In Today's Gig Economy, Are Dealerships Classifying Dealer-Trade Drivers Correctly?

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The term gig economy is not just one you hear millennials use; it's a continuously growing workforce of independent contractors who value flexibility over what used to be referred to as a steady job.

The term gig economy arose from the idea that musicians are paid per gig, but encompasses far more industries than just music. Studies indicate that by 2020, nearly 40% of the American workforce may be independent contractors. Independent workers enjoy being their own boss and the flexibility of deciding when and how often to work, while employers looking to keep costs down like the idea of having necessary services performed by temporary, independent workers instead of regular, full-time employees.

When a business treats an individual as an independent contractor, it can reduce its costs in several ways: it doesn't pay unemployment taxes or workers compensation insurance; it doesn't pay the employer portion of FICA; depending on the state, it can disregard overtime laws for contractors who work more than 40 hours in a work week; it doesn't have to provide expensive employee benefits, like health insurance and vacation; and it doesn't have to withhold state and federal income taxes on compensation (in most instances, contractors are liable for paying their own taxes on income received through these arrangements).

Auto dealers have become willing participants in the gig economy; in fact, they aren't new to the game. The use of dealer-trade drivers as contract workers goes back well before the term gig economy was first uttered by a hipster. But dealers are undoubtedly aware that the gig economy has generated litigation that has heated up regarding improper classification of independent contractors.

Federal and state governments have begun to crack down on misclassification in formal audits, and plaintiff attorneys have filed class action lawsuits against employers in all industries, challenging the classification of many groups of employees, including drivers, sales representatives, and even strippers, seeking to prove they are not independent contractors, but rather employees who are entitled to overtime pay and other employment benefits.

Dealerships are susceptible to misclassification issues

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Auto dealerships, in particular, are faced with challenging employee classification issues. Some dealers have historically sought outside assistance with dealer trades, marketing and merchandising, make-ready, and even new and pre-owned sales functions.

If not set up properly, these arrangements can create ongoing liability for unpaid employment taxes, overtime wages, and potentially even employee benefits. Unfortunately for dealerships, these types of employment misclassification lawsuits are typically time- and cost-intensive—even more so than a regular employment lawsuit, like discrimination or harassment.

In the most common circumstance, many dealerships have treated their dealer-trade drivers (DX drivers, auction drivers, hikers, etc.) as contract labor or independent contractors, paying them for their services on a per-run or by-the-mile basis and without withholding taxes. For many years, this was a fairly well-accepted practice and it rarely resulted in raised eyebrows from regulators or plaintiff lawyers.

During the Obama administration, however, the U.S. Department of Labor began scrutinizing the alleged misclassification of independent contractors, including dealer-trade drivers. Dealers started losing these cases regularly. The pendulum may have started to swing in the other direction; recent case law is favoring independent contractor status for dealer-trade drivers.

Dealer-trade drivers may be independent contractors—in certain circumstances

Smaller dealerships in rural areas often utilize contract dealer-trade drivers. Drivers are often retired individuals who move cars on an as-needed basis. These drivers are used to accomplish a dealer-trade, a commercial transaction whereby one dealership agrees to swap vehicles with another dealership, usually to accommodate a customer's preference.

For example, when a customer has decided on a model but desires a specific option or color that the dealership doesn't have in stock—but is available at a nearby dealership—a dealer trade is often arranged. Most dealers look first to commercial auto transport companies to get the vehicle to the dealership, but trades in very small quantities often mean that this is not feasible. In these cases, drivers may be utilized to pick up vehicles from an auction or another dealership.

In a recent case involving a Texas dealership, the Texas Workforce Commission (TWC) determined during an unemployment tax audit that the dealership incorrectly categorized drivers as independent contractors, saying the drivers were actually employees and should have been paid as such, resulting in the dealership being fined unemployment taxes plus interest. The dealership brought suit in an effort to overturn the determination, and ultimately prevailed in a trial against the TWC in Austin.

The sole issue for the court to decide was whether the dealership properly categorized its dealer-trade drivers as independent contractors. This inquiry turned on the requisite control that the dealership maintained over drivers' work.

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In Texas, there is a common law five-factor test used to determine whether a relationship is an independent contractor or employee relationship; it centers on the control that the employer has over the worker's services.

There is also a 20-factor test (similar to the IRS's former 20-factor test) that the TWC uses as a guide for applying the five common-law factors to determine whether the employer exercises enough control over the work to establish an employment relationship.

In arguing that it did not control the drivers' work, the dealership asserted, among other things, that:

- Drivers drove for other area dealerships;
- Drivers controlled their drives by choosing their own routes and making independent decisions about when to start and how to get from point A to point B;
- Drivers were responsible for their own expenses;
- Drivers charged a flat fee; and
- The dealership was not in the business of transporting vehicles—rather, its business was selling and servicing new and used vehicles, and transportation services were merely a peripheral function, like landscaping services, parking lot maintenance, etc.

The dealership, represented by our attorneys, introduced this evidence at trial, and the court sided with it, finding that the drivers were independent contractors, not employees. Given this decision, dealerships may treat their drivers as independent contractors.

Dealers should be cautious in celebrating this victory. The Texas case included facts that lined up well for the dealership, including factoring expenses like gasoline into the fee and requiring drivers to pay for them themselves, allowing drivers to make runs for competitors, and not requiring the drivers to wear uniforms or follow general work rules applicable to regular employees.

Dealers who treat their drivers this way can feel comfortable considering drivers to be contractors. As always, a prudent employer should consult with employment counsel familiar with the retail automotive industry prior to making important classification decisions that may result in significant liability if handled improperly.

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