EXHIBIT 5
DATE 3·10·05
SB 108

Independent Contractor Exemptions
A Final Report on Senate Bill 270

EXECUTIVE SUMMARY

Since 1984 the Department of Labor and Industry has been issuing independent contractor (IC) exemptions. Over time, many changes have occurred both legislatively and procedurally to the exemption process. Until very recently, the exemptions have been held by the Workers' Compensation Court to be conclusive as to the status of an independent contractor. The Montana Supreme Court in Kelly Wild v. Fregein Construction threw out the conclusive nature of the exemptions in 2003. In this decision, the Court found that the exemptions were not conclusive. The court said an employer must make an initial good faith inquiry to determine the worker meets the control and independently established business tests before employing the worker as an IC.

With the Wild case disrupting the original legislative intent of the exemption process, the 59th legislature passed SB 270. The bill required the Department of Labor and Industry to establish a committee to study and make recommendations regarding the issues relating to independent contractors.

The question of whether an individual is an independent contractor or an employee is a complex one that is driven by the facts in each individual case. An independent contractor is defined in Montana law as "one who renders service in the course of an occupation and (a) has been and will continue to be free from control or direction over the performance of the services, both under contract and fact; and (b) is engaged in an independently established trade, occupation, profession or business". This is commonly referred to as the AB test.

As part of its deliberation, the SB 270 independent contractor study committee recognized that there is a real need for processes that ensure a degree of certainty in determining whether the working relationship is one of employer to employee, or hiring agent to independent contractor. The committee further agreed that whatever the outcome, there is a need for all parties to fully understand their respective rights and responsibilities under the law, and under contract. To the extent the Department of Labor and Industry can facilitate this understanding and bring some certainty to the relationship it should do so. The recommendations summarized in this report endeavor to assist the department and the legislature in accomplishing those objectives.

In reaching its recommendations, and ultimately a legislative proposal to carry out its recommendations, the committee relied on a variety of data and input. This included a report commissioned by the Department of Labor and Industry and prepared by Hays Companies of Minneapolis Minnesota. The report titled "Independent Contractor Best Practices" formed the basis for much of the initial discussion. Among data in the report was information indicating that Montana has the highest percentage of independent contractors (8%) as a percentage of the total workforce than any other state that registers

- **The department should provide education to independent contractors, hiring agents, and employees as to their rights and responsibilities.** The committee believes that because this area of the law is so complex and because there are so many situations that could be prevented before they happen, an education program is a vital component in bringing needed stability to this area of the law. The committee believes that a designated portion of the registration fee needs to be specifically allocated for this purpose. As part of the education process the Department should provide a sample contract that could be used by the contracting parties to define the independent relationship.

- **The cost of the exemption should be increased in order to support enhanced enforcement and education efforts.** The committee believes that the current charge for exemption is so minimal that it could not begin to support the recommended changes. An increase, determined through administrative rule, and with the necessary legislative guidance, would be a small price to pay to bring stability, certainty, and fairness to the business and worker community.

- **The legislature should provide penalties for violations of law consistent with the recommendations of this committee.** The committee believes that in addition to meaningful exemption review and investigative capabilities, the department needs the ability to assess fines against those hiring agents and independent contractors who abuse the exemption process.

- **To the extent possible, the department should implement objective standards – a point system – a soon as practical to assist in determining whether applicants are engaged in independently established businesses.** Ultimately the committee recognized that the traditional AB test needed to remain a part of the statute. The committee also recognized that of those two prongs, the B portion is the easier to evaluate and measure. An objective point system known to applicants and the Department alike, will meaningfully measure if applicants are truly engaged in an independently establish business. This will leave the Department with the ability to concentrate its resources on education and enforcement efforts, with a focus on those who are not registered and providing information on what it means to be free from direction and control, the A prong of the exemption criteria.

The SB 270 Study Committee presented these recommendations and draft proposed legislation to the Economic Affairs Interim Committee on September 7, 2004. Members of the Study Committee testified in support of the proposed legislation as a means of addressing the issues regarding independent contractors. Following discussion of the recommendations, the Economic Affairs Interim Committee unanimously approved the motion to adopt the SB 270 Study Committee draft proposed legislation as an EAIC committee bill.