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The GSH 60-Second Memo

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Independent Contractor Agreements: One Size Does Not Fit All

By Michael Mishlove, Esq.

A recent GSH 60-Second Memo reported developments and initiatives that are clearly harbingers of increased enforcement activity by the U.S. Equal Employment Opportunity Commission and the Department of Labor ("DOL"). Any doubt about what level of "heightened enforcement" the DOL contemplates in relation to one of those initiatives - employee misclassification prevention and enforcement - should be immediately dispelled upon review of the FY 2011 Congressional Budget Justification the agency submitted to Congress earlier this year. Indeed, review of the DOL's FY 2011 Budget and FY 2011 Congressional Budget Justification report is ominously telling with respect to what employers may reasonably expect in this area.

The DOL's FY 2011 Budget includes approximately \$25 million to support a new multi-agency initiative designed to strengthen and coordinate governmental efforts to combat labor and employment law violations and the substantial losses to the Treasury Department and the Social Security, Medicare, and Unemployment Insurance Trust Funds that result from the misclassification of employees as independent contractors. (See DOL FY 2011 Congressional Budget Justification at 33.) "This initiative includes State audits of problem industries supported by Federal audits, enforcement activities, litigation against major employers that cross state lines, and additional interagency cooperation between DOL and the IRS at the Federal and State levels." (DOL FY 2011 Budget in Brief at 28.) More specifically, the DOL budget provides for allocating:

- Approximately \$12.0 million and 90 full-time equivalent employees ("FTEs") to the Wage and Hour Division to "support field investigator training activities and an additional 4,700 investigations [directed at] industries with misclassification

characteristics, such as construction, child care, home health care, grocery stores, janitorial, business services, poultry and meat processing, and landscaping" (*id.* at 44);

- \$11.25 million and 2 FTEs for the Employment and Training Administration "for competitive grants to States to increase their capacity to focus on misclassification and reward the States that are most successful at detecting and prosecuting employers that fail to pay their fair share of taxes due to misclassification" (*id.* at 1); and
- \$1.6 million and 10 FTEs allocated to the Solicitor of Labor for the purpose of pursuing "misclassification litigation, including multi-State litigation to coordinate enforcement with States and leverage their groundbreaking work." (*id.* at 2)

In addition, the DOL seeks \$150,000 targeted for the Occupational Safety and Health Administration "to modify training curriculum and investigation guidelines to allow inspectors to identify potential employee misclassification and share information with WHD." (*id.*)

The initiatives envisioned by the DOL and reflected in its FY 2011 budget acquire added significance by the recent reintroduction in both Houses of Congress of bills to amend the Fair Labor Standards Act so as to provide for, among other things, a special penalty for persons who misclassify employees as independent contractors. These bills reflect a renewed initiative in Congress to pass the "Employee Misclassification Prevention Act," a bill previously introduced in 2008 that died in committee. The new Senate bill (S. 3254), introduced on April 22, 2010, has already been referred to committee, and on June 17, 2010, hearings on the bill were held before the Senate Committee on Health, Education, Labor, and Pensions. Given the federal government's ever-increasing need for additional revenue and in view of the unqualified success at the state level in recouping millions of unpaid payroll taxes, unemployment insurance contributions, and worker's compensation payments through coordinated multi-agency task forces, it is no small wonder that the DOL is ramping up and budgeting for exactly the same sort of initiative at the federal level. Indeed, based on these considerations, many pundits believe the Employee Misclassification Prevention Act of 2010 has a high likelihood of passage this time around. Coincidentally, it just so happens that on the very day GSH issued its 60-Second Memo discussing the harbingers of increased enforcement activity, Wisconsin Governor Doyle signed into law Senate Bill 672, which will become effective January 1, 2011, and requires the Wisconsin Department of Workforce Development (DWD) to establish a system ensuring the proper classification of workers under unemployment insurance, worker's compensation, and labor standards laws. The law specifically requires the DWD to implement measures for receiving and investigating complaints of alleged employee misclassification and to inform other state or local agencies of such misclassification.

Needless to say, these developments provide a compelling

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reason for employers to reexamine their employee-classification practices, and more specifically to review their Independent Contractor Agreements. In that vein, the fact that misclassification legislation at both the state and federal level emphasize interagency coordination and multi-agency task force enforcement initiatives calls attention to an extremely important but routinely overlooked consideration relating to the issues of employee/independent-contractor classification - namely, there is no single universally determinative definition of "employee." Consequently, not only might there be differences between the way federal and state agencies might construe that term, but also, even among the various agencies within a given state, the term "employee" can have different definitions for purposes of applying laws pertaining to unemployment insurance, state tax withholding, and workers' compensation. In Wisconsin, for example, the statutory definition of "employee" applicable to the state's unemployment insurance differs from the statutory definition of "employee" under the state's workers' compensation laws, and neither of these statutory definitions is the same as that used by the state and federal government for income tax purposes.

Employers, and their accountants and lawyers alike, tend to be most familiar with the 20-point test often used by the IRS (although it should be noted that the IRS has begun to regroup these factors into a new qualitative approach that looks at the degree of control and independence in three separate categories), and they often are not even aware that different tests/standards might exist in their jurisdiction for purposes of determining whether contributions must be made to the state's unemployment insurance and/or workers' compensation systems. For that reason, employers commonly base their employee-classification practices and craft their Independent Contractor Agreements with only that standard in mind. However, when it comes to crafting Independent Contractor Agreements, one size simply does not fit all. When the multi-agency employee-misclassification task force does one of its "main street sweeps," as the New York Joint Enforcement Task Force on Employee Misclassification likes to call them, employers who have not had their Independent Contractor Agreements reviewed by counsel for purposes of compliance with *all* applicable employment-related laws are likely in for an unpleasant awakening.

Making a close-to-unmanageable problem even worse is the fact that even where the same criterion (or variant thereof) is used by different agencies, there can be considerable variance in the way the different agencies apply the criterion and in the administrative procedures used by the respective agencies for resolving employee-misclassification disputes. Such procedural differences are often not inconsequential, encompassing, for example, issues such as who (the employer or the government) bears the burden of proof in a contested employee-misclassification dispute.

It is impracticable here to provide any detailed account of the different definitions of "employee" within and across the states. However, it is extremely important that employers take such measures as are necessary to review their employee-classification practices and any agreements relating to employee/independent-

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contractor classification to ensure they pass muster under all of the myriad employment and tax laws that might apply.

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