
Think Your Worker Is an Independent Contractor? Think Again

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- Crackdown by DOL and other state and federal governmental agencies
- DOL Memorandum of Understanding
- DOL Administrator's Interpretation

Misclassification Is a “Multifaceted Problem”

- DOL – FLSA Protections
- IRS – no tax withholding
- Immigration – no I-9s filled out
- Industrial Commission – no workers’ compensation insurance
- NC Department of Commerce – no unemployment tax

Legal Tests

- Vary from federal and state agencies and courts
- Complex, subjective, and differ from law to law
- DOL – economic realities
- IRS
- Common law
- Some states have statutory tests

DOL Misclassification Initiative

- Why?
 - Misclassified employees are denied access to critical benefits
 - Misclassified employees are denied access to employment protections such as:
 - Minimum wage
 - Overtime compensation
 - Family and medical leave
 - Unemployment insurance
 - Safe workplaces

DOL Misclassification Initiative

- Misclassification generates substantial losses to federal and state governments:
 - Lower tax revenues
 - Lower unemployment insurance
 - Lower workers' compensation funds
- Foster fair competition

DOL Misclassification Initiative

- Wage and Hour Division (“WHD”) is working with IRS
- WHD has entered into partnerships with 28 states:
 - Information sharing
 - Coordinated enforcement
- Some of the agreements include cooperation of:
 - Employee Benefits Security Administration
 - OSHA
 - OFCCP

Misclassification Initiative

On July 15, 2015, the DOL's Wage and Hour Division Head issued an "administrator's interpretation" clarifying the line between independent contractors and employees: the "suffer or permit standard"

Administrator's Interpretation

- Economic realities test reinterpreted
- Does not change independent contractor test
- De-emphasizes amount of control
- Focus on whether worker is in business for himself and economically independent
- Changes the way DOL applies the test
- Presumption that most workers are employees

Misclassification Initiative

- DOL directs employers to look at the “economic realities” of the worker’s situation: whether the worker economically depends on the employer.
- If the worker economically depends on the employer, the worker is an employee.
- According to DOL, “applying the economic realities test in view of the broad definition of ‘employ’ under the Act, most workers are employees under the FLSA.”

Misclassification Initiative

An employer's own classification of a worker's status is irrelevant.

- Even if the worker agrees
- Even if the worker insists

Key Factors to Consider

1. Extent to which the work performed is an integral part of the employer's business.
 - Work integral to business indicates employer-employee relationship
 - Whether workers are integral does not depend on whether they are easily replaceable
 - » a worker making calls at a call center may be one of hundreds but his work is still integral to the business purpose of the call center
 - Work can be integral no matter where performed

Key Factors to Consider

2. Opportunity for the worker's own profit or loss depending on worker's managerial skill
 - whether the worker's managerial skill can affect his/her profit and loss
 - the more managerial responsibility affecting profits and losses a worker has, the more likely to be an independent contractor
 - profit-and-loss-making managerial skills
 - decisions on hiring, purchasing, advertising, and renting space
 - managing timetables
 - employee typically does not have the ability to make decisions affecting ability to make more money, except to decide to work more hours (which does not indicate managerial responsibility)

Key Factors to Consider

3. The extent of the relative investments of the employer and the worker.
 - Independent contractor should make investments that support the worker's business beyond any one job
 - employers must compare that investment with their own
 - if worker's investment is relatively minor, that suggests the worker may be economically dependent on the employer
 - The worker's investment must be significant in nature and magnitude relative to the employer's investment in its overall business to indicate the worker is an independent contractor.

Key Factors to Consider

4. Whether the work performed requires special skills and initiative
 - a worker's business skills, judgment, and initiative are determinative
 - a worker's technical skills are not determinative
 - For example, cable installers, carpenters, and electricians have technical skills
 - to be independent those skills should be used in some independent way such as demonstrating business-like initiative (i.e. determining sequence of work, ordering materials, bidding on jobs)

Key Factors to Consider

5. The permanency of the relationship
 - transient relationships suggest independent contractor
 - lack of permanence does not automatically suggest independent contractor – the reason should be reviewed
 - is it due to operational characteristics?
 - is it due to worker's own initiative?
 - permanent or indefinite engagements suggest employer – employee relationship

Key Factors to Consider

6. The nature and degree of control exercised by the employer.
 - worker must exercise control over meaningful aspects of work
 - nature and degree of employer's control is relevant, not the reason for it
 - control should not play an oversized role in the analysis

Now What?

Message is clear that DOL is waging war on misclassification

- DOL budget request asked for about \$32 million to hire 300 full-time enforcement employees and support staff
- “Additional resources dedicated to planned enforcement – as opposed to reactive – would allow the agency to address systemic compliance problems more strategically.”

Now What?

- In litigation, defense attorneys can rely on cases not mentioned in the guidance that reflect more neutral application of the economic realities test.
- Issue the what degree of deference, if any, courts will give the DOL guidance.
- Administrator's determination sends the clear message that DOL views most workers as employees – difficult to use this guidance to confirm IC but very easy to confirm an employee.

US DOL

- Hiring more investigators to “detect and deter” independent contractor misclassification
- Prosecuting more companies
- Grants to state workforce agencies to identify misclassification and recover unpaid unemployment taxes

IRS

- Actively seeking to restore lost tax revenue
- Questionable Employment Tax Practices
 - Program to share information and enforcement techniques with state revenue commission and workforce agencies
- Enhanced efforts to promote SS-8 Program
- Voluntary Classification Settlement Program
- Audit Process

State Workforce Agencies

- Increase in number of random and targeted audits
- Focusing on misclassification through unemployment and workers' compensation claims process
 - Potential for “mini-class action”
 - “all similarly situated” workers
- State attorneys general taking active role

Consequence of Misclassification

- Back taxes
- Social Security and Medicare taxes
- Unemployment insurance taxes
- Workers' compensation premiums
- Civil penalties
- Criminal penalties

Consequence of Misclassification

- Government audits
- Overtime compensation and minimum wage
- Attorney's fees
- Health insurance and benefits
- Work-related expenses
- Unpaid sick and vacation pay

Is it making a difference?

FY 2015 WHD investigations =

\$74 million in back wages for more than 102,000 workers in industries such as janitorial, temporary help, food service, day care, hospitality, and garment

Now What?

- Reevaluate compliance
- Reclassify
- Review and strengthen independent contractor agreements and internal policies
- Seek advice

Questions?

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