BC EST #D337/98

EMPLOYMENT STANDARDS TRIBUNAL
In the matter of an appeal pursuant to Section 112 of the
Employment Standards Act R.S.B.C. 1996, C. 113

- by -

3717 Investments Ltd. operating Student Works Painting
("Student Works Painting")

- of a Determination issued by -

The Director Of Employment Standards
(the "Director")

ADJUDICATOR:	John L. McConchie
FILE NO.:	98/104
DATE OF HEARING:	April 27, 1998
DATE OF DECISION:	July 29, 1998

DECISION

APPEARANCES

Andrew Britnell for 3717 Investments Ltd. operating Student Works Painting

Adelle Adamic for the Director of Employment Standards

OVERVIEW

This is an appeal under Section 112 of the *Employment Standards Act* (the "*Act*") by 3717 Investments Ltd. operating as Student Works Painting ("Student Works Painting" or the "Company") against a Determination which was issued on January 27,1998 by a delegate of the Director of Employment Standards in favour of Jason Black, Stephen Lam and Juan Lefno. The Director's delegate determined that Student Works Painting had contravened Sections 18 and 58 of the *Act* and was required to pay the following sums:

Jason Black	**$350.52**
Stephen Lam	**$270.23**
Juan Lefno	**$261.96**

An individual called Kaleki Lloydd employed the three complainants to work as house painters. Although Lloyd's business card identified her as being a "manager" of Student Works Painting, she was a franchisee of that Company operating under a complex agreement called an Owner-Operator Agreement (the "Agreement"). The Director's delegate was called on to determine which of two entities was the actual employer of the three complainants: Student Works Painting or Kaleki Lloyd Painting. That question, said the Delegate, was to be determined by deciding whether Kaleki Lloyd was herself an employee of Student Works Painting. If she was an employee of that company, then the employees hired by her could as well look to Student Works Painting as being their true employer. When Kaleki Lloyd Painting failed to pay wages to the three painters, they filed complaints alleging that their employer was Student Works Painting. After reviewing the various legal tests for determining the true employer, the Director's delegate concluded that the true employer was in fact Student Works Painting.

Student Works Painting appeals the Delegate's decision, submitting that Kaleki Lloyd Painting was the true employer.

A hearing was held in Vancouver, B.C. on April 27, 1998 at which time evidence was given under oath or affirmation by Andrew Britnell, the President and owner of Student Works Painting, and Yuki Chippendale, a former painter and now franchisee of Student Works Painting. The complainants did not attend the hearing, and no evidence was adduced on their behalf.

ISSUE TO BE DECIDED

The issue in this case is whether Student Works Painting is the employer of the complainants and thus responsible for their unpaid wages.

FACTS

Andrew Britnell, President and owner of Student Works Painting, testified about the nature of the Company's arrangements with its franchisees. He testified that the company typically grants house painting franchises to about 65 students in western Canada. The franchisees are responsible for every aspect of the business from recruiting through hiring and paying their own staff. Overall, about 300 to 400 people become employed through the franchisees every year in British Columbia. The biggest franchisee might have as many as 12 or 13 students working for it.

Kaleki Lloyd was a franchisee like any other, he said. Student Works Painting operates a computerized payroll service for the franchisees, and so comes to learn about the franchisee's employees for that purpose. However, Lloyd hired her own employees and Student Works Painting had no say in their selection. As the exhibits demonstrated, the complainants Black and Lam signed Painter Payroll Information Forms in which they specifically agreed that they were working for the franchisee (called a Branch Operator on the Payroll Form). Their T4 income tax records were issued by Kaleki Lloydd Painting. Student Works Painting had no record at all of **Juan Lefno**, as no request was ever made by Kaleki Lloydd to have him put on her payroll. Kaleki Lloydd had her own business number with Revenue Canada for the purposes of payroll deductions. The legal status of Kaleki Lloydd is described in the business number information as "sole proprietorship".

Mr. Britnell identified the Agreement which had been entered into with Kaleki Lloydd and explained its provisions. The Agreement purports to grant an exclusive license for residential painting and for the use of the Trade Marks of the Company to the Operator for the territory of Coquitlam for a term which expired on December 31, 1997. The Agreement specifies that it does not create an employer/employee relationship, that the Operator is an independent contractor and that the Operator is solely responsible for the wages of his or her employees, paint bills and all other liabilities incurred through the business (Clause 31). The Operator agrees to devote his or her full time efforts to the business, to perform duties without absences and not to engage in any other business or activity that may interfere with the success of the business (Clause 6).

The Agreement stipulates that the Operator must attend and satisfactorily complete one weekend training seminar, along with other training seminars as requested by the Company. The Company loans study manuals to the Operator (Clause 3). The Agreement also requires that the Company provide intensive seminars covering recruiting, paint technology, estimating, marketing, professional selling skills, production management, training and motivating employees; and accounting for small business. Additionally, the Company makes staff available to the Operator for consultation and advice on operational aspects of business (Clause 21). For a first time Operator, the Company provides a District Manager to work with, and be responsible for, the Operator (Clause 25). The Company also provides the Operator with business forms for customer contracts, estimate forms, daily planner, scheduling forms and job planners (Clause 22). The Operator is issued 150 client contracts and is responsible for returning all 150 contracts, with a $50 charge per missing client contract levied by the Company to reflect the cost of auditing contracts. (Clause 13)

Advertising materials, such as flyers, lawn signs, vehicle signs, business signs and telephone pole flyers are provided to the Operator by the Company. The Company arranges for the Operator to participate in local home and trade shows, and pays up to $50 towards the cost of such participation, with the balance being paid by the Operator. The Operator's municipal business license may be obtained by either the Company or the Operator, but is paid for by the Operator (Clause 23). All job sites and vehicles used by the Operator must be identified with signage approved by the Company and the Operator's painters must wear shirts specified by the Company (Clause 14).

The Operator is required to make mandatory weekly telephone reports to the Company (Clause 15) and to maintain records, accounts and status of all business activities in compliance with the standard procedures prescribed by the Company (Clause 16). The Operator is also required to submit records and information to the Company as to the services sold, facilities maintained, methods of operation employed, personnel employed by the Operator, daily planner, quotes, job sheets, material and procedures as the Company may request. The Company has the right to communicate freely with employees of the Operator (Clause 16). The Operator agrees to comply with any laws with respect to the collection and remittance of federal and provincial taxes and to fully co-operate with the Company in abiding by taxation regulations (Clause 6).

The Operator agrees to appoint the Company to establish a line of credit to $5000 with a major supplier, to enable the Operator to obtain supplies as required. The Company also negotiates terms of supply and payment with suppliers on behalf of the Operator. The Operator is responsible for any payment for supplies, with the Company having the right to collect any outstanding payments from the Operator,

including the right to set off against amounts payable by the Company (Clause 28). The Operator is responsible for providing a vehicle to carry out the business, is responsible for the insurance of the vehicle and must indemnify the Company against any loss or damage incurred by the Company as a result of operation of the vehicle (Clause 8).

The Agreement requires that the Operator obtain executed contracts for sales by specified dates. It also requires a minimum value of sales of $25,000 be achieved by the Operator and a schedule of Royalty payments must be paid to the Company, based on a percentage sliding scale which decreases as the value of the sales increase (as high as 26% on sales up to $35,000 to as low as 8% on all sales over $80,000). If the minimum production target is not met the Royalty percentage is 28% (Clauses 4 and 5). All customer payments are received by the Operator in trust for the Company and must be promptly forwarded to the Company. After deducting any "indebtedness" of the Operator to the Company (and maintaining a $1000 float balance with the Company), the gross profits are forwarded to the Operator (Clause 19).

The Company guarantees that the Operator will earn a minimum gross profit of $2,500, provided certain criteria are met with respect to completion of estimates and sales, continuous work and attendance and participation in a job site exercise. The Company pays the Operator additional specified sums of money when $45,000 in collected sales is reached and if the Operator signs a contract to return for the next season. The Company also pays the Operator 40% of deposits collected in the preseason as an advance on profit (Clause 5). The Operator is not permitted to carry out any work that the Company is in the business of providing, without paying royalties. The Operator must restrict its business to painting; must not operate outside of its assigned territory; must only provide guarantees within guidelines provided by the Company; and agrees to reimburse the Company for any damage incurred by the Company as a result of the Operator performing any other kind of work (e.g. carpentry) (Clause 6).

The Operator agrees to complete, with compensation, all warranty work arising in the territory to a maximum of 100 hours of labour and the Company agrees to pay for the cost of materials and the wages of the Operator's painters engaged in the warranty work. Any individual warranty work projects requiring more than six labour hours must be approved by the Company prior to the Operator commencing work. For warranty work in excess of 100 hours of labour, the Company and the Operator agree to negotiate the rates to be paid for such work. If the Operator fails to complete warranty work which is assigned prior to July 15, 1997, the Operator is required to pay the Company a fee of $500 to enable the Company to pay for an alternate to perform the work (Clause 7).

The Company, at its expense, provides computerized payroll services, accounting, bank relations services, makes arrangements for Workers Compensation for the Operator's employees and offers a three year warranty to the Operator's customers. The Company also provides, for a fee, telephone answering services for the Operator (Clause 24). With respect to the warranty, the Company retains $500 in the account of the Operator until July 1998 to pay for any warranty work costs which are deemed by the Company to be caused by poor workmanship (Clause 29).

Public liability and property damage insurance is maintained by the Company with a deductible of $5000 per claim. The Operator is obliged to pay 15% of the deductible amount per insured claim. The insurance does not cover spray painting and the Operator is personally liable for any such damage (Clause 17).

The Company either owns or has the right to use the Trade Marks and the Operator is only allowed to use the Trade Marks as necessary to conduct business during the term of the Agreement (Clause 9). The Operator is bound by confidentiality and non-competition provisions contained in the Agreement (Clauses 10 and 11).

Either the Company or the Operator can terminate the Agreement. The Company may terminate it at any time and on five days notice in the event of any uncured default by the Operator. If the Agreement is terminated by the Company for non-fulfillment of the minimum sales requirement (except if caused by severe illness), the Operator must pay the Company $3,500 in liquidated damages for lost royalties (Clause 26). The Company is also entitled to injunctive relief if the Operator breaches the terms of confidentiality and non-competition contained in the Agreement (Clause 12).

The Operator can terminate the Agreement on ten days notice but must pay the Company an amount in "liquidated damages" for doing so. The amount of those damages varies depending on the availability of a suitable replacement (Clause 27). The Operator also agrees to indemnify the Company for any losses or liabilities suffered by the Company as a result of the failure of the Operator to comply with the terms of the Agreement (Clause 20).

The Agreement also specifically provides that the Operator is solely responsible for the wages of his or her employees (Clause 31), although the Company provides, at its expense, computerized payroll services and makes the arrangements for Workers' Compensation for all employees of the Operator (Clause 24). The Company is also entitled to receive, at its request, information from the Operator with respect to personnel employed by the Operator (Clause 16). The Company agrees to pay the wages of the Operator's employees engaged in warranty work (Clause 7). All painters employed by the Operator must wear shirts specified by the Company (Clause 14).

The upshot of the arrangement, said Mr. Britnell, is that Student Works Painting provides a very good opportunity for students to operate as entrepreneurs during the summers. As I understood Mr. Britnell's evidence, the Agreement attempts to ensure that the franchisee is able to take advantage of his/her exclusive rights to a territory in the interests of both the Company and the franchisee. The franchisee is entitled to and does receive training, advice, accounting and payroll services, and ongoing business advice on request. This is necessary because the franchisees are students who often do not have much business experience. This may be their first true business experience, and the Company's systems maximize their opportunities to make it a success. Through the Agreement, the Company also maintains quality control, which is an essential characteristic of any franchise arrangement.

The franchisees typically take advantage of the Agreement's provisions as they see fit. For example, the Company supplies forms to the franchisees but they are entitled to use their own if they prefer. The operators buy all of their own equipment. The company provides marketing material, but the franchisees use their own methods of advertising as well. The price for a particular painting job is established by the operator, using estimating standards developed by the Company. The profit that the franchisee is able to generate depends on his or her abilities, energies and commitment. The commission structure in the Agreement establishes that it is the Company, not the franchisee, who gets a commission on sales. The more successful the franchisee becomes, the more profit the franchisee is able to keep for himself or herself.

Yuki Chippendale also testified for the Company. The purpose of her testimony was to establish how a franchisee's operation worked on a day to day basis. She testified that she began as a painter for a franchisee. She was interviewed and hired by the franchisee, from whom she received her daily direction. She also signed the Information Sheet on which she agreed that she was an employee of the franchisee. If she had a problem on a job or was out of paint, she would deal with the franchisee, not Student Works Painting.

She testified that when she became a franchisee herself, she did not consider herself to be an employee of the franchise operator. She testified that she understood the risks of being a franchisee when she signed her Owner-Operator Agreement. She "knew what [she] was getting into". There may not be enough business. She may have difficulty finding good painters. She might not make much money. As it turned out, she worked hard, did good estimates, booked the business and fulfilled her contracts with the painters she hired. She recruited her painters by placing advertisements at colleges and high schools, and other such places. She interviewed candidates and hired those of her choice. No Student Works Painting employee ever participated in the interviews or hiring process. Nor did the Company involve itself in controlling or terminating the painters. The obligation to pay the painters, she said, was her own.

She testified about the business realities of being a franchisee. There were start-up costs, including the need for good transportation, insurance and equipment. In her view, Student Works Painting exercised "no control" over her on a day to day basis. Although the Company certainly had its guidelines, she did not necessarily follow them. She was a successful franchisee nonetheless. When she did her taxes, she

identified her employee costs as a deduction, as any business would. She did not receive a T4 record from Student Works Painting as she was not employed by that Company. She testified that at one point she employed seven painters and marketers. The marketers, two high school students, conducted cold-calls after school in the neighbourhoods in her territory.

Oral Submissions

Student Works Painting argued that the relationship between the Company and the franchisees was not an employer-employee relationship. Similarly, the painters, who are the actual complainants in this case, clearly were engaged by the franchisee and not by the Company. The Company never even meets the painters. All of the indicia point to an employer-employee relationship between the franchisee and its own employees.

The Company agreed that the Owner-Operator Agreement reveals a degree of control, but argues that it does not amount to the kind of control which is required to find the existence of an employer-employee relationship. Although the systems and guidelines are expressed in mandatory terms, the reality is that the franchisees run their own show. Based on its experience, the Company had a very good idea of what it takes to make a successful business venture, and encourages the use of its forms and procedures, but it has "very little if any control" over the franchisee. The fact is that the franchisee is an entrepreneur and will be successful or not depending on their own initiative.

The Company went through the Determination and the reasons contained therein and sought to rebut the legal conclusions reached by the Director's Delegate. Mr. Britnell argued that the telling point of this case is that the Company had no idea whether or not the monetary claims being made by the complainants were accurate. It did not hire them, had never met them, and did not assign them work. To this day, it did not know if complainant Lefno had even worked for Kaleki Lloydd. In summary, the Company argued that becoming a franchisee for Student Works Painting was an "unbelievable entrepreneurial experience". To find that the franchisees and their employees were all employees of Student Works Painting would completely alter the nature of the business relationship and jeopardize jobs. Having said this, in order to safeguard against this kind of thing happening again, the Company was now starting a program whereby franchisees would be charged a 1% burden on their labour in order to ensure that funds were available to compensate franchisee employees in cases such as this.

Counsel for the Director argued that the franchisees were employees, and by extension, the employees of the franchisees were all employees of Student Works Painting. She pointed to the definition of "employee" of section 1 (1) of the Act and observed that it is an inclusive definition. The Delegate's Reasons identified the whole of the relationship between the parties and correctly concluded that Student Works Painting was the true employer. The fact that the relationship worked well for Ms. Chippendale is irrelevant. The evidence, said counsel, established that the real business was the business of Student Works Painting. Three-quarters of the franchisees do not return after the first year.

Counsel argued that the issue in this case was whether the operators were sufficiently dominated by the Company that it must be said that they were not carrying on the business on their own. The fact here is that painting is the essence of the Company's business. The Owner-Operator Agreement evidences the Company's concern for quality control, which is very important to the Company. It is so important that it provides a 3 year guarantee. Counsel submits that the lack of day to day control by the Company does not mean an absence of managerial control. The power of the control is evidenced in the Agreement, not in the day to day exercise of managerial control. Looking at the Agreement, she said, the question is: what scope is truly left for entrepreneurial activity by the franchises?

The only thing that the franchises really bring to the relationship is an automobile and their labour. While they may do some advertising on their own, they depend on the goodwill of Student Works Painting in order to secure business. It is true that if the franchisee does very well, he or she can make an income. This is not much different than the position of any employee who is paid on an incentive basis. Again, counsel submits that there is really nothing entrepreneurial about the franchisee's business.

The Director seeks as well a declaration that Kaleki Lloydd Painting and Student Works Painting are a single employer within the meaning of section 95 of the Act. Although the Determination does not mention this issue, counsel submitted that it is "there by implication." The employment standards purpose is to protect those who are dependent in their short-term employment on Student Works Painting. Dependency here is established by the Operator Agreement. Since it is the contractor who bears all of the risk in the relationship, it may not have the funds to pay its employees. The purpose of the Section 95 declaration is therefore remedial.

The Company replies that the majority of its operators do not return because they graduate from college or travel to Europe or other such things. As for what the franchisee brings to the relationship, for an 18 or 19 year old budding entrepreneur, risking $1500 or more on equipment and purchasing a vehicle is a major investment. However, the Company submitted, the investment pays off with hard work and good business practices. The average operator makes between $8,000 and $10,000 each summer. One operator, who had many employees, made $64,000 in one summer. Making money also involves controlling costs.

Mr. Britnell submitted that other companies, including the sprinkling franchisers, distance themselves by refusing to perform payroll services for the employees of the franchisees. Student Works Painting rejected this approach in favour of maintaining systems to ensure that people were paid. In the end, however, success in this venture for a franchisee comes down to a willingness to work hard to succeed. This is clearly an entrepreneurial experience for the students, he said.

ANALYSIS

True Employer Issue

The first issue to be decided in this case is whether the student painters are employees and, if so, by whom are they employed.

Section 1 of the *Act* contains the following definitions of employee and employer:

> "employee" includes
>
> (a) a person, including a deceased person, receiving or entitled to wages for work performed for another,
> (b) a person an employer allows, directly or indirectly, to perform work normally performed by an employee,
> (c) a person being trained by an employer for the employer's business,
> (d) a person on leave from an employer, and
> (e) a person who has a right of recall;
>
> "employer" includes a person
>
> (a) who has or had control or direction of an employee, or
> (b) who is or was responsible, directly or indirectly, for the employment of an employee.

The Tribunal has noted that these definitions do not set out an exhaustive list of all the circumstances under which a person will be seen to be an "employee" or an "employer". Thus, the *Act* allows for the application of common law principles to assist in making this determination: see *Re Pink Dot Enterprises Inc. (c.o.b. Pink Dot Delivery)*, BC EST #D039/98.

The question of whether a person is an employee is one that is based on an assessment of all elements of the relationship between the parties. In assessing this relationship the Tribunal has utilized several common law legal tests. Those tests include the "control test", the "four-factor test", the "integration test" (which is also known as the "organization test"), the "economic reality test" and the "specific result" test: see *Re Tennant (c.o.b. Anthony Robbins and Associates)*, B.C.E.S.T. #D302/97; *Re On-Line Film Services Inc.*, BC EST #D319/97; and *Re 515600 B.C. Ltd.*, BC EST #D128/98.

The "control test" considers four indicia of employment status: the employer's power of selection of the servant; payment of wages or other remuneration; the employer's right to control the method of doing work; and the employer's right to suspend or dismiss the employee. The "four factor" test examines who in the relationship has control, ownership of tools, chance of profit and risk of loss. The "integration test" or "organizational test" looks at the degree of integration of the worker into the employer's business. The "economic dependency" test focuses on an analysis of the relationship between the parties in order to determine whether a particular individual is carrying on business for himself or for someone else. The "specific result" test looks at the intent of the parties and whether a contract is to provide a single service leading to a specific result or rather is one to provide general efforts.

Having received the authorities cited by counsel, and the evidence bearing on all elements of the relationship between the parties, it is my conclusion that Kaleki Lloydd was not an employee of the Company and that the complainants were employees of Kaleki Lloydd Painting, not employees of Student Works Painting.

There is no doubt that through the device of the Owner-Operator Agreement Student Works Painting has a significant degree of control over certain important aspects of the franchisee's business. They have been listed above. However, this control falls well short, in my opinion, of establishing an employer- employee relationship between the franchiser and the franchisee.

I have no doubt from a review of the evidence that the experience of the franchisee is an *entrepreneurial* one. The successful operation of the franchise on a day-to-day business is in the hands of the franchisee. She hires her own staff without interference from Student Works Painting. It is trite to say that attracting and retaining good employees must be a key objective of any business. The franchisee must decide when to hire employees and how many she will need. She must decide how to find and attract good people to join

her business. She must decide what she can afford to pay her employees, within the constraints of law and the reality of the market-place. Those employees become registered for Workers' Compensation insurance under the name of the franchisee. The franchisee does all of these things without interference from or the involvement of the Company, other than the assistance which it provides on an administrative level.

The employees themselves, like the complainants in this case, are hired by the franchisee and are aware from the outset that they are employees of the franchisee and not the Company. On the evidence of Ms. Chippendale, the franchisee is equally clear that she is running her own business and is not an employee of the Company. (Having said that, while the use of the term "manager" on Kaleki Lloydd's business card is anomalous in light of the facts, it brings with it a risk in less clear case that the relationship between the franchisee and the franchiser will be misconstrued.)

It is the franchisee who must find customers in order to ensure the profitability of her business. Ms. Chippendale hired two students to do cold-calls after school, in an effort to secure contracts. It is also the franchisee who provides the tools with which the work is done. The operator's out-of-pocket expenses, including travelling and incidental expenses, are their own. Although the operators are specifically trained in the methodologies of Student Works Painting, the franchisees often use their own methods and are free to do so within the limits set out in the Agreement.

Although there is a relatively small guarantee of income from the Company, it is clear that the risk of profit or loss is on the franchisee. Although the franchisee's investment may appear small in some eyes, I accept that for a student the investment is a substantial one. In short, the franchisee's business is run by the franchisee and it bears the risk of failure or the economic and other benefits which come with a successful business. In summary, it is my finding that Kaleki Lloydd was not an employee of Student Works Painting, and the complainants were employees of Kaleki Lloydd, not Student Works Painting.

Associated Employers

As mentioned above, the Director seeks as well a declaration that Kaleki Lloydd Painting and Student Works Painting are a single employer within the meaning of section 95 of the Act. Although the Determination does not mention this issue, counsel submitted that it is "there by implication."

In my opinion, a section 95 finding should not be found to have been made "by implication." As I explained to counsel at the hearing, the issue in my view was not properly before me, and therefore I willnot consider it.

ORDER

I order, under Section 115 of the *Act*, that the Determination dated January 27,1998 be cancelled.

John McConchie
Adjudicator
Employment Standards Tribunal