



June 19, 2009

Mr. Thomas Short
Assistant Director
Strategic Issues
Government Accountability Office
441 G St., NW – Room 2044
Washington, DC 20548

Re: Data Collection Regarding GAO Study on Worker Misclassification

Dear Mr. Short:

American Trucking Associations, Inc. (ATA), on behalf of the national trucking industry, would like to offer to the Government Accountability Office (GAO) some brief general comments regarding the recent data collection efforts related to the agency's study on worker misclassification. As you may know, the independent contractor business model is widely used in the trucking industry and has been since virtually the industry's inception. Over those decades, the legitimacy of the relationship has been repeatedly upheld by courts and administrative bodies. Indeed, the United States Supreme Court as far back as 1947 affirmed the appropriateness of independent contractor classification in the trucking industry. *United States v. Silk*, 331 U.S. 704 (1947).

In trucking, individuals, who own or lease their tractors and provide driving services (referred to as "owner-operators"), play a significant role in virtually every segment of the trucking industry. They are used in long-haul trucking, household goods moving, home delivery, intermodal operations and in many other sectors. While no precise number of owner-operators is available, it is widely believed that more than 300,000 such individuals are involved in the national trucking industry. The reasons that independent contracting is attractive to both motor carriers and owner-operators are clear.

For motor carriers, owner-operators provide a number of advantages. Owner-operators quite often are seasoned business persons with truck driving experience who are highly skilled and motivated. The availability of such owner-operators and their equipment (through leases of equipment and driver services to motor carriers with operating authority) enables motor carriers to save on equipment and capital costs and provides flexibility to meet fluctuations in demand for trucking services. In addition, owner-operators, like other independent contractor business vendors, typically share the

Good stuff.



For owner-operators, independent contracting provides numerous advantages. The trucking industry offers a unique opportunity for individuals to begin their own businesses. Start-up costs in the trucking industry are within reason and reach of many small business entrepreneurs, consisting principally of the cost of a power unit and various licensing and insurance fees. Thus, while not inexpensive, an initial investment of \$50,000 to \$75,000 can place such a small business person in some segments of the trucking industry and in a position to earn annual revenue of three times that amount. Owner-operators can eventually purchase additional trucks and trailers and employ drivers and other staff to assist in carrying out their business. While most will not have the success—or ambition—of J.B. Hunt, who started with five trucks and seven trailers in 1969 and took his company public in 1983, independent contracting in the trucking industry allows owner-operators to live out their own version of the American dream. Owner-operators transitioning into fleet owners (leasing multiple trucks and drivers to motor carriers) and then into motor carrier themselves is commonplace in the trucking industry.

Moreover, owner-operators feel strongly about their independent status. It allows them to run their own businesses, control their own finances, work the hours and days they choose and ultimately control their working environment. Studies show high levels of job satisfaction among independent contractors. *See Upper Great Plains Transp. Inst., Creating a Competitive Advantage Through P'ship with Owner-Operators* 12 (1992) (95% of the owner-operators surveyed rated “independent lifestyle” as the most important aspect of their job). Indeed, given the historical driver shortage in the trucking industry, owner-operators would have little difficulty finding work as employee drivers. However, they **choose** independent contractor status because of the benefits and opportunities noted above.

The most recent GAO questionnaire regarding possible worker misclassification can be aggregated into five general areas: the need for a clearer definition of independent contractor status; protocols/protections for worker challenges to status; IRS guidance and Section 530 issues; independent contractor tax reporting requirements; and IRS and other governmental efforts to address misclassification. Instead of replying to each individual question, ATA will provide comments related to each of those five general areas.

Clearer Definition of Independent Contractor Status

While no one would dispute that there is some confusion relative to the legal standards for differentiating between an independent contractor and an employee; in general, most laws for which such a distinction is needed (*e.g.* federal employment taxes, federal labor laws, and state workers compensation programs) rely on the common law agency test, often referred to as the right-to-control test. The inherent nature of the right-to-control test, based on an analysis of multiple factors, does not lead to black and white results. Nor does the fact that the definition is applied to a wide variety of circumstances (even in the same industry) lead to precise distinctions. We believe that result is not the

fault of the legal standard, but simply a consequence of the complexity of the analysis and the breadth of circumstances to which it is applied.

While we acknowledge that the common law agency test is not perfect, it is the fairest general standard available and Congress could not simplify it without losing the flexibility needed to examine the diverse situations presented in the real world. Any more categorical approach would result in unfairness. Moreover, creating a new definition would destroy decades of judicial and administrative precedent that guide a classification analysis under the common law standard and provide businesses with information on how to structure their worker relationships to meet independent contractor criteria. A “new” definition would only lead to more uncertainty and years of litigation defining its parameters. Consequently, ATA submits that an attempt by Congress to broadly clarify the definition of independent contractor status would be practically impossible and in many respects counterproductive.

We do note, however, that if Congress elects to wade into that quagmire, it would be best served by developing industry-specific definitions. The factors that most efficiently separate employees from independent contractors in the trucking industry are certainly substantially different from the factors in the health care industry, direct sales industry, or any of the scores of other industries where independent contractor status is common. The Internal Revenue Service has recognized the efficiencies of creating industry specific independent contractor criteria. *See, e.g.* Internal Revenue Service, *Employment Tax Guidelines: Classifying Certain Van Operators in the Moving Industry*, <http://www.irs.gov/pub/irs-utl/van-ops.pdf>. As that IRS effort indicates, more precise definitions and better guidance needs to be aimed as narrowly as possible, probably at various segments of the trucking industry and not necessarily at the industry in general. However, if only a single trucking industry-specific definition is possible, ATA would submit that the following model language provides the best broad-based, industry-specific criteria:

A person operating a motor vehicle for a carrier of property shall be considered an independent contractor and not an employee if each of the following factors is substantially present:

- a. The person makes a material investment or incurs a material obligation related to equipment contracted to the carrier and used in performing service.
- b. The person has direction and control in meeting and performing contract obligations subject to conformance with governmental dictates, lawful requirements of third parties relative to the transport or other contractual obligations undertaken, and any reasonable administrative and clerical procedures needed for contract administration.
- c. The person has the principal burden of the operating costs and personal expenses related to contract work.

- d. The person's compensation is based primarily on factors related to contract work and not on the number of hours worked and affords the person the opportunity to realize a profit or loss based on the relationship of business receipts and expenditures.
- e. The person is responsible for hiring or otherwise engaging and paying the necessary personnel to operate the equipment and meet any contract obligations related to it.
- f. A written contract governs the relationship and specifies the relationship of the parties to be that of independent contractor and not an employer-employee relationship.

The above definition was developed by a Committee of ATA member companies to focus the independent contractor inquiry on those trucking-specific factors that best reflect independent contractor status in our industry.

Protections for Workers Challenging Status

A number of the questions in your latest survey ask about facilitating and/or protecting workers who wish to challenge their independent contractor status. While seemingly well-intentioned, the procedures suggested (*e.g.* access to U.S. Tax Court and providing standardized documents to workers about classification rights) would ensure virtually constant administrative turmoil for companies that utilize independent contractors.

In the trucking industry, many companies contract with hundreds of independent contractor/owner-operators, some with thousands. Among those ranks, no matter how diligently a motor carrier follows independent contractor legal requirements, a few independent contractors may question their status. Consequently, it can reasonably be expected that efforts to facilitate workers' challenging their independent status would increase formal complaints and the attendant drain on the business to deal with them. According, we see little value in creating additional administrative burdens for American businesses to have to deal with.

IRS Guidance and Section 530 Issues

Many of the questions posed in the survey relate to allowing the IRS to provide greater guidance on worker classification questions. As mentioned above, the *Employment Tax Guidelines* developed by the Service for the American Moving Industry illustrates that they can already develop that classification guidance with appropriate industry input. Other more internal Service efforts, such as Revenue Rulings, were limited as a part of Section 530 protection. As discussed below, ATA respectfully submits that the protections of Section 530 are absolutely necessary to curb the natural tendency of the IRS to use its unlimited resources to intimidate small taxpayers into classification

changes. Taxpayers can be put in the position of either having to face crippling legal bills to defend independent contractor status or to having to acquiesce to a status change. Our experience with the Service is that it too often takes a highly adversarial position with taxpayers and is sometimes more interested in maximizing assessment dollars than with fairly administering the law.

Section 530 was enacted in 1978 by Congress in reaction to what was generally perceived as overzealous reclassification efforts by the IRS. *See* H.R. Rep. No. 1748, 95th Cong., 2d Sess. 3-4 (1978). Section 530 was designed and does in practice only protect taxpayers that in good faith have consistently treated workers as independent contractors. Despite the clear wording of the relief in the provision, the IRS tried for years to narrow its scope so as to be able to continue to use its weight to intimidate taxpayers into status changes. Chief among its arguments were that a Section 530 analysis is not available until an expensive adjudication of a workers status is made and employee status found and that the Service could, even when Section 530 was legitimately invoked, still require a prospective reclassification.

The motive behind those positions is obvious. It costs tens of thousands, probably in most cases hundreds of thousands, of dollars to challenge an IRS assessment based on employee reclassification if a fact-intensive trial based on the common law factors is required. If that trial is required either as a prerequisite to invoking Section 530 or for a prospective determination, the taxpayer is positioned to either having to settle with the Service by accepting a reclassification with limited retroactive liability or having to incur potentially prohibitive litigation costs. Given those choices, most small taxpayers would really have no choice at all and would be required to abandon even the most legitimate of independent contractor relationships.

Fortunately, Congress became aware of the IRS strategy and intervened yet again to make clear that taxpayers cannot be leveraged into a settlement by the Service by postponing the analysis of whether Section 530 is available to them. In 1996, Congress amended Section 530 to expressly state that nothing in the law was to be construed to mean that Section 530 “only applies where the individual involved is otherwise an employee of the taxpayer.” *See also*, Internal Revenue Manual § 4.23.5.2.1 (noting the under the 1996 law, that “Section 530 is a relief provision that should be considered as the first step in any case involving worker classification.”). In addition, the 1996 amendments made it clear that when a taxpayer established a *prima facie* case of entitlement to Section 530 relief, the burden shifted to the IRS to prove why Section 530 did not apply. By forcing Section 530 to be considered up front, without a classification determination, Congress effectively forbade prospective reclassifications – once Section 530 is found to legitimately apply, the case is over with no opportunity for prospective reclassification. The Service has recognized that result within its procedures

manual. *See*, IRM § 4.23.5.2.1 (“If the business is entitled to [Section 530] relief, the issue of worker classification will be discontinued.”).

ATA respectfully submits that there is no reason to believe that the decades of heavy-handed IRS reclassification tactics will disappear. Because of that threat and because the limits of Section 530 protection as currently formulated do not apply to those who classify or reclassify workers as independent contractors in bad faith, ATA believes strongly that no adjustment that would weaken Section 530 relief would serve the public interest. To the contrary, unleashing the IRS on a reclassification mission would only create another business-destroying threat for those American businesses that have somehow managed to survive to date the economic turmoil of the last several months.

Independent Contractor Tax Reporting Requirements

A number of the survey questions relate to independent contractor taxation protocols and whether some form of independent contractor withholding should be instituted. As an organization representing primarily businesses that engage independent contractors and not the independent contractors themselves, ATA has limited familiarity with the full implications of such a proposal. However, at least in the trucking industry, independent contractors are truly small businesses and cash flow is almost certainly an ongoing concern. Being unsure of the level of the problem that withholding would create for independent contractors, ATA would simply note that it would oppose any significant withholding requirement that would adversely affect the viability of independent contractor’s businesses. Independent contractors in the trucking industry, like motor carriers, are having a difficult enough time surviving without additional bureaucratic obstacles. Finally, ATA is not aware that there is a tax reporting problem (at least in the trucking industry) related to independent contractors. Indeed, we understand that a recent IRS study found a 97% tax compliance rate for taxpayers receiving Form 1099. Until such time as it is empirically demonstrated that independent contractors are not properly complying with their federal tax obligations, ATA sees no justification in changing the tax withholding laws.

Government Misclassification Detection Efforts

Lastly, several of the survey questions seek a reaction to various types of governmental efforts to measure and investigate misclassification. First, it is difficult to understand how even an impartial evaluator could “measure” the extent of misclassification. Literally, every business that works with independent contractors would have to be individually evaluated relative to its specific circumstances. Theoretically if such a measurement was possible and could be accomplished without bias, no one could legitimately oppose its undertaking.

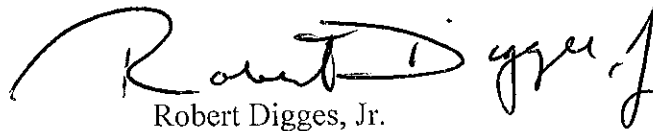
However, we don't see the IRS or state labor departments as that impartial judge and don't see how a business-by-business review could be conducted.

Further, the move to investigate misclassification is plainly politically driven, with almost identical misclassification investigative proposals having been made in the majority of state legislatures. It does not take a crime scene style investigation to figure out who is behind these proposals and why. In our view, this type of misclassification analysis, done by persons whose interest coincides with broad employee classification, will become a self fulfilling witch hunt that will result in enormous administrative burdens for businesses regardless the appropriateness of their independent contractor relationship.

Conclusion

ATA respectfully submits that the focus of the questions asked in the GAO study suggests a philosophy that virtually all independent contractors are being improperly classified. That philosophy comes dangerously close to throwing the baby out with the bath water and so chilling the legitimate use of independent contractors that their place in the American economy will be eliminated. If that happens, American businesses will be less able to compete in the global market and our current economic problems will only get worse.

Sincerely,



Robert Digges, Jr.