir. 1978) involved a California-based contract carrier with operations in 22 states. The company was engaged primarily in the local delivery of household appliances to residential customers. The issue before the court was an appeal by the company from an NLRB determination that had treated certain of its owner-operators as employees of the company. The court recognized that it "is the rare case where the various factors [regarding employment status] will point with unanimity in one direction or the other". 580 F2d at 973. The court found a number of factors in the case that could indicate control by Merchants over some details of the deliveries: the fact that the deliveries must be made in washed, painted, distinctively identified and well maintained vehicles by courteous, cooperative and possibly uniformed personnel, and the fact that Merchants could enforce compliance by means of notices of sub-standard performance, three of which could result in termination.

The Ninth Circuit found that the entrepreneurial characteristics of the arrangement tipped the balance in favor of independent contractor status, pointing to the fact of the owner-operators' investment in equipment, their responsibility to maintain the equipment, their right to hire assistants, and the fact that two of the six operators in question owned more than one vehicle. The court noted the fact that the owner-operators did not have a proprietary interest in their territories, and treated this as an adverse factor, but still not one strong enough to tip the balance in favor of employment.

North American Van Lines v. NLRB, 869 F.2d 596 (D.C. Cir. 1989), involved an interstate trucking company that recruited, trained and provided competitive vehicle financing to most of its owner operators. In order to match loads with available drivers, company personnel used threats and promises of benefits to convince drivers to carry contracted loads. The company issued "30-day letters" to drivers with whom it was dissatisfied, informing them that the company would decide within 30 days whether it wished to terminate the driver's contract. In support of its finding that the owner-operators were independent contractors, the court noted that the drivers held an equity interest in their trucks, and assumed entrepreneurial risks through their control over their operations, and they were paid by the job rather than on the basis of time worked.

Lerma v. United States, 716 F. Supp. 1294 (N.D. Cal. 1988) *aff'd without opinion*, 876 F.2d 897 (9th Cir. 1989) is one of a series of cases considering the potential liability of the United States under the Federal Tort Claims Act, pursuant to which the United States is liable for negligent acts of a government employee, but not for those of an independent contractor engaged by the government. *Lerma* involved a claim by an injured plaintiff that, because of certain "controls" it imposed relating to scheduling, type of equipment and certain operating procedures, the United States Postal Service should be considered to be the employer of a truck driver engaged by a delivery service to transport mail. In finding that the independent contractor status of the delivery company should be respected, the court examined the detailed contract used by the Postal Service, but found it to be specifying results only.

These cases, and a number of others, establish the over-whelming presumption that, regardless of the definitional standard used, owner-operators of trucking equipment are recognized to be independent contractors. No different standard applies for California purposes. For example, in *S. G. Borello & Sons v. Department of Industrial Relations*, 48 Cal. 3rd 341 (1989) the California Supreme Court, used a "purposeful" test to find that migrant workers engaged to harvest cucumbers were to be treated as employees for purposes of the California workers' compensation statute.³ The California Court cited and relied upon the decision of the United States Supreme Court in *Silk*, discussed above, to find that these individuals, who performed "only simple manual labor" and who invested nothing but personal service and hand tools, were, like the coal unloaders in *Silk*, employees, rather than independent contractors. The

³ Unlike the California unemployment tax statute, which mandates the use of the common law test, the workers compensation statute at issue in *Borello* is silent as to what test is to be used.

Borello decision furnishes no basis for finding any of the Contractors to be employees, much less the Claimant, who had a significant investment in two vans and employed drivers himself.

2. **The Independent Contractor Issue as Applied to FedEx Ground Contractors.**

The issue raised by the Claimant's appeal is not a new one for FedEx Ground, as both the IRS and the Department proposed, under a different Operating Agreement that was in effect in the first years of the company's existence, to reclassify the Contractors as employees. (At the time of those proposals, the Contractors almost exclusively served single work areas.) After a thorough review, both the IRS and the EDD resolved the cases by settling—for a fraction of the proposed assessments—the years before 1994 (the year the current Operating Agreement went into effect), and acquiescing in the Company's treatment of the Contractors as independent contractors for years subsequent to the implementation of the revised Operating Agreement.⁴

As shown below, the decision of both the IRS and the Department to respect the independent contractor treatment was correct when it was made. Nothing has happened since that would justify a change. FedEx Ground and the Contractors have relied on these decisions in structuring their business relationships over the past nine years, and it would be manifestly unfair to upset those relationships now, particularly given the fact that there have been no changes to the contractual arrangement.

FedEx Ground began operations in 1985 as Roadway Package System, Inc. The contract in use at that time did not specifically limit the authority of officials of the company from making demands on the Contractors that were not specified in the contract; it did not provide a financial remedy to a Contractor who was terminated by the Company even though he was not in breach of the contract; it imposed no financial burden on a Contractor who simply abandoned his contractual obligations; it did not place any limits on the Company's ability to add or take away accounts from a particular contractor; it did not make it clear that a Contractor could add additional vans; and it did not provide the Contractors with any equity interest in their work areas. The IRS, upon examination, proposed to treat the Contractors as employees, and, in order to obtain a resolution of the matter, the Company paid the tax and sued for refund in the United States Court of Claims.

The case was resolved through discussions between the Company on the one hand and the IRS and the United States Department of Justice on the other. The Company agreed to implement an entirely new Contractor Operating Agreement that addressed each of the areas of concern to the IRS. With minor changes, this is the Operating Agreement that is in place today. It limits the authority of anyone in the Company to impose requirements on the Contractors that go beyond the terms of the Agreement; it recognizes that the Contractors have a proprietary

⁴ The Operating Agreement between Claimant and the Company was created when FedEx Ground established its Home Delivery Division in 2000. In all respects material to this appeal, it is identical to the agreement implemented in 1994.

interest in their work areas and recognizes their right to sell these areas; it provides that a Contractor is to be compensated if, in the course of a re-configuration of a work area, the Contractor loses accounts; it provides for a liquidated damage remedy to the Company if a Contractor abandons his contractual obligations; and it provides that a Contractor who believes his Agreement has been wrongfully terminated (because he did not breach the Agreement) may pursue arbitration, with significant financial exposure to the Company.

With these changes in place, the IRS agreed that it would respect the independent contractor status of the Contractors, so long as the Company adhered to the terms of the Operating Agreement. The IRS and the Department of Justice settled the years in suit, along with the remaining years prior to 1994, in return for a payment by the Company of approximately 16 percent of the amounts at issue.

The agreement between the Company and the IRS is memorialized in a Closing Agreement, a copy of which is attached hereto as Exhibit "G." The Company has adhered to the terms of this agreement in the years since it was accepted by the IRS. The IRS has examined the Company's compliance, and has not challenged the status of the Contractors. In addition, from time to time, Contractors have submitted so-called Forms SS-8 (which ask for a determination of whether they are employees) and the IRS has consistently concluded that the Contractors are independent contractors.

At the same time the issue with the IRS was pending, the Department proposed to re-classify the Contractors as employees. This issue was resolved by a payment by the Company of approximately one-third of the amounts at issue in the pre-1994 years. The later years are governed by a Closing Agreement, a copy of which is attached hereto as Exhibit H, between the Company and the Department, on which the Company has relied for the past nine years. It provides that if the issue of the employment status of the Contractors were resolved—one way or the other—by a United States Court of Appeals, the parties would be bound by that decision. Otherwise the issue was left open for re-examination. Implicitly, the Closing Agreement recognizes that decisions by the NLRB (which can be appealed by either party only in the event there is a vote in favor of union organization) are not determinative as to the employment status of the contractors, as such decisions are subject to *de novo* review by a United States Court of Appeals. There have been no such votes in favor of union organization at any terminal, and hence there has been no review of any NLRB determination. There is, therefore, no basis to upset the determination made by the Department to respect the treatment of the Contractors as independent contractors.

B. Contractors (Such as Claimant) Operating under the Operating Agreement Are Not Employees.

FedEx Ground is a duly licensed motor carrier engaged in providing a small package information, transportation and delivery service throughout the United States, including California. Since commencing business in 1985, it has provided the package pick-up and

delivery portion of its services through a network of independent contractors. The Contractors are responsible for providing their own vehicles to make the pick-ups and deliveries. They either purchase these vehicles, new or used, or obtain them through bona fide lease arrangements with third parties. The vehicles are required to meet safety requirements and to meet general specifications to ensure their adequacy to perform the required hauling services; within these limits, the Contractors may select vehicle make and model.

The Contractors are responsible for maintenance of their vehicles, and for operating expenses, such as fuel, oil, tires, repairs, etc. Pursuant to federal regulatory requirements, the equipment is marked with the company's logos, colors, etc. While in the service of FedEx Ground, the Contractors may use their vehicles for other purposes, but when they do so, they are required by government regulations to mask or otherwise cover the FedEx Ground logos and identifying marks.

The Operating Agreement specifies a standard of service (the "Agreed Standard of Service") pursuant to which the Contractor agrees to provide daily delivery service to consignees within the Contractor's "Primary Service Area". A Contractor may, however, have more than one Primary Service Area. A Contractor is permitted, with the consent of FedEx Ground and consistent with the capacity of the terminal serviced by the Contractor, to own and operate more than one vehicle under the terms of the Operating Agreement, with any such additional vehicles to be driven by qualified drivers employed by the Contractor. Claimant took advantage of this opportunity.⁵ Because the Contractor is obligated to provide daily service, it is also the Contractor's obligation, at his or her own expense, to secure a qualified replacement driver in the event the Contractor is absent on any day. The Contractor is responsible for assuring that all such employed or replacement drivers meet the applicable regulatory standards, and for all details of the compensation of the employed drivers, including applicable employment taxes.

The Operating Agreement divides insurance obligations between the Contractor and the Company. The Contractor is required, at his or her own expense, to provide "empty mile" coverage in specified amounts. The Company agrees to indemnify the Contractor against liability from operation of the equipment when it is loaded with any FedEx Ground package, provided the Contractor and his/her drivers adhere to a written safe driving policy. In the event the Contractor fails to adhere to this policy, he or she is obligated to provide this coverage at his or her own expense. The Contractors are also responsible for the first \$1,000 of any liability claim, though this obligation is progressively reduced if the Contractor provides continuing safe operations over a period of years. Contractors are, in all events, liable for the first \$1,000 in loss or damage to packages under their responsibility.

⁵ At the time his Operating Agreement was terminated, Claimant had two vans and served two Primary Service Areas. Claimant drove one van himself and paid another individual to drive Claimant's second van and service the second Primary Service Area under Claimant's supervision.

The Operating Agreement provides a compensation package with several components. The principal payment to Contractors is a "Package Pick-up and Delivery Settlement" which is a payment for each package handled and stop made. In situations where the customer density in a particular area is still developing, or when a Contractor is absorbing increased or unusual costs of operation, the Contractor also receives a Temporary Core Zone Density Settlement, which is an amount computed according to an objective formula which takes into account the expected package volume in the area, as well as the particular costs associated with servicing the area, such as, for example, "stem miles," which are the number of miles the Contractor must drive from the terminal to the first customer in the area. Each Contractor also receives a daily Contractor and Van Availability Settlement, which is payable with respect to each business day in consideration of the Contractor making available to FedEx Ground at the start of that day a clean, properly maintained van, driven by a qualified and uniformed operator. Finally, Contractors receive certain incentive payments for meeting performance standards specified under the Operating Agreement.

The Operating Agreement recognizes the Contractor's proprietary interest in the package volume and customers in the Contractor's Primary Service Area, and provides a mechanism whereby a Contractor may sell accounts to another Contractor. A Contractor relinquishing an account is entitled to specified payment from the Contractor assuming that account; Contractors may, however, negotiate increased payments on their own.

The Operating Agreement provides that FedEx Ground will, at the Contractor's election, provide a Business Support Package to the Contractor under which the Company will provide the electronic communications equipment required under the Operating Agreement, provide a wash service for the vehicle, provide a supply of clean uniforms, and permit the Contractor to participate in company-negotiated volume price arrangements for maintenance items, all at a cost that the Company calculates as its cost of providing these items. Contractors who elect not to participate in the Business Support Package must provide these items on their own.

An unrelated investment management firm has designed an HR-10 program, in which a number of the Contractors participate. Such programs are available only to self-employed persons. While the Company directs such portion of the Contractor's settlement to this program as the Contractor specifies, the plan is elective with each Contractor, and the Company makes no contribution to it on the Contractor's behalf. Contractors are not furnished with paid vacations, sick leave, or other "fringe benefits" generally associated with an employment relationship.

At the election of the Contractor, the Operating Agreement is for a term of one or two years. Thereafter it automatically renews itself for successive one-year periods, unless either party gives written notice of cancellation not later than 30 days before the end of the term. A Contractor who terminates the Operating Agreement without giving the required notice is subject to a required liquidated damage provision of \$1,000.

Contrary to Judge Garcia's erroneous conclusion, the Company does not have the right to terminate the Operating Agreement at will. The Operating Agreement is explicit in providing that the Company may terminate the Operating Agreement during the course of any term only in the event the Contractor fails to qualify for company-provided liability insurance and is unable to procure substitute coverage, the Contractor breaches the Agreement, or the Company discontinues or curtails operations at the terminal area. A Contractor who believes that termination by the Company is not authorized by the Operating Agreement may invoke arbitration under the rules of the American Arbitration Association, which will appoint a neutral arbitrator to hear and decide the matter. In the event the arbitrator concludes the termination was not authorized under the terms of the Agreement, the Contractor may specifically perform the Agreement through reinstatement or the Company may elect to "buy out" the remaining term of the Agreement. In either event, a Contractor who prevails in the arbitration is also compensated for lost earnings from the time of the termination.

The Company's operations are subject to the "Lease and Interchange" and other regulatory requirements of the I.C.C., the Department of Transportation ("DOT"), and other state and federal agencies. These regulations require the Company to assume responsibility for the safe operation of the equipment.

The Company provides a familiarization program for new Contractors, including an introduction to the Company, a session reviewing the terms of the Agreement, a session on documents the Company needs for settlement, the use of electronic communications equipment, and a review of the Company's safety program, which has been developed and is conducted pursuant to Department of Transportation regulations. After completion of this formal presentation, representatives of the Company ride with the Contractor to verify his or her ability to operate the communications equipment and the vehicle. The Company expressly informs each Contractor that any advice given to a Contractor during the course of these sessions on techniques that have proven success-full in daily operation is advice only, and that the Contractor is not obligated to accept any such advice.

The Operating Agreement permits the Company a maximum of four company-initiated "Customer Service Rides" (in which a company representative rides with the Contractor) each year. (In addition to the company-initiated rides, an individual Contractor might request additional rides if he or she believes they might be helpful in adjusting his or her Primary Service Area or his or her Temporary Core Zone Density Settlement.) The Customer Service Rides serve the following purposes: to confirm familiarity of the Company and the Contractor or both with the Service Area (this is especially applicable to a Contractor new to the Service Area); to confirm safe vehicle operation as required by both DOT⁶ and insurance carriers; and to assist the

⁶ The Federal Motor Safety Carrier Regulations (49 C.F.R. 390 et seq.) include detailed rules of vehicle operation and require that "every commercial motor vehicle must be operated in accordance with the laws, ordinances and regulations of the jurisdiction in which it is being operated". 49 C.F.R. 392.2. These regulations also provide that whenever "a duty is prescribed for a driver or a prohibition is imposed upon the driver, it shall be the duty of the motor carrier to require observance of such duty or prohibition". 49 C.F.R. 390.11.

Company and the Contractor in the design of the Service Area. The Customer Service Rides are likely to be concentrated in the period immediately after the Contractor begins service under the Agreement, assumes a new Service Area, or after a reported safety violation. The Company personnel who conduct the Customer Service Rides understand, through written instruction to them from the Company, that they have no "command" authority, and that any advice they provide to the Contractor concerning the Contractor's performance of service or about techniques that have proven to be successful for other Contractors is advice only, and not instruction.

The above summary of operations under the Operating Agreement would have been supported by evidence if the Company had been permitted to participate in the hearing. Such evidence would have demonstrated that Contractors such as Claimant should not be characterized as employees under California law. The principal test of whether a relationship is one of employment is whether the person to whom service is rendered has the right to control the manner and means of accomplishing the result desired. Empire Star Mines Co. v. California Employment Commission, 28 Cal.2d 33, 43; 168 P.2d 686 (1946). If control may be exercised only as to the result of the work and not the means by which it is accomplished, an independent contractor relationship is established. Moody v. Industrial Acc. Com., 204 Cal. 668, 670; 269 P. 542 (1928). The terms of the Operating Agreement make it clear that each Contractor has the right to determine how he or she will perform his or her duties within his or her Primary Service Area free of interference from the Company so long as he or she meets the Agreed Standard of Service. On the other hand, the Company has no right to control the means by which the Contractor provides the service, except with respect to safety and other regulatory requirements imposed upon the Company by governmental agencies. As noted below, Judge Garcia's decision ignores the long line of cases that hold that contractual requirements imposed by governmental agencies are not to be taken as an indication of an employment relationship.

It has been held that the right to discharge at will, without cause, is strong evidence in support of an employment relationship. See, California Employment Commission v. Los Angeles Down Town News Corp., 24 Cal.2d 421; 150 P.2d 186 (1944). Conversely, the absence of a right to discharge at will, without cause, would be indicative of the existence of an independent contractor relationship. As noted above, perhaps because he only heard one side of the story, Judge Garcia concluded wrongly that the Company exercised a non-existent right to terminate Claimant's contract at will. In fact, the Company may terminate the Operating Agreement during the course of any term only under very specific circumstances, and even when termination appears to be appropriate, the Agreement provides the Contractor with recourse through arbitration by a neutral third party. In addition, consistent with the independent contractor relationship, a Contractor who terminates the Agreement without providing the company with appropriate notice is liable for a liquidated damage payment of \$1,000.

Several other factors that the California Supreme Court has found to be indicative of a relationship between a principal and an independent contractor are present in the relationship between FedEx Ground and the Contractors under the Operating Agreement. See, Empire Star Mines Co. v. California Empl. Comm., 28 Cal.2d 33, 168 P.2d 686 (1946). For example, the

Contractors fix their own working time. They may arrive for work at the terminal as early or as late as they choose, so long as they complete their routes to the satisfaction of their customers. Also, while Company representatives accompany Contractors on Customer Service Rides a maximum of four times per year, they do not regularly visit the Contractor's route. Nor do they give Contractors directions during the Customer Service Rides. As was the case in Empire Star Mines, the Company representatives may give the Contractors helpful suggestions, but no orders.

C. The Claimant Was An Independent Contractor.

The decision issued by Judge Garcia contains a number of errors that could have been avoided if FedEx Ground had been permitted to participate in the hearing. For example, Judge Garcia found that Claimant's vehicle must be "permanently affixed" with a FHD logo. His opinion displayed no recognition of DOT rules pertaining to vehicle identification; no recognition of prior case law on the point; and no recognition of the ability to mask the logo when the vehicle is used for other purposes.

The opinion states that "Whenever a person was not at home or at a business to accept a package to be delivered, the claimant would leave a door tag with FHD identification advising of the delivery attempt." In fact, Claimant agreed to provide this service. One of the reasons Claimant's contract was terminated was that he failed to leave such notices.

The opinion seems to recognize that Claimant's second van driver was "employed by him." If Claimant has his own employees, he is an employer, not an employee.

The opinion finds that the terminal managers directed or controlled Claimant's employed driver. In fact, business discussion notes that would have been introduced if FedEx Ground had been permitted to participate in the hearing document that all complaints regarding the performance of Claimant's employed driver were directed to the Claimant.

The opinion states that Claimant was terminated because he did not acquire a larger van as instructed. The opinion does not mention that Mr. Henderson was given the option of keeping his smaller van if he would agree to reduce his territory to a size that he could service with the vans he owned, facts that would have been introduced if FedEx Ground had been permitted to participate.

The opinion finds the most important of the FedEx Ground control factors was a non-existent right to terminate the Operating Agreement at will. There is no elaboration of the basis for this finding, and no discussion of the terms of the Operating Agreement. Of course, Judge Garcia did not see the business discussion notes that document Claimant's service failures nor does it appear that anyone pointed out to Judge Garcia the fact that the contract both permitted termination only in specifically defined circumstances and gave Claimant the right to contest his termination in arbitration.

V. Conclusion

As we predicted in our letter of February 25, 2005, Judge Garcia was led into error because he was presented with a one-sided presentation. FedEx Ground was not even permitted to participate, much less to submit evidence which could have resulted in a different outcome. The fundamental unfairness of the situation is readily apparent. FedEx Ground should be permitted to present its evidence, either to the Board or, on remand, to an Administrative Law Judge.

Please direct all future communications concerning this matter to the undersigned at the above address. However, as required by the Board's regulations, FedEx Ground's mailing address is:

c/o FedEx Corporation
Legal Department
942 S. Shady Grove Road
2nd Floor
Memphis TN 38120-4117
Attn: Kathleen L. Chambers, Esq.
Staff Director – Tax Law

Thank you for your attention to this matter.

Very truly yours,

William H. Bradley
by RGM

William H. Bradley

WHB/epb

cc: Mr. Jerrett W. Henderson
Mr. Gale Ferren (California Employment Development Department)
Kathleen L. Chambers, Esq.