

STEPPED UP SCRUTINY OF CLASSIFYING INDIVIDUALS AS INDEPENDENT CONTRACTORS

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As the economy begins to pick up employers looking to increase their workforce often consider doing so through the use of independent contractors rather than hiring employees, at least until they begin to feel more secure that the recovery will continue. However, the length of time an individual might provide services to a company has nothing to do with whether the person can legally be classified as an employee or an independent contractor. An individual working a single day for a company might be an employee, while another person providing services to the same company for an indefinite period might be an independent contractor.

Recognizing that employers coming out of the recession might be tempted to misclassify individuals that are employees as independent contractors either because of insecurity in the recovery and/or to save on various payroll taxes and the cost of workers' compensation insurance, state and federal agencies have recently joined forces to uncover such practices. These agencies estimate that employers' misclassifications of employees as independent contractors costs them billions of dollars in lost revenue and leaves workers and their families without any income when they lose their job or are injured at work.

As a result of these concerns, the Obama Administration's proposed fiscal year 2011 budget provides significant funding for the Department of Labor to uncover employees misclassified as independent contractors:

"... the Departments of Labor and Treasury are pursuing a joint proposal that eliminates incentives in law for employers to misclassify their employees; enhances the ability of both agencies to penalize employers who misclassify; and restores protections to employees who have been denied them because of their improper classification. This proposal will increase Treasury receipts by more than \$7 billion over 10 years. The 2011 Budget for [the Department of Labor] includes an

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additional \$25 million to target misclassification with 100 additional enforcement personnel and competitive grants to boost States' incentives and capacity to address this problem."

Here in New Hampshire, the Departments of Labor, Employment Security, Insurance and Revenue Administration have already begun to work together to uncover and prevent misclassification of individuals as independent contractors rather than as employees. And, the Internal Revenue Service is providing reports to the NH Department of Employment Security relating to issuance of 1099 forms given to independent contractors instead of W-2's given to employees. First and foremost these New Hampshire agencies have teamed up to educate employers in New Hampshire on requirements that must be met in order for an individual to be considered an independent contractor. But, while hoping that education on this issue will do the trick, these agencies have made it clear that failure to comply will result in enforcement actions. In conjunction with this effort the state has formed a Task Force for the Misclassification of NH Workers. The Task Force's web site asks individuals to report tips of misclassifications and promises confidentiality of the source, www.nh.gov/nhworkers. Maine, Massachusetts and Vermont all have similar task forces on this issue and similar web sites asking for reports of misclassifications.

Effective January 2008 the legal requirements for an individual **to qualify as an independent contractor under New Hampshire wage/hour, whistleblower and worker's compensation laws** was unified into a single twelve factor test, while New Hampshire's unemployment law has retained a three part test. Under the twelve part wage/hour, whistleblower/worker's compensation test any person who performs services for pay is presumed to be an employee unless the hiring entity can show that the individual meets all twelve criteria. This is not an easy test to meet. The twelve criteria that must be met in order for a person to be classified under these laws as an independent contractor are the person must:

1. **Have a federal employer ID # or SS #** or agree in writing to carry out the responsibilities imposed on employers under these laws;
2. **Have control and discretion over the means and manner of performance** of the work in that the result is the primary element bargained for by the hiring party (i.e. will paint house);
3. **Have control over the time the work is performed**, although hiring party can reach agreement with the person as to a completion schedule, range of work hours and maximum number of hours to be provided by person.

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4. **Hire, pay and supervise any assistants;**
5. Hold themselves out to be **in business for themselves;**
6. Have **continuing or recurring business liabilities** or obligations;
7. Have the **success or failure of their business depend on the relationship of their business receipts to expenditures;**
8. **Not have their compensation determined unilaterally by the hiring party;**
9. Be **responsible in the first instance for the main expenses related to work performed** (office space, advertising, insurance, continuing training/education etc.), but hiring party can provide supplies and materials necessary to perform the work (such as paint for the house);
10. **Supply principal tools** and instrumentalities used in the work, except hiring party may furnish tools or instrumentalities unique to its special requirements or which are located on its premises (i.e. independent painting contractor would use own ladders but hiring party supplies paint for specific project
11. Be responsible for satisfactory completion of work and may be held **contractually responsible for failure to complete the work;**
12. **Not be required to work exclusively for hiring party.**

To be classified as an **independent contractor under New Hampshire Unemployment Compensation law** the following three criteria must be met:

1. The individual must be **free from control or direction** over the performance of the service **both under contract and in fact;**
2. The **service** is either **outside the usual course of the business** for which it is being **performed, or the service is performed outside of all places of business** of the enterprise for which it is performed;
3. The individual must be **customarily engaged in an independently established** trade, occupation, profession or **business.**

Employers in this current environment of heightened governmental scrutiny of classification of anyone who provides services to them as an independent contractor should be extremely careful in doing so. Classifying an individual as an independent contractor is being



watched and enforcement action will be taken for misclassifications. Misclassification can result in a government investigation and orders for payment of unemployment and worker's compensation assessments, back wages, overtime, lost benefits, fines and attorneys fees. Please contact anyone in our group if you have any questions or need any help in determining if an individual you employ or are hiring can legally meet the tests required to be classified as an independent contractor in the state in which they are working.

The Devine, Millimet & Branch Labor, Employment and Employee Benefits Group offers this free Friday E-Mail Alert service to provide information on recent developments in labor, employment and employee benefits law. If you have any questions about this e-mail, or if you know of anyone else who may be interested in receiving these alerts, please send us an e-mail at employment@devinemillimet.com.

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