

Misclassification - Independent Contractor vs. Employee

Workers' Compensation and
Unemployment Insurance Programs



November 1, 2010

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Today's Goals

- Provide better understanding of the legal definitions of an employee
- Improve employers ability to distinguish between independent contractors and employees
- Provide information on law changes related to employee classification.

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This is an overview. Actual situations will be facts specific



Employee vs. Independent Contractor . Simple truth

- More often than not
- If the individual working for you does not have any employees
 - ☞ 99% of the time, they are YOUR employee for the purposes of Workers Compensation (WC) and Unemployment Insurance (UI) purposes.
- For purposes of WC and UI, an independent contractor is someone you hire, who
 - ☞ performs a job that is not similar or connected to your business, and
 - ☞ whose work you have no direction or control over.



Who is an Employer?

- For WorkersqCompensation Program,
 - Technically ò An employer is: any body of persons, corporate or unincorporated, public or private, and owner or lessee of premises, or other person who is virtually the proprietor or operator of the business there carried on, but who by reason of being an independent contractor is not the direct employer of the workers employed there.
 - Can be as simple as ò if an individual performs work for you that would otherwise have to be performed by yourself or an employee, the individual **IS** your employee.



Who is an Employer?

- For Unemployment Insurance Program,
 - Technically ÷ An employer is an entity who has individuals working for them. There are various tests on whether or not the employer is liable to pay into the unemployment trust fund and whether the wages paid are reportable and taxable.
 - Can be as simple as ÷ if an individual performs work for you that would otherwise have to be performed by yourself or an employee, the individual **IS** your employee.

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Who is an employee?

- Most labor/tax laws assume anyone compensated for work is an employee unless the employer can demonstrate otherwise, or there is a specific exemption in the law.
- The laws were intended to provide WC and UI coverage in most cases



Employee vs. Independent Contractor - Tests

- There are a number of legal test to determine who is an employee:

Common Law . IRS

Right to control/nature of business . VT WC

Economic Reality Test . FLSA

Hybrid test . UI~~§~~ ABC Test



What does all this mean?

- If you are an employer, who has one or more employees, and you hire another individual, most likely that individual is YOUR employee.
- To validate such, there are various tests.
- For the purposes of WC and UI, it is imperative that you use the right test to avoid misclassification penalties.



WC Program

- Is individual my employee for Workersq Compensation purposes?
 - YES - if the individual has entered into the employment of, or works under contract of service or apprenticeship with you as the employer ò
- There are a few limited exemptions



WC Program Exceptions . Not liable for coverage if:

- Work of a casual nature AND not for the purpose of the employers trade or business
 - Casual work is generally one time in nature and not similar to work done by the employer
- Amateur Sports
- Agriculture employment if farm payroll < \$10,000 per year
- Family member living in employer's house
- Licensed real estate broker/sales



WC Program Exceptions . Not liable for coverage if: (continued)

- Service in and about a private dwelling
- With approval of VDOL, up to 4 executives of a corporation or LLC
- Sole proprietor or partner owner, if
 - Work is different than work of the person the individual contracts with, AND
 - Individual is in business for self, AND
 - Individual is not treated as employee for income tax, AND
 - There is a written contract expressly waiving coverage.



WC Program - Employee vs. Independent Contractor

- Once its determined employer is providing covered employment, is the worker your employee?
 - Depends
- Ask the following questions:
 1. Did the individual perform services? If yes,
 2. Did you pay the individual wages? If yes, an %ight to control/nature of business+test must be applied.



WC Program . Employee Test

- The worker is only an independent contractor if, the employer meets his or her burden by showing:
 - A. Worker is free from direction and control;
AND
 - B. Worker is doing work outside the usual course of the business



WC Program . No wages exempt

- If an individual is an employee under the WC tests they must be covered with WC insurance even if the wages earned are small or the hours worked are few.
- Sales persons, other than real estate sales persons are considered employees, even if they only receive commissions



UI Program - Employee vs. Independent Contractor

- Is individual my employee for Unemployment Insurance purposes?
- Ask the following questions:
 1. Is the person or entity you hired an individual? If yes,
 2. Do they have other workers? If no,
 3. Did the individual perform services? If yes,
 4. Did you pay the individual wages? If yes, ABC+test must be applied.

UI Program - ABC+test

- The worker is an independent contractor only if, the employer meets his or her burden by showing:
 - A. Worker is free from direction and control; AND
 - B. Worker is doing work outside the usual course of the business, or outside the place where the business is conducted; AND
 - C. Worker is independently established in a trade, occupation, profession or business.
- All three prongs of the test must be met to find individual is not your employee

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A failure of any part or parts of this test will require the individual be included on the quarterly unemployment tax report for unemployment **and for the health care assessment**

UI Program - %ABC+test additional thoughts

- A. Individual is free from direction and control; examples of this might be:
 - Individual bids for the job and is paid by the job
 - Individual completes job with no direction, supervision, or set hours
- B. Individual is doing work outside the usual course of the business, or outside the place where the business is conducted; examples might be:
 - Individual does work which none of your employees does and for which you do not advertise
 - Individual does all work at their own facility
- C. Individual is independently established in a trade, occupation, profession or business; examples might be:
 - Individual has employees of their own
 - Individual has liable UI account with VDOL
 - Individual advertises their business services to the general public

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The UI B test is a two part test; if either part of the B test fails, B fails.

Someone who has a liable UI account with VDOL should be able to provide you with a copy of their last quarterly UI report.



UI Program - Wage exemptions

- While a worker may be your employee, certain wages are not useable for determining liability and are exempt for coverage/reporting purposes:
 - Religious/church employment
 - Work-study students
 - Insurance sales, if paid by commission
 - Employment authorized under certain VISAs

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Further information is provided on Labor's website.

<http://labor.vermont.gov/Default.aspx?tabid=577>



UI Program - Wage exemptions (continued)

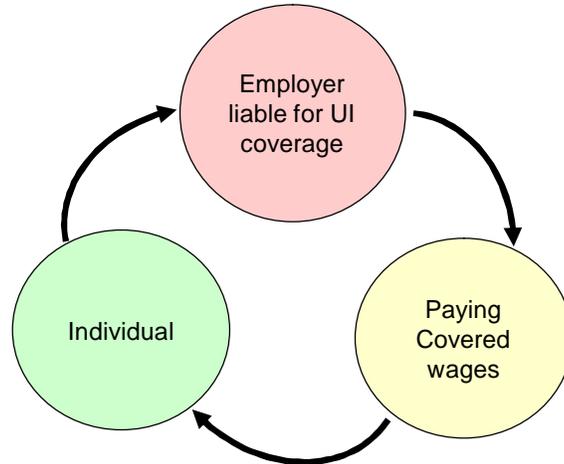
- Any sales for which the State requires a license
- Full time students working at summer camp (if returning to school)
- Direct sellers (like vacuum cleaner salespersons, home paper delivery, etc)
- Casual employment (\$50 of wages or less, services outside usual course of the business.)

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Individuals engaged in the sale of real estate and fire protection systems, if paid by commissions, etc.

Full time students returning to school for an organized camp, which operates for less than 13 calendar week in a year.

UI Program . Bigger Picture



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Each of the following topics are connected:

~ An employer must meet liability tests . as it relates to %covered+wages.
<http://labor.vermont.gov/Default.aspx?tabid=573>

~ An employer can be found liable for unemployment insurance coverage, with some of the wages being exempt from reporting/use.
<http://labor.vermont.gov/Default.aspx?tabid=577>
<http://www.labor.vermont.gov/Default.aspx?tabid=574>

~ An individual is the one performing the work; the question is whether or not an employer/employee relationship exists.



WC and UI - Employee vs. Independent Contractor

- As you can see, if there is a connection between your business and the individual, in most cases the individual is your employee for WC and UI purposes
 - EVEN when the individual believes him or herself to be an independent contractor
- Reminder
 - individual is one who has no workers
- Side note:
 - For the past 2 years VDOL has attempted to get law changed to have the same test for both programs



Examples for determining \tilde{o} Is this individual my employee?

- The Carpenter
- The Truck Driver
- The Catered Event



Example A . The Carpenter

- A building contractor needs extra help to finish a project so it engages a carpenter, who is in business for himself, to complete part of the project
 - Building contractor facts:
 - Has already been found liable for reporting under the UI program
 - Exercises no direction or control over carpenter; doesn't tell the carpenter how or when to do the work
 - Has other workers performing same or similar functions
 - Carpenter facts:
 - Does not have any employees. For UI purposes is considered to be an individual. Having employees is not relevant for WC purposes
 - Did not bid on the job; is fitting the building contractor's job in among other jobs he already has lined up

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Example A . The Carpenter

UI-ABC test (<i>Must meet all 3</i>)			WC “two-part” test – (Must meet both)		
A	Right to Control	✓	1.	Right to Control	✓
<p>The Carpenter is sufficiently skilled to operate without supervision, was not involved in the bidding, and works his own schedule. Additionally, the Building Contractor is overall responsible for getting the job done, but does not exercise any control over means/manner of Carpenter’s work. Therefore this part of the test are met for UI and WC.</p>					
B	Outside course/places of business	X	2.	Outside course of business	X
<p>Inasmuch as the nature of a Building Contractor’s business is such that employing carpenters is essential, this part of the test is <u>not</u> met for UI or WC.</p>					
C	Independently established (UI account and/or other clients before/during/after)	✓			
<p>Even though the Carpenter does not have any employees, he has an established business. Such is demonstrated by the fact he is already registered with VDOL, provides services to many, files tax returns for his business, and advertises regularly. Therefore, this part of the test is met for UI.</p>					

Inasmuch as not all portions of the respective tests are met, worker is the Building Contractor’s employee for UI and WC purposes.



Example B . The Truck Driver

- A freight delivery company hires a driver to deliver freight. The driver uses his own truck.
 - Freight delivery company facts:
 - Has already been found liable and has other workers performing same or similar functions
 - Assigned the route/territory
 - Truck driver facts:
 - Has own truck
 - Delivers freight for others

Example B - The Truck Driver

UI-ABC test (<i>Must meet all 3</i>)			WC "two-part" test – (Must meet both)		
A	Right to Control	X	1.	Right to Control	X
<p>Although the Freight company does not exercise any control over means/manner of Truck driver's work, the Freight company is ultimately responsible for the undamaged delivery of the freight although, it. Therefore this part of the test is not met for UI or WC.</p>					
B	Outside course/places of business	X	2.	Outside course of business	X
<p>Delivering freight is the nature of the Freight company's business and the route/territory is within the places of the Freight company's business. This part of the test is <u>not</u> met for UI or WC.</p>					
C	Independently established (UI account and/or other clients before/during/after)	X			
<p>Although the trucker owns the truck and driver delivers for others, he has no other employees, is not registered, and does not operate like a business. This part of the test is <u>not</u> met for UI.</p>					

As no parts of either test were met, worker is an employee of the Freight company for UI and WC purposes.

Example C . The Catered Event

- A restaurant agrees to cater an event. It hires college students to work as servers, bartenders and to bus for this one night of work.
 - Restaurant facts:
 - Is a sole proprietor liable under the UI program
 - Student Facts:
 - Some students are under 18 and one is the son of the sole proprietor of the Restaurant
 - Some are exchange students and some have J1 VISAs
 - Bartenders
 - Are regular employees of the restaurant

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This example draws in the relationship of an employer who is liable under the unemployment laws, but has wages that are exempt from coverage.

Example C - The Catered Event

UI-ABC test (Must meet all 3)			WC "two-part" test – (Must meet both)		
A	Right to Control	X	1.	Right to Control	X
The Restaurant owner directs and controls the entire event. Therefore this part of the test is <u>not</u> met for UI or WC.					
B	Outside course/places of business	X	2.	Outside course of business	X
Although this is the first catered event, when the Restaurant accepted the event, it became part of the nature of their business. This part of the test is <u>not</u> met for UI or WC.					
C	Independently established (UI account and/or other clients before/during/after)	X			
As none of these workers is liable or reporting to UI, this part of the test is <u>not</u> met for UI.					

J1 VISA holder wages are exempt from UI, but not from WC. The son of the sole proprietor's wages are exempt from UI and from WC provided he lives in the proprietor's home. There is no casual work exception under UI or WC as the work is for the purpose of the restaurant's trade or business. All other workers fail all parts for UI and WC purposes and are the Restaurant's employees.

This example draws in the relationship of an employer who is liable under the unemployment laws, but has wages that are exempt from coverage.



Consequence for Misclassification

- For the past 3 years there has been a huge focus on misclassification
 - Legislative Study group
 - Labor and Employer groups want level playing field
- Last legislative session created new penalties, raise existing penalties and allows for debarment from state contracts for employers who misclassify
- Legislation also mandated reporting instances of misclassification and requires collaborative efforts to share information among state agencies



Misclassification Penalties

Act 142 - 2010 Legislative session

- For UI:
 - Up to \$5,000 penalty for each misclassified worker
 - Up to \$5,000 penalty for a willful misstatement
- For WC:
 - Up to \$20,000 fine for willful misstatement
- For Both:
 - Barred from doing business with the state up to 3 years
- VDOL is in the process of creating policies and rules for administration of misclassification penalty and debarment period



What can I do if I have questions?

- Call VDOL
 - Better to get reporting correct now than to be tagged with penalties upon completion of an investigation. (VDOL will not validate 3/10 reporting against prior quarters)
 - If you have been reporting incorrectly in the past, this must be corrected with filing of the quarter ending 9/30/10 to avoid assessment of misclassification penalty. (Although misclassification penalty can only be applied to quarter 3/10 and after, interest on UI and HC will apply from the due date of each quarter until payment)
- UI Employer Services . 802-828-4344
- WorkersqCompensation Division . 802-828-2286



Field Contacts Areas

■ WC Investigators

- Montpelier: 828-1344
- Burlington: 652-0313
- Rutland: 775-2203

■ UI Auditors

- Bennington: 447-2867
- Middlebury: 652-0328
- Rutland: 786-8806

■ UI Auditors

- Montpelier: 828-1147
- Morrisville: 888-2542
- Barre: 828-4200
- Springfield: 885-1411
- Burlington: 951-5147
- St Albans: 863-7480
- Newport: 334-3303



How do I report suspected fraud?

- Providing complete and accurate information is the first step
 - Name, address, and telephone number (if available) of individual(s) involved
 - Dates and locations work was performed
 - The more information you provide, the better our chances are of finding misclassification
 - Application or reporting forms found at www.labor.vermont.gov .
%Fraud Reporting+under %News+heading on our home page
- Check our website to see if business has a current WC policy
 - Report to us any business that is employing workers and does not have a current WC policy



How do I report suspected fraud?

- Remember ã
 - Information of who filed the report will be kept confidential. Your contact information will only be used in the event we need more information to complete our investigation
 - Unless or until EVERYONE is not only concerned, but acting upon fraud, the underground economy will:
 - continue to erode a fair playing field for businesses and workers alike, and
 - contribute to undermining the economy.



Central Office Contacts

- Stephen Monahan, WorkersqComp and Safety Director
 - stephen.monahan@state.vt.us
 - 802-828-2138
- Tracy Phillips, Unemployment Insurance & Wages Director
 - tracy.phillips@state.vt.us
 - 802-828-4242
- Maria Beede, UC Programs Administrator III
 - maria.beede@state.vt.us
 - 802-828-4254