

**TAKE A MEMO: USCIS ADDS COSTS, UNCERTAINTY
AND QUESTIONABLE LEGALITY IN REDEFINING THE
EMPLOYER-EMPLOYEE RELATIONSHIP**

By Sherry Neal and Michael Hammond

EXECUTIVE SUMMARY

The Associate Director of U.S. Citizenship and Immigration Service (USCIS) issued a controversial January 8, 2010 memorandum to adjudicators who review H-1B petitions for skilled foreign nationals that limits who can be considered an “employee” of a company.¹ In essence, the memorandum states that in some third-party placements – where the worker is assigned by a company to work at the location of a client – the worker would not be considered an employee of the company. The memorandum affects physicians, physical therapists, occupational therapists, specialty nurses, software engineers and many other professional occupations.

The effect of the memorandum bears no correlation to the goal of combating fraud. The memorandum oversteps the authority of a government agency, hindering business and economic recovery by harming companies who do third-party placements. The memorandum also contradicts other areas of immigration law and other federal laws that protect only “employees.”

The cost of doing business will increase, even for employers who have petitions approved under the new policy. A company is required to provide an itinerary so USCIS can examine the “employer-employee relationship” for each project that an H-1B worker will perform at a third party site. Unless USCIS concludes that the “employer-employee relationship” exists for ALL projects, USCIS may limit the approval date to cover only one project. Consequently, companies will need to do H-1B filings on a more frequent basis, thus incurring additional government filing and legal fees.

This new policy changes current regulations by making “control” of a worker the central focus and creating a standard of what USCIS considers to be sufficient “control.” Furthermore, it creates new rules that apply only to staffing companies. USCIS does not have the authority to change the law, consequently banning certain classes of businesses from H-1Bs. By summarily concluding that what it defines as “job shops” are not employers, USCIS has clearly engaged in rulemaking (or even lawmaking). The fact that it was done at the urging of a U.S. Senator to avoid the legislative process only adds to the need for the public notice and comment period that the Administrative Procedures Act requires.

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The memorandum from USCIS restricts employment in staffing industries and may have a detrimental effect on the economy by reducing flexibility, raising costs and increasing uncertainty for employers. This memorandum is bad policy and its issuance was procedurally defective. The memorandum should be withdrawn and changes to the H-1B laws should be left to Congress, or at the very least, any new rules should be issued pursuant to the Administrative Procedures Act. Raising costs, reducing flexibility and inhibiting business growth should not be the hallmark of any new policy on the definition of an employee.

THE GOAL OF THE MEMORANDUM

The H-1B temporary worker classification is the most regulated temporary employment classification for foreign nationals to work in the United States. Among other criteria, it is applicable to employers who seek to hire a foreign national in a position that requires at least a bachelor's degree or equivalent of education. It also requires the employer to pay the "required wage," which is the higher of the prevailing wage for the job in the location of employment or the actual wage the employer pays to its other employees who work in a similar position. The company must adhere to several reporting requirements including posting a notice of the job offer and wage to its current employees, maintaining a public inspection file regarding the petition, and providing foreign nationals with return transportation to their home country if the employment is terminated.²

On September 29, 2009 Senator Charles Grassley (R-IA) sent a letter to USCIS Director Alejandro Mayorkas requesting Mayorkas to take agency action to tighten enforcement of H-1B petitions.³ In the letter, Grassley pointed to a 2008 report by USCIS on H-1B visas⁴ and cited a company in his home state that has been indicted based upon USCIS allegations that the company did not have jobs available for the H-1B workers they petitioned for and failed to pay the workers the required wage. Based upon this, Grassley wrote:

We don't need a long, arduous legislative process to get at some of the problems. The agency can take immediate steps to eliminate fraud in the H-1B program, including cracking down on body shops that do not comply with the intent of the law.

On November 19, 2009 USCIS Director Mayorkas sent a letter to Senator Grassley stating the agency plans to conduct up to 25,000 worksite visits and inspections in fiscal year 2010.⁵ In addition, Director Mayorkas announced his plan to "issue further guidance to H-1B adjudicators that will clarify what evidence must be submitted when beneficiaries work at third-party worksites." Then on January 8, 2010 USCIS Associate Director Donald Neufeld released a memorandum limiting who qualifies under an "employer-employee" relationship. The Neufeld memorandum specifically concluded that "job shops" do not qualify as employers and may not employ H-1B workers, as Senator Grassley had recommended.

Leaving aside the good intention to combat fraud, the effect of the memorandum bears little relationship to the goal. The memorandum oversteps authority, hinders business and undermines companies that do third-party placements. The memorandum also contradicts other areas of immigration law and other federal laws that protect only "employees" or are premised on the number of "employees" at a company.

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THE CONTENTS OF THE MEMORANDUM

The memorandum from U.S. Citizenship and Immigration Services is guidance to the officers who process H-1B temporary employment petitions by U.S. employers.⁶ It has been added to the Officers Field Manual for USCIS.⁷ Although courts have said that agency memorandums are not “binding authority,” USCIS officers often follow the memorandum when reviewing immigration petitions.⁸ Indeed, USCIS has already denied some H-1B petitions based on the employer-employee relationship since the memorandum was issued.

The memorandum outlines some common law concepts of the employer-employee relationship but then takes several additional steps in deciding that some types of businesses would not qualify as employers. The Associate Director advised that a valid employer-employee relationship would exist in the following scenarios:

1. *Traditional Employment*: person works at an office location owned/leased by the company, the person reports to the company on a daily basis, uses the company’s tools and has work directly reviewed by the company.
2. *Temporary/Occasional Off-Site Employment*: person receives salary and employment benefits from the company and has an assigned office space at the company office but makes temporary, occasional visits to clients such as an accountant performing auditing service for a client of the company.
3. *Long Term Placement at a Third-Party Work Site*: person receives salary and employee benefits from the company and the company sends him to a client of the company to develop a program using the company’s tools and proprietary knowledge.

In contrast, the Associate Director advised that a valid employer-employee relationship would *NOT* exist in the following scenarios:

1. *Self-Employed Beneficiaries*: person is the sole operator, manager and employee of his own business. There is no outside entity that can exercise control over the person.
2. *Independent Contractors*: person works on commission to sell equipment of various companies that design and manufacture equipment. The person controls his own schedule, location, sales process and reports his own taxes.
3. *Third-Party Placement/“Job Shop”*: person has been assigned by the company to work at client location of the company. There is a contract between the company and the client location for the company to fulfill specific staffing needs. The person reports to a manager at the client location and the client location completes progress reports on the person.

*Take a Memo***THE MEMORANDUM HINDERS BUSINESS**

There is not “one-size-fits-all” when it comes to business models.⁹ Indeed, the growth of the U.S. economy in the last few decades is no doubt in part to broadening concepts on how to do business. In a traditional employment setting, the employer-employee relationship is easy to identify because the employer hires, supervises and pays the employee, typically with all work being performed at the employer’s location. The traditional employment setting has two willing participants – an employer and an employee. In today’s business world, the traditional employment relationship still exists but there are a myriad of other business models. For example, a standard staffing model has three willing participants – an employer, an employee, and a client or end user. But there are also more complex business models that may include not only an employer, employee and end-user but also contractors or vendor management organizations that are also a part of the business arrangement of an employer placing its employee at an end-user.

The staffing industry is a vital part of the U.S. economy. Approximately 2.6 million people are employed by staffing companies who hire and pay the employee while the employee performs the work at another location for a client under contract with the staffing company.¹⁰ Furthermore, the U.S. Bureau of Labor Statistics estimates that employment services, mostly staffing, is expected to be the second largest job-growth industry in the next six years.¹¹ The staffing industry crosses nearly every industry: healthcare, technical (information technology), professional – managerial, commercial and industrial.¹² Moreover, companies of all sizes use staffing companies. A survey by the American Staffing Association found that staffing services were used by 12% of companies with 25 to 99 employees and 24% of companies with 100 or more employees.¹³

The memorandum may hinder business growth. While the main impact is on staffing companies the memorandum may have a wider impact on other businesses. Even companies that are not in the staffing industry sometimes send employees to a third party site where the client supervises and controls the work. For example, a marketing company may send one of its employees, a marketing advisor, to a client to work onsite with the client to evaluate, design, and implement a marketing campaign for the client. Unless the marketing company is “controlling or supervising” the marketing advisor, USCIS could conclude that the marketing company is not the employer.

Furthermore, the memorandum may discourage entrepreneurship. Entrepreneurs who want to start a business in the U.S. may consider the policy in the USCIS memorandum to be an obstacle to starting or expanding a business. A natural result of this memorandum may be a decrease in business growth in the U.S. coupled with an increase in outsourcing work to other countries. This memorandum takes away the staffing flexibility that companies have enjoyed and seems to place the “client” in the unexpected position of taking on the legal responsibility of an employer.

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Without a doubt, the cost of doing business will increase: employers who receive denials based upon this new approach to the employer-employee relationship will have to pay additional filing fees and legal fees if they choose to appeal the cases or re-file new cases. Moreover, a company is required to provide an itinerary so USCIS can examine the “employer-employee relationship” for each project that an H-1B worker will perform at a third party. Unless the USCIS concludes that the “employer-employee relationship” exists for ALL projects, the USCIS may limit the approval date to cover only one project. Consequently, companies will need to do H-1B filings on a more frequent basis, thus incurring additional government filing and legal fees.

THE MEMORANDUM LIKELY VIOLATES THE ADMINISTRATIVE PROCEDURES ACT

Federal agencies often perform roles that are executive, judicial and legislative in nature. For example, when Congress enacts federal legislation that pertains to an agency, it is the responsibility of the agency to write the regulations that define the specifics of the law. The agency then acts in carrying out the regulations.

Agencies must follow the provisions of the Administrative Procedures Act (APA), a federal statute which was created in 1946 to regulate federal agency action. One of its basic purposes is “to require agencies to keep the public informed of their organization, procedures, and rules and to provide for public participation in the rulemaking process.”¹⁴ The notice requirement of 553(b) of the APA says:

General notice of proposed rulemaking shall be published in the Federal Register, unless persons subject thereto are named and either personally served or otherwise have actual notice thereof in accordance with law.¹⁵

Thus, federal agencies are required to issue a Notice of Proposed Rulemaking (NPRM) in the Federal Register before promulgating a new rule. The notice requirement not only ensures fairness to the affected parties but it also improves the quality of agency rulemaking because it allows the agency to gather information about the impact and potential problems with the proposed rule so that they can issue more informed rules.¹⁶

U.S. Citizenship and Immigration Services likely violated the APA because it did not provide notice and comment in the Federal Register before issuing a new policy on “employer-employee” relationship. While USCIS may contend that it was simply “clarifying an existing rule” rather than creating a new rule, it is evident that it is in fact a new rule because it exceeds what the USCIS regulations state and diverges from previous agency policy.

USCIS regulations define an employer as “A person, firm, corporation, contractor or other organization in the United States which:

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- (1) engages a person to work in the United States;
- (2) has an employer-employee relationship with respect to employees under this part, as indicated by the fact that it may hire, pay, fire, supervise or otherwise control the work of any such employee; and
- (3) Has an Internal Revenue Service tax identification number.”¹⁷

This new policy changes the above regulations by making “control” the central focus and creating a standard of what USCIS considers to be sufficient “control.” Furthermore, it creates new rules that apply only to staffing companies. USCIS does not have the authority to change the law, consequently banning certain classes of businesses from H-1B’s. By summarily concluding that what it defines as “job shops” are not employers, USCIS has clearly engaged in rulemaking. The fact that it was done at the urging of a U.S. Senator to avoid the legislative process only adds to the need for the public notice and comment period that the Administrative Procedures Act requires.

THE MEMORANDUM IS INCONSISTENT WITH OTHER PROVISIONS OF IMMIGRATION LAW

The USCIS memorandum conflicts with other areas of immigration law. First, the USCIS memorandum creates a standard for “employer-employee relationship” in the context of H-1B petitions that is more onerous than other nonimmigrant (or even immigrant) visa petitions. For example, a staffing company could apply for TN visa classification, available only to Canadian citizens and Mexican citizens, for the same position as an H-1B petition and the foreign national would be considered an “employee” and receive TN status but not be considered an “employee” for H-1B purposes, and thus receive an H-1B denial.

Second, the memorandum conflicts with the scope of an employer-employee relationship in the employment sanctions context. Specifically, the Immigration Reform and Control Act of 1986 (IRCA) requires employers to verify the identity and employment eligibility of all new hires within the first three days of employment. An employees is deemed to be “an individual who provides services or labor for an employer for wages or other remuneration” except for independent contractors and casual hires.¹⁸

Third, the memorandum is inconsistent with the scope of the employment-employee relationship in the regulations pertaining to the H-1B category itself. For example, the H-1B temporary visa classification – the same category which is the subject of the recent memorandum – bases a portion of its filing fee (called the “H-1B training fee”) on the number of employees. Specifically, a company with 25 or fewer “employees” must pay \$750 whereas a

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company with more than 25 employees must pay \$1500 with each H-1B petition.¹⁹ Furthermore, the H-1B category imposes additional burdens on companies that employ a percentage of H-1B workers (deemed to be “H-1B dependent employers”) by requiring such employers to attempt to recruit U.S. workers for the position. USCIS, by using the regulations, deems a worker at a staffing company to be an employee for purposes of the H-1B dependency calculation and the H-1B training fee calculation.

If there is not an employer-employee relationship in third-party placements per this recent memorandum, then there would not be an employer-employee relationship across the entire spectrum of H-1B applicability. Thus, the staffing company may assert as a defense that a worker is not an employee, consequently, the regulations pertaining to the required wage do not apply, the I-9 employment verification laws do not apply, and the H-1B dependency rules do not apply because the H-1B employees at third-party placements are not “employees.” This would be an absurd result. But USCIS needs to be consistent. Simply put, USCIS cannot have it both ways by asserting that there is no employer-employee relationship to deny a benefit and yet assert that there is an employer-employee relationship to impose obligations and assess penalties.

THE MEMORANDUM IS INCONSISTENT WITH OTHER AREAS OF THE LAW

The USCIS memorandum is far-reaching and inconsistent with other provisions of the law. The Equal Employment Opportunity Commission (EEOC) has previously considered this same scenario as USCIS and found that a worker of a staffing company is the employee of the staffing company. In a notice about the applicability of EEOC laws to workers of staffing firms, the EEOC said:

The relationship between a staffing firm and each of its workers generally qualifies as an employer-employee relationship because the firm typically hires the worker, determines when and where the worker should report to work, pays the wages, is itself in business, withholds taxes and social security, provides workers' compensation coverage, and has the right to discharge the worker. The worker generally receives wages by the hour or week rather than by the job and often has a continuing relationship with the staffing firm. Furthermore, the intent of the parties typically is to establish an employer-employee relationship.²⁰

The Internal Revenue Service is consistent with the EEOC on the “employer-employee” relationship. Specifically, IRS Section 1706 of the 1986 tax code defines the treatment of contract workers for tax purposes. Under the tax code, the person is not considered an “independent contractor” but rather an “employee” of the staffing company. When Congress passed that section of the law, it “singled out” engineers, designers, drafters, computer programmers, systems analysts and other similarly skilled workers who provide work for a staffing company.²¹

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It is illogical for USCIS to reach a conclusion opposite from the EEOC and IRS on the definition of an employee. The clarity of an “employer-employee relationship” is important for both employers and employees. Certain rights are available to employees that are not available to independent contractors or self-employed individuals. For example, workers compensation is a program in all U.S. states that provides compensation to employees who get injured on the job, but does not apply to independent contractors. If an employer meets the employee threshold in the law, a foreign national on an H-1B would be considered an employee of a staffing company under the *Family and Medical Leave Act of 1993* (FMLA), the *Consolidated Omnibus Budget Reconciliation Act* (COBRA), and the *Americans with Disabilities Act* (ADA) – but still not be considered an employee by U.S. Citizenship and Immigration Services.

CONCLUSION

The USCIS memorandum declares that a worker of a company, in a third-party placement arrangement, is not an employee of the company. USCIS did not say what it believed the worker to be. There can be only three possibilities: the worker is either an employee of the staffing company, an employee of the client/end-user, or an independent contractor. The willing participants in the employment setting – the company, the worker, and the client/end-user – have a stake in the worker’s status. None of them intend for the worker to be an independent contractor. None of them intend for the worker to be an employee of the client/end-user. USCIS probably did not intend to make a class of individuals as “non-employees” thereby affecting a host of legal rights and responsibilities, including tax, workers compensation, discrimination, and disability coverage.

The memorandum from USCIS restricts employment in staffing industries and may have a detrimental effect on the economy by reducing flexibility, raising costs and increasing uncertainty for employers. This memorandum is bad policy and its issuance was procedurally defective. The memorandum should be withdrawn and changes to the H-1B laws should be left to Congress, or at the very least, any new rules should be issued pursuant to the Administrative Procedures Act. Raising costs, reducing flexibility and inhibiting business growth should not be the hallmark of any new policy on the definition of an employee.

END NOTES

¹ Memorandum to Service Center Directors, “*Determining Employer-Employee Relationship for Adjudication of H-1B Petitions, Including Third-Party Site Placements*,” (January 8, 2010). Additions to Officer’s Field Manual (AFM) Chapter 31.3(g)(15)(AFM Update AD 10-24).

² Certain employers – those who are deemed “dependent” based upon a workforce of at least 15% H-1B workers, those who are deemed “willful violators” based upon previous noncompliance with the requirements or those who are deemed “TARP employers” based upon receipt of TARP funds under the stimulus bill – cannot file an H-1B petition unless they file additional attestations.

³ Available at www.grassley.senate.gov/news.

⁴ On September 2008 USCIS issued a report on the H-1B program. As part of the study, the USCIS sampled 246 petitions out of 96,827 petitions that were denied, approved or pending between October 1, 2005 and March 31, 2006. USCIS concluded that 33 cases may have contained fraud and 18 cases appeared to contain technical violations.

⁵ USCIS and the Department of Labor have certain authorities to investigate H-1B employers. Employers who file an H-1B petition must pay an additional \$500 fraud fee to the USCIS, which is designed, in part, to fund investigations. In 2009 the USCIS started doing unannounced on-site audits of H-1B employers.

⁶ The H-1B classification is for “specialty occupations,” positions that require at least a bachelor’s degree or equivalent level of education.

⁷ Memorandum to Service Center Directors, “*Determining Employer-Employee Relationship for Adjudication of H-1B Petitions, Including Third-Party Site Placements*,” (January 8, 2010). Additions to Officer’s Field Manual (AFM) Chapter 31.3(g)(15)(AFM Update AD 10-24).

⁸ Courts have declared, “Agency interpretations that are not arrived at through precedent decision or notice-and-comment rulemaking – such as those in opinion letters, policy statements, agency manuals, and enforcement guidelines – lack the force of law. See AAO Decision, *In Re: Technical Services, Inc.*, (July 22, 2008) citing *Christensen v. Harris County*, 529 U.S. 576 (2000).

⁹ In a study by Sloan School of Management, *Do Some Business Models Perform Better than Others? A Study of the 1000 Largest US Firms*” (2004), the authors recognized that U.S. firms use a myriad of business models. They analyzed four basic types of business models and 16 specialized variations of those basic types.

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¹⁰ See “*Looking for Growth – Annual Economic Analysis Puzzles Through the Data and Explains the Trends*”, American Staffing Association (2009), citing statistics from U.S. Bureau of Labor Statistics. www.americanstaffing.net.

¹¹ *Ibid.*, 8.

¹² *Ibid.*, 8.

¹³ *Ibid.*, 8.

¹⁴ Attorney General’s Manual on the Administrative Procedure Act (1947).

¹⁵ 553(b) of the APA.

¹⁶ *Small Refiner Lead Phase-Down Task Force v. United States EPA*, 705 F.2d 506, 547 (D.C. Cir. 1983)

¹⁷ 8 C.F.R. 214.2(H)(4)(iii).

¹⁸ 8 C.F.R. 274a.1(f).

¹⁹ *The American Competitiveness and Workforce Improvement Act of 1998* (ACWIA) initially created the H-1B education and training fee of \$500 for H-1B petitions.

²⁰ EEOC Notice, Number 915.002, “*Enforcement Guidance: Application of EEO Laws to Contingent Workers Placed by Temporary Employment Agencies and Other Staffing Firms*” (12/03/1997), which was later increased to \$1,500.

²¹ Harvey Shulman, “*Our Low-Tech Tax Code*”, *The New York Times* (Feb. 20, 2010).

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