

IOWA DEPARTMENT OF INSPECTIONS AND APPEALS
DIVISION OF ADMINISTRATIVE HEARINGS
Wallace State Office Building
DES MOINES IOWA 50319

Appeal Number: 11IWD008

Respondent (4)

DECISION OF THE ADMINISTRATIVE LAW JUDGE

This Decision Shall Become Final, as of the date of mailing stated below unless:

**BUNGO CONSTRUCTION
CLARENCE BAILEY
1903 190TH STREET
PROMISE CITY, IA 52583-8711**

1. Either party files a WRITTEN application for a rehearing WITHIN TWENTY (20) DAYS AFTER the date below. The written application must state the specific reasons for the rehearing and the relief sought. If the request for a rehearing is denied or if the rehearing decision is not satisfactory, either party may petition the District Court WITHIN THIRTY (30) DAYS of either action;
OR

**IOWA WORKFORCE DEVELOPMENT
MATT MARDESEN
1000 EAST GRAND AVENUE
DES MOINES, IA 50319**

2. Either party may petition the District Court WITHIN THIRTY (30) DAYS after the date below.

YOU DO HAVE THE RIGHT TO HIRE A LAWYER at your own expense to represent you in these proceedings.

JASON TRYON, IWD
JOSEPH BERVID, IWD
NICHOLAS OLIVENCIA, IWD
RYAN DOSTAL, IWD
VERLE NORRIS, ATTY

(Administrative Law Judge)

June 15, 2012

(Decision Dated & Mailed)

STATEMENT OF THE CASE

Bungo Construction filed an appeal of two decisions issued by Iowa Workforce Development (the Department), both dated December 16, 2010. In one decision, the Department determined that an employer-employee relationship existed between the appellant and its workers from 2005 through 2010. In the other decision, the Department found the appellant liable for unemployment insurance contributions effective January 10, 2005.

The case was transmitted from Workforce Development to the Department of Inspections and Appeals on August 1, 2011 to schedule a contested case hearing. A hearing regarding the timeliness of the appeal was held on October 25, 2011. After a decision was issued finding the appeal was filed timely, a telephone hearing was scheduled regarding the merits of the appeal. The hearing was initially scheduled for December 15, 2011, but was continued at the Appellant's request. The hearing was held on February 13, 2012 before Administrative Law Judge Laura Lockard at the Wallace State Office Building in Des Moines, Iowa. The Department was represented by Matt Mardesen, investigations and recovery manager, who presented testimony. The

Appellant was represented by attorney Verle Norris. Charles Bailey, Jeff Wells, George Bailey, and Paul Bailey testified for the Appellant. The Department submitted Exhibit B, pp. 1-523, which was admitted into the record as evidence. The Appellant submitted Exhibits 1 – 3 and 5 – 7, which were admitted into the record as evidence.

ISSUE

Whether the Department correctly determined that an employer/employee relationship existed between Bungo Construction and the individuals performing services for the business between 2005 and 2010.

FINDINGS OF FACT

A. The Department's Investigation

On approximately February 5, 2010, the Department initiated an investigation of Bungo Construction relative to its status as a potential employer in the state of Iowa. The investigation was initiated after George Bailey and Paul Bailey, sons of the owner of Bungo Construction, Clarence Bailey, filed applications with the Department for contractor registration numbers.

Investigator Matt Mardesen contacted both George and Paul¹ separately on February 5, 2010. Mardesen spoke with each of them for approximately five minutes. George reported to Mardesen that he is a subcontractor for his father's company, Bungo Construction, and is paid by the hour. Paul also reported to Mardesen that Bungo pays him by the hour. Paul reported having worked for Bungo Construction for approximately eight years. Paul reported that Clarence's three sons all work for Bungo. (Mardesen testimony; Exh. A, p. 20). Clarence's third son is Charles Bailey; neither Mardesen nor any other representative of the Department attempted to contact Charles during the course of the investigation. (Mardesen testimony).

Mardesen spoke by phone with Clarence Bailey on March 1, 2010. During that call, Clarence reported that his sons are subcontractors rather than employees. The Department requested at that point that Bungo Construction complete a Report to Determine Liability and a Questionnaire for Determining Status of Workers. (Exh. A, p. 20).

In March, 2010, Mardesen spoke with Stephanie Mendenhall, CPA for Bungo Construction. Mendenhall reported that Bungo Construction does not issue any form 1099s. Mendenhall also stated that Clarence's sons were not employees of the business, but rather a family that all works together. The Department requested that Bungo produce 1099s that it had issued to any workers from 2005 to present; none were ever produced. (Exh. A, p. 21).

The Department reviewed checks and deposit slips that Clarence provided from a bank

¹ Clarence Bailey, George Bailey, Paul Bailey, and Charles Bailey will be referenced in this decision by first name to avoid confusion.

account held in the name of J&B Farms/Clarence or Joan Bailey. On a deposit slip dated May 1, 2009, there was a deduction in the amount of \$2,691 with the notation "Less Kids & Justin Payroll." On a May 13, 2009 deposit slip there was an indication that funds were issued to "Less workers" in the amount of \$3,118. On a September 14, 2009 deposit slip, there was a deduction for "Less Boys" in the amount of \$3,050. On a June 10, 2009 deposit slip, there was a deduction for "Less employees" in the amount of \$3,625. (Exh. B, pp. 21, 180, 184, 202). The majority of the checks written to George, Paul, and Charles on the account during the time period investigated had "pay" written in the memo line. A handful had "wages" or "payroll" written in the memo line. (Mardesen testimony; Exh. B, pp. 177, 232, 412). Clarence issued checks to his sons periodically, but the Department was not able to determine that they were paid on a set day or date, such as weekly, bi-weekly, or monthly. The checks were typically issued between seven and 14 days apart, but there was no consistent pay schedule. (Mardesen testimony).

Clarence testified at hearing that he did not make the notations on the deposit slips that the Department reviewed; typically, the bank teller would make the notation after he instructed how the teller regarding how much money was to be deposited from his check into each of his son's accounts. (Clarence Bailey testimony).

In June, 2010, Bungo Construction completed a Questionnaire for Determining Status of Workers. The questionnaire relates to services performed by Clarence's three sons. In the Questionnaire, Bungo reports that the workers are required to perform services personally and are engaged for a specific job. Workers' hours vary from day to day and month to month. Additionally, it is reported that Clarence's sons work on projects other than Bungo projects, both separately and together. With respect to how the workers are paid, the questionnaire indicates that they are paid either a piece work rate or a lump sum, depending upon the job. (Exh. A, p. 34).

In the Questionnaire, Bungo reports that the workers are paid by the customer and that the sons determine what to charge for their services. (Exh. A, p. 34). In a conversation with Mardesen, however, Clarence reported that he once had to sell some calves from his farm to pay his sons when a customer had not paid for a job that was completed. Clarence sold the calves and absorbed the loss in order for his sons to get paid for the job. (Mardesen testimony).

Bungo reports that equipment, supplies and tools are provided by both the business and the worker, but that each worker supplies his own vehicle. In response to a question about what financial risk or economic loss the worker can incur, Bungo indicated "nonpayment on job" and "theft/damage to tools." (Exh. A, p. 34).

Under the heading Relationship Between Firm and Worker, Bungo reported that the business does not have the right to direct and control the manner in which the services are performed. Additionally, Bungo reported that it does not have priority on the worker's services. Bungo wrote that Clarence and the sons work together and "everyone supervises." With respect to discharge, Bungo reported that it does not have the right to discharge the workers at any time, but that the worker may terminate services at any time without incurring liability or penalty. Additionally, Bungo reported that Clarence's

sons have separate construction jobs. (Exh. A, p. 35). In a conversation with Mardesen during the investigation, Clarence indicated that he functions as the quality control person, making sure everything gets done to the customer's specifications. (Mardesen testimony).

After reviewing information provided by Mr. Bailey and other information obtained during the course of the investigation, the Department issued a Notice of Employer Status and Liability to Bungo Construction on December 16, 2010. The notice advised the Appellant that the Department had determined that an employer-employee relationship existed between Bungo Construction and the individuals performing services for the business during the years 2005 through 2010. The notice further advised Bungo Construction that compensation for 2005 through 2010 was being reported for unemployment purposes. (Exh. B, pp. 13-14).

Also on December 16, 2010, the Department issued another decision to Clarence Bailey. This decision advised Clarence that he was liable for unemployment insurance contributions effective January 10, 2005. The decision listed the contribution rate applicable for the years 2005 through 2010. (Exh. B, pp. 11-12). Bungo Construction appealed the decisions. (Exh. B, p. 9).

B. Bungo Construction's Organization and Business Practices

1. *Charles Bailey, Paul Bailey, George Bailey*

Bungo Construction is a sole proprietorship owned and operated by Clarence Bailey. Bungo is primarily engaged in residential construction and remodeling. Clarence's sons, Charles, Paul, and George, are 29, 28, and 26 years old, respectively. Each has performed services for Bungo Construction during the years between 2005 and 2010. (Exh. B, pp. 15-18; 22; 37-84; Charles Bailey; Paul Bailey testimony).

Charles Bailey has been licensed as a master plumber since 2009 and has done plumbing work off and on since he was 16 years old. During the time period in question, he took plumbing jobs apart from his work with Bungo. He got jobs mainly through word of mouth and through referrals from Jeff Wells, an outside salesperson, and other employees of Lockridge, Inc., a hardware supply store. (Charles Bailey testimony). Wells testified that he referred approximately six to 12 small jobs per month to Charles. (Wells testimony).

Charles owns most of the tools he requires to do plumbing jobs. He occasionally uses a skid steer that Bungo owns if it is necessary for a plumbing job. (Charles Bailey testimony). Charles testified that, while he did use Bungo tools at times if he did not have a particular tool that a job called for, if the tool was damaged he had to repair or replace the tool. This occurred one time with a saw that he borrowed from Bungo. (Charles Bailey testimony).

Charles dealt with all of the responsibilities related to plumbing when Bungo bid a job, including talking to the customers about the layout and ordering the

supplies and fixtures necessary for the job. Clarence would give his opinion regarding the plumbing aspects of a job, but he and Charles disagreed at times and Charles was not obliged to follow Clarence's suggestions. (Charles Bailey testimony).

On a typical day, Charles decided which project he would work on that day based upon the respective customers' needs. (Charles Bailey testimony).

George Bailey specializes in wiring and had had his electrician's license since 2008 or 2009. Additionally, he works as a general contractor doing remodeling, wiring and installation of overhead doors, windows, screens, and roofs. (George Bailey testimony). George owns a bucket truck that he uses for electrical work. (Wells testimony).

George was responsible for working up the bid for the electrical portion of jobs for which Bungo provided estimates. Much like Charles, George attempted to determine how much time the job would take and made the bid based on the time it would take to complete the job. George also did the ordering of materials for the electrical portion of Bungo jobs. (George Bailey testimony).

Like Charles, George also did jobs – specifically wiring projects – that were separate from his work for Bungo. He was typically juggling Bungo and non-Bungo projects at the same time. He would make the determination regarding which project to work on each day based upon which project was the farthest behind or the most important. While Clarence did not direct where George worked each day, George would coordinate with Clarence with respect to scheduling the electrical work he was obligated to complete for Bungo. (George Bailey testimony).

Charles also testified that he occasionally did framing or drywalling on a Bungo job. He testified that he did whatever was needed and was paid a set hourly rate for that type of work. Charles testified that if Bungo was framing an entire house, Clarence would have all his sons there to help with the work. (Charles Bailey testimony). George confirmed that he, too, occasionally assisted with work on Bungo projects that was not directly related to wiring; he occasionally helped with framing, siding, windows, and roofing on Bungo projects. (George Bailey testimony).

Paul Bailey has been involved in construction since 2002. When he worked on jobs for Bungo, he was typically in charge of insulation, flooring, doors and windows, trim, keeping the job site tidy, and any finishing touches that were required. Like his brothers, he worked up the portion of the bid that dealt with these items on Bungo jobs. (Paul Bailey testimony).

Paul was also responsible for ordering the supplies for the parts of the job that he was in charge of. He had most of the tools necessary to complete the work he was responsible for, including a circular saw, drills, an air compressor, a caulk gun, and other staple tools like a hammer and a level. (Paul Bailey testimony).

Occasionally Paul needed Charles or George to assist him with some aspect of a Bungo job that he had bid; he typically figured those hours into the bid and he took responsibility for paying Charles or George to assist in those tasks. As with his brothers, Paul took ultimate responsibility for determining how his parts of the job were to be completed. Clarence did not dictate the manner and method of completion. (Paul Bailey testimony).

After Bungo bid a job, each of the Bailey sons was responsible for fulfilling the parts of the job for which he prepared the bid. If he was able to complete the work within the bid schedule (i.e. if a job that he estimated at 400 hours was done in 400 hours or less), the job was financially advantageous. If, however, the work that he agreed to took longer than the amount of time reflected in the bid, there was no extra compensation for that time; for example, if a 400 hour job took 450 hours, the extra time worked was uncompensated and the job would represent a financial loss. (Charles Bailey testimony).

Bungo paid Charles, George, and Paul on a draw schedule. Every week or so, Bungo would deposit money into their accounts relative to the portion of the job that they had completed. If one of Clarence's sons was working on a side job for a period of time, he would stop being paid by Bungo as he was no longer completing work for the business. Charles was the person who kept track of the hours that everyone worked for Bungo. (George Bailey; Clarence Bailey testimony).

Additionally, if there was a problem with the work undertaken by one of the sons, he was responsible to fix the problem without additional compensation. For example, Charles worked on a house for Bungo where he did not put a compression valve on tight enough, which led to water damage to the walls. Charles fixed the problem and repaired the damage at his own expense. (Charles Bailey testimony).

Charles, George, and Paul all had commercial general liability coverage independent of Bungo during at least part of the time in question. Charles, d/b/a Charlie Bailey Construction, had general liability coverage from 2002 through 2003, then from 2004 through 2011. George had general liability coverage from 2007 through 2012. Paul, d/b/a Paul Bailey Construction, had general liability coverage from 2005 through at least 2008. (Exh. 5, 6, 7).

2. *Justin Trower*

The bank records that the Department reviewed showed that Justin Trower was paid out of Clarence's account during 2008 and 2009. He was paid \$1,079 in the third quarter of 2009; \$1,615 in the second quarter of 2009; \$1,778 in the first quarter of 2009; \$2,226 in the fourth quarter of 2008; and \$2,062 in the third quarter of 2008. (Exh. B, pp. 48, 50, 52, 54, 56). The checks that were issued to Justin were issued on the same dates that Clarence paid Charles, George, and Paul. During the investigation, Clarence told Mardesen that he had hired Trower to do fence work for him. (Mardesen testimony).

REASONING AND CONCLUSIONS OF LAW

A. Overview

For purposes of unemployment compensation, an “employer” is defined as an employing unit that, in any calendar quarter in the current or preceding calendar year, paid wages of \$1,500 or more, or employed at least one individual for some portion of a day in each of twenty different calendar weeks during the current or preceding calendar year.² “Employment” is defined as service performed for wages or under any contract of hire, written or oral, express or implied.³ When an employer claims that any employment is not employment under the Iowa Employment Security Law, the burden is on the employer to prove the exemption claimed.⁴

In the unemployment compensation context, it is well-settled that “the right to control the manner and means of performance is the principal test in determining whether a worker is an employee or independent contractor.”⁵

The relationship of employer and employee exists when the person for whom services are performed has the right to control and direct the individual who performs the services, not only as to the result to be accomplished by the work but also as to the details and means by which that result is accomplished. An employee is subject to the will and control of the employer not only as to what shall be done but how it shall be done. It is not necessary that the employer actually direct or control the manner in which the services are performed; it is sufficient if the employer has the right to do so.⁶

The Department’s regulations set out in some detail the factors to be considered in determining whether a worker is an employee or an independent contractor.⁷ Factors that support the existence of an employer-employee relationship include:

- Right to discharge an employee without being held liable for damages for breach of contract;
- Furnishing of tools, equipment, material, and a place to work;
- Continuous performance of work for the employer;
- Payment of a fixed wage on a weekly or hourly basis.

Factors that support an independent contractor relationship include:

- Performance of a specific job at a fixed price;

² Iowa Code § 96.19(16)(a) (2009).

³ Iowa Code § 96.19(18)(a) (2009).

⁴ 871 Iowa Administrative Code (IAC) 22.7(3), 23.55(2).

⁵ *Gaffney v. Department of Employment Services*, 540 N.W.2d 430, 434 (Iowa 1995).

⁶ 871 IAC 23.19(1).

⁷ See generally 871 IAC 23.19.

- Following a distinct trade, occupation, business, or profession in which an individual offers services to the public to be performed without the control of those seeking the benefit of his or her training or experience;
- Unreimbursed expenses and fixed, ongoing costs regardless of whether work is currently being performed;
- Significant investment in real or personal property that is used in performing services for someone else;
- Right to employ assistants with the exclusive right to supervise their activity and completely delegate the work.⁸

The regulations also provide that if, upon examination of the facts of a case, an employer-employee relationship exists, the designation or description by the parties of their relationship as anything other than an employer and employee is immaterial.⁹

B. Charles Bailey, Paul Bailey, George Bailey

The evidence presented here demonstrates that Charles Bailey, Paul Bailey, and George Bailey were not employees of Bungo Construction during the time period in question. I found the testimony of each of them, as well as the testimony of Clarence Bailey, credible as to the nature of the working relationship. The sons essentially functioned as independent contractors, with each specializing in a different aspect of the job. Each of the sons was responsible for his area of expertise, from working up the bid to ordering materials to completion of the task. Typically, they provided the tools necessary to complete the work. If they borrowed a tool from Bungo and the tool was lost or broken, they were responsible for repair or replacement.

One of the key elements that demonstrates that Clarence's sons were independent contractors is the financial risk they faced on Bungo jobs. While an employee is typically paid an hourly wage for all of the hours that he or she works on a particular job, this was not the case for Clarence, Paul, or George. Once the bid was completed, each of them was paid only the bid amount – no more and no less – for the work on their particular area of expertise. Consequently, if they underestimated the hours that a particular job would take – working, for example, 100 hours instead of the 75 estimated – their profit on the job would drop. Conversely, if they finished the job quicker than expected their profit would rise in relation to time expended.

The Department argued at hearing that the fact that Bungo paid George, Paul, and Charles before the business was paid by the customer means that Clarence's sons incurred no financial risk in the jobs that they did for Bungo. The Department's argument here is incorrect. Subcontractors incur financial risk in a variety of ways; for example, if a subcontractor inadvertently underbids a job, this has a significant impact on the bottom line since the subcontractor is paid only the bid amount even if he or she underestimated the time necessary to complete the job. Since the subcontractors are typically in a contractual relationship with the general contractor, not the customer directly, the fact that Bungo paid Clarence's sons before the customer paid for a job does

⁸ 871 IAC 23.19.

⁹ 871 IAC 23.19(7).

not tip the scales in favor of an employer/employee relationship.

Additionally, the fact that Clarence was responsible for quality control and making sure that the customer's needs were met does not necessarily indicate that there was an employer/employee relationship. The fact that the general contractor oversees the quality of the final product does not necessarily mean that he oversees the manner and methods by which the workers create that final product. In this case, each of Clarence's sons had a particular specialty and each one was responsible for determining how best to complete the part of the job that he was responsible for. In one case, Charles completed a job with a defect in craftsmanship that resulted in water damage to the property. Charles was responsible for remedying the damage and making the customer whole. This points to an independent contractor, rather than employer/employee, relationship.

Another key element in finding that Charles, Paul, and George were independent contractors is the fact that each of them worked independently of Bungo during the time period in question in their particular area of expertise. They received referrals from employees at the local hardware store and got business through word of mouth. Each carried his own commercial liability coverage at the same time that he was completing jobs for Bungo. They decided which job they would work on on any particular day, taking into account the needs of Bungo's customers as well as their own.

Under these circumstances, the Department's decision finding Charles Bailey, Paul Bailey, and George Bailey to be employees of Bungo Construction from 2005 to 2010 was incorrect.

C. Justin Trower

As noted above, it is the employer's burden to prove that employment is exempt under the Employment Security Law. The only evidence regarding Justin Trower demonstrates that he was paid by Bungo in five consecutive quarters during 2008 and 2009 and that he was paid to do "fence work" for the business. Bungo presented no further details regarding the nature of the relationship. Under these circumstances, Bungo has failed to meet its burden of proving that Trower's employment was exempt. The Department's decision finding Trower an employee of Bungo was correct.

DECISION

The Department's decision is **AFFIRMED IN PART** and **REVERSED IN PART**. Charles Bailey, Paul Bailey, and George Bailey were not employees of Bungo Construction from 2005 through 2010. Justin Trower was an employee of Bungo Construction during that time period. The Department shall take any action necessary to implement this decision.

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