

# Independent Contractor or Employee?

## *A Review of Federal Guidance*



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## Learning Objectives

- Intro to Misclassifications: Who cares and why?
- Wage & Hour Guidance
- So What Type of Worker Should I Hire
- Ripped From the Headlines: Recent Investigations
- Moving Forward: “To Do’s” for maintaining compliance
- Discussion & Questions

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## Intro to Misclassifications

### Who Cares & Why?

#### What does an independent contractor look like?

Typically, individuals who provide *freelance* professional, creative, or technical services:

- Advisors, editors, experts, interpreters, admin law judges, outside legal counsel, project managers, referees, corporate trainers, consultants, translators
- Screenwriters, graphic designers, photographers, artists, actors, writers, directors, conductors, singers, entertainers
- Web developers, software developers

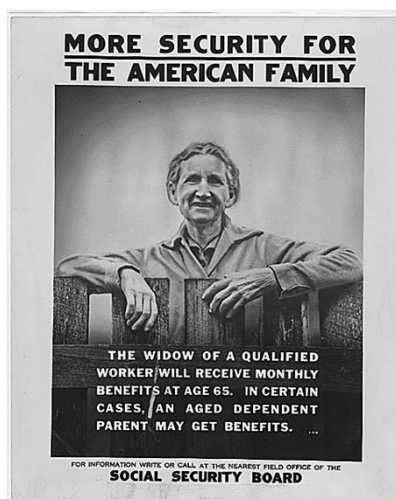
## Intro to Misclassifications

### Who Cares & Why?

#### History...

-In the early 1900s, Congress adopted the employee/independent contractor distinction to define the coverage of New Deal-era statutes designed to protect workers.

-In the early 1990s, the IRS methodically began to look for employers who were misclassifying employees as independent contractors, and has since obtained *billions* of dollars in Social Security back taxes.



## Intro to Misclassifications

### Who Cares & Why?

#### **Employees Treated as Independent Contractors Lose Legal Protections and Benefits**

- Fair Labor Standards Act
- Minimum wage and overtime (if hourly)
  - Participate in benefits programs (non-taxed healthcare; retirement with employer contribution...)
- Social Security Act; Disability Coverage
- Equal Employment Opportunity Commission
- Americans w/Disabilities Act
- Age Discrimination in Employment Act
- Family & Medical Leave Act
- Nat'l Labor Relations Act
  - Right to organize & bargain collectively
  - Job protection under existing CBAs
- Workers' Compensation; Unemployment



## Intro to Misclassifications

### Who Cares & Why?

#### **Employers Misclassifying Employees as Independent Contractors “Cheat” by avoiding:**

- Paying social security, Medicare, federal unemployment tax, other payroll taxes, state unemployment tax (i.e., tax evasion)
- Paying unemployment to individuals
- Covering individuals for on-the-job injuries (WC)
- Paying benefits—retirement, health care, paid sick leave, long-term disability, FMLA, EAP, vacation...
- Protecting against employment discrimination based on protected class
- Compliance with their own internal policies that provide rights/protections to employees
- Having to prove person is eligible to work in US; visa issues



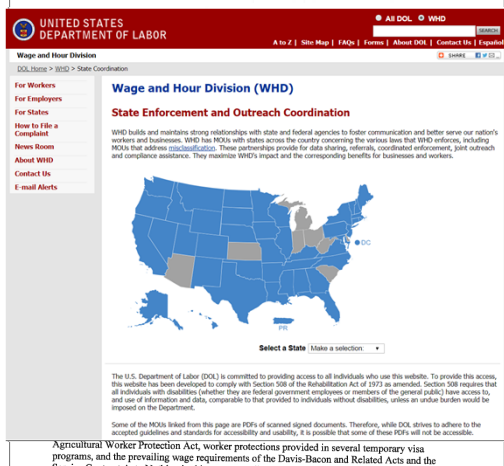
## Intro to Misclassifications

### Who Cares & Why?

And It's Not Just the  
Feds!

In Iowa, Workforce  
Development has staff  
and resources dedicated  
to reducing  
misclassification in Iowa.

We are one of 43 states  
with agreements with  
WHD to collaborate on  
such efforts.



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## Intro to Misclassifications

### Who Cares & Why?



ISU is a large institution that  
has been around for a long  
time. If we were caught  
misclassifying:

- (1) How convincing would  
an ignorance defense be?
- (2) What would this do to  
our reputation?
- (3) What impact would this  
have on the trust of our  
employees? Our  
community?

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## Wage & Hour Guidance

Various federal government agencies and some states have their own tests to determine worker status.

### DETERMINING A WORKER'S STATUS

COURTS TYPICALLY APPLY ONE OF THREE TESTS:

Test	Description	Laws Under Which Test has Been Applied by Courts
<b>Common Law Test</b>	Employment relationship exists if employer has right to control work process, as determined by evaluating totality of the circumstances and specific factors	<ul style="list-style-type: none"> <li>Federal Insurance Contributions Act</li> <li>Federal Unemployment Tax Act</li> <li>Income Tax Withholding</li> <li>Employment Retirement and Income Security act</li> <li>National Labor Relations Act</li> <li>Immigration Reform and Control Act (IRS Test)</li> </ul>
<b>Economic Realities Test</b>	Employment relationship exists if individual is economically dependent on a business for continued employment	<ul style="list-style-type: none"> <li><u>Fair Labor Standards Act</u></li> <li>Title VII</li> <li>Age Discrimination in Employment Act</li> <li>Americans with Disabilities Act</li> <li>Family and Medical Leave Act (likely to apply)</li> </ul>
<b>Hybrid Test</b>	Employment relationship is evaluated under both common-law and economic reality test factors, with a focus on who has the right to control the means and manner of a worker's performance	<ul style="list-style-type: none"> <li>Title VII</li> <li>Age Discrimination in Employment Act</li> <li>Americans with Disabilities Act</li> </ul>

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## Wage & Hour Guidance

### Department of Labor

The Fair Labor Standards Act (FLSA) defines “employ” broadly, as meaning “to suffer or permit to work.” 29 U.S.C. 203(g).

This definition is more expansive than the common law definition of “employee.”



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## Wage & Hour Guidance

### Department of Labor

The employer-employee relationship under the FLSA is tested by “economic reality.”

While “there is no single rule or test for determining whether an individual is an independent contractor or an employee for purposes of the FLSA,” there are six factors which are considered significant.



See DOL Fact Sheet #13: Employment Relationship Under the Fair Labor Standards Act.

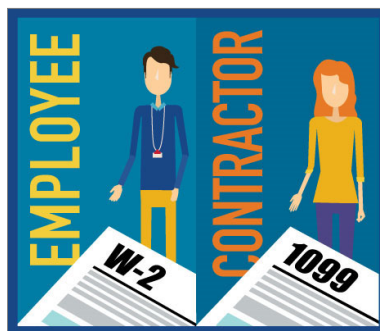
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## Wage & Hour Guidance

### FLSA Guidance

The six factors or questions in the “economic realities” test include:

1. Is the work an integral part of the employer’s business?
2. How permanent is the worker’s relationship to the employer?
3. How does the worker’s relative investment compare to the employer’s investment?
4. What is the nature and degree of the employer’s control?
5. Does the work performed require special skill and initiative?
6. What is the worker’s opportunity for profit and loss?



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## Wage & Hour Guidance

### Economic Realities Test

#### 1. Integral to Business

- A worker who performs the essential work of the business – such as manufacturing the product it sells – is more likely to be classified as an employee.
- A worker who performs tangential work – such as a landscaper performing work for an accounting firm – is more likely an independent contractor.



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## Wage & Hour Guidance

### Economic Realities Test

#### 2. Permanency of Relationship

- Indefinite, ongoing relationships resemble employment.
- Fixed, project-based relationships are more typical of independent contractors.



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## Wage & Hour Guidance

### Economic Realities Test

#### 3. Relative Investment



- If the employer has purchased the necessary tools to get the job done, such as a laptop and specific software, it is more likely the worker is an employee.
- If the worker has purchased those items or is paying office rent, or their own professional licensure or dues, he is more likely an independent contractor.

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## Wage & Hour Guidance

### Economic Realities Test

#### 4. Degree of Control?



- Is the worker told where to do the job, when to do the job, and how to do the job? If yes, they are probably an employee.
- Is the worker given specifications as to the final product, but generally determines how and when to do the work? If yes, they are probably a contractor.
- The degree of control is a small part of the analysis, but is secondary to economic factors.

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## Wage & Hour Guidance

### Economic Realities Test

#### 5. Skill/Initiative Requirement

- The DOL's guidance emphasizes a worker's "business skill, judgment, and initiative" and *not* their technical skills under this factor.



- This language seems to explicitly dismiss any consideration of a worker's technical ability and would focus the analysis solely on the worker's business acumen.

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## Wage & Hour Guidance

### Economic Realities Test

#### 6. Potential for Profit/Loss

- An independent contractor sets the price for the work and can charge as much as the market will bear.
- An employee typically earns an hourly wage or salary, regardless of the business' fortunes.



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## Wage & Hour Guidance

### Internal Revenue Service

The IRS looks at 11 factors within three areas to determine if a worker is properly classified as an employee or an independent contractor:

- Behavioral: Does the business control or have the right to control what the worker does and how the worker does his or her job?
- Financial: Are the business aspects of the worker's job controlled by the payer?
- Type of Relationship: Are there written contracts or employee-type benefits? Will the relationship continue, and is the work performed a key aspect of the business?



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## Wage & Hour Guidance

### Behavioral Control

Whether the business has a right to direct and control the work performed by the worker, even if that right is not exercised.

Employee	Independent Contractor
Instructed when and where to work	Uses own judgment to determine when and where to work
Instructed what tools to use	Uses own tools
Instructed where to purchase supplies and services	Uses own judgment to determine where to purchase supplies and services
Receives more detailed instructions	Receives less detailed instructions
Receives training about procedures and methods to do the job	Uses own methods to do the job

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## Wage & Hour Guidance

### Financial Control

Whether the business has the right to direct or control the financial and business aspects of the worker's job.

Employee	Independent Contractor
Has little to no investment in equipment; typically provided equipment by business	Has significant investment in the equipment used in working for someone else
Less likely to incur unreimbursed expenses	More likely to incur unreimbursed expenses
Has little to no opportunity to make a profit or suffer a loss as a result of the work, other than receiving regular wage amount	Has greater opportunity to make a profit or suffer a loss as a result of the work, aside from the money earned from the project
Cannot seek out new business opportunities	Generally free to seek out new business opportunities; often advertises, maintains a visible business location, and is available to work in the relevant market
Generally guaranteed a regular wage amount for an hourly, weekly or other period of time	Most often paid for the job by a flat fee or, in some professions, hourly

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## Wage & Hour Guidance

### Type of Relationship

How the worker and business perceive their interaction with one another.

Employee	Independent Contractor
Receives insurance, pension plan, vacation and sick leave	Receives no benefits
Expectation that the relationship will continue indefinitely	Expectation that relationship will continue only for a specific project or period
Services performed are directly related to the regular business of the company	Services performed are peripheral to the regular business of the company
Typically works for only one employer	Can work for more than one business at a time
Can quit at any time without incurring liability	Has legal obligation to complete the contract

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## So What Type of Worker Should I Hire?



Consider Hiring an Employee If:

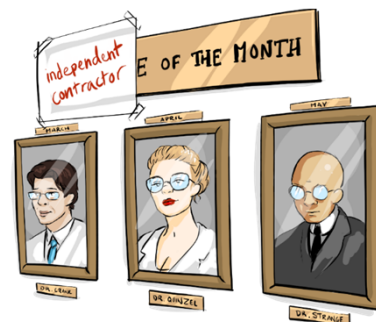
- The work needs to be done under your supervision,
- You want to control the hours of work and the tools and equipment used by the worker,
- This is a long-term need\*, and
- The work is essential to your business and not a peripheral job.

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## So What Type of Worker Should I Hire?

Consider Hiring an Independent Contractor If:

- The work is not central to your business,
- The work can be done by a professional who doesn't need much supervision,
- The work is a short-term project that will be completed in a defined period of time, and
- The worker has the professional expertise or is someone who needs little supervision.



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## Ripped From the Headlines

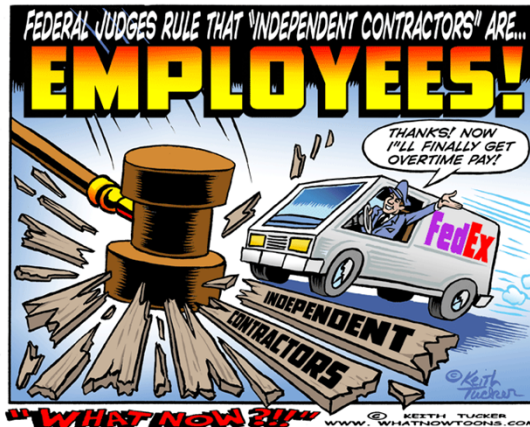
### Recent Investigations

-*Donahue v. Harvard University*

-FedEx (\$228 million settlement – 2015)

-Lowe's (\$10 million settlement – 2015)

-Deja Vu Consulting Inc. (\$6.5 million – 2017)



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## Moving Forward

### The Bottom Line

- An agreement between an employer and a worker designating or labeling the worker as an independent contractor is *not relevant* to the analysis of the worker's status.
- State and federal agencies will presume the person is an employee. The burden is on the employer to show that's not the case.
- State and federal agencies are driven to protect workers from misclassification, thus stripping them of overtime pay and other protections.



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## Moving Forward To Do's for Maintaining Compliance

- ✓ Evaluate all existing “independent contractor” relationships
- ✓ Review any impacted policies or procedures
- ✓ Review any template or commonly used written agreements
- ✓ Train/Retrain impacted staff, as needed
- ✓ Assure checks/balances for any newly proposed independent contractor relationships (need several layers of review)



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## Discussion? Questions?



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