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**Independent Contractors vs. Employees: Government Agencies Are Cracking Down on Worker Misclassification**

By David L. Weinstein and Elizabeth Ann Peters

The proper classification of workers as independent contractors or as employees is among the most important issues facing employers today. Proper classification determines a company’s obligations with respect to issues ranging from minimum wage and overtime requirements, payroll taxes, benefit plan eligibility, workers’ compensation, unemployment benefits, immigration documentation and potential exposure under workplace discrimination laws. This article discusses recent enforcement efforts in Illinois and the tests applied by various governmental agencies to determine whether a worker is properly classified as an independent contractor or as an employee.

**Recent Enforcement Efforts in Illinois**

Government agencies often take the view that employers willfully misclassify their workers as independent contractors in order to avoid obligations under state and federal labor laws. Misclassification is alleged to unfairly limit workers’ access to workers’ compensation, unemployment assistance, employee benefits, fair wages and the protection of laws prohibiting employment discrimination. Moreover, misclassification reduces unemployment insurance and workers’ compensation contributions collected from employers. Willful or not, worker misclassification results in a loss of revenue to the state and federal government, and enforcement agencies are cracking down.

The Illinois Department of Labor (“IDOL”) and Attorney General Lisa Madigan have announced plans for increased enforcement of the Illinois Employee Classification Act (“ECA”), 820 ILCS 185/1-999. The ECA focuses on misclassification in the construction industry. It creates a rebuttable presumption of employment for workers performing services for construction contractors on or after January 1, 2008. In cases of misclassification, IDOL may assess civil penalties and must notify the Illinois Department of Employment Security, the Department of Revenue and the Workers’ Compensation Commission. These agencies are then required to assess the contractor’s compliance under the laws they administer. The ECA also allows misclassified employees to sue their employers for lost wages and benefits, liquidated damages, compensatory damages, costs and attorney fees.

Attorney General Madigan recently settled a suit against five Chicago-area construction firms who allegedly misclassified their employees as independent contractors in violation of the ECA, the Illinois Whistleblower Reward and Protection Act, and the Illinois Consumer Fraud and Deceptive Business Practices Act. Under the settlement, each company must pay more than $79,000 and is barred from participating in government contracts for four years.

The Illinois Department of Employment Security (“IDES”) is also ramping up enforcement of the Illinois Unemployment Insurance Act. Some companies have received communications from IDES regarding audits and assessment of past-due unemployment insurance contributions for allegedly misclassified employees. These audits are often triggered by complaints from disgruntled workers or unemployment benefit claims filed by independent contractors whose contracts have been terminated.

**Determining Whether a Worker is Properly Classified as an Independent Contractor**

It is often difficult to determine whether a worker is properly classified as an independent contractor because governmental agencies have varied interpretations of the proper classification standards. Given the same fact pattern, one agency might find a worker to be an employee, while another agency finds the worker to be an independent contractor. The classification issue is further complicated by the refusal of some governmental agencies to accept another agency’s conclusions about the proper classification of a company’s workers.

It is important for employers to realize that the existence of an independent contractor agreement, by itself, is not determinative of a worker’s status. There are multiple relevant factors, including the degree of control the company has over the worker and the entrepreneurial nature of the worker’s business. Because there is no universal test, employers should strive to satisfy as many conditions as possible to make it clear that a worker is properly classified as an independent contractor. The following are examples of tests employed by certain government agencies.

**IRS 20 Factor Test**

http://www.wildman.com/bulletin/100609a/
The IRS employs a 20 factor test to determine independent contractor status under the Internal Revenue Code. These factors generally relate to evidence of behavioral and financial control and the nature of the worker's relationship with the employer. The twenty factors are:

1. Whether the worker is required to follow the company’s instructions.
2. Whether the company provides training to the worker to accomplish the work.
3. Whether the worker's services are integrated into the company’s regular business.
4. Whether the company requires that the worker perform the services personally, as opposed to assigning work to others.
5. Whether the company hires, supervises and pays the worker's assistants.
6. Whether there is a continuing relationship between the company and the worker.
7. Whether the company sets the worker's hours.
8. Whether the company requires the worker to work full-time.
9. Whether the worker works at the employer's place of business.
10. Whether the company sets the order or sequence of the worker's work.
11. Whether the worker is required to provide oral or written status reports to the company.
12. Whether the worker is paid by the hour, week or month, rather than upon completion of the project.
13. Whether the worker is reimbursed for business or travel expenses.
14. Whether the company provides the employer with tools and materials.
15. Whether the worker has made a significant investment in performing the services.
16. Whether the worker can realize a profit or loss.
17. Whether the worker works for more than one company at a time.
18. Whether the worker makes the services available to the general public.
19. Whether the company has the unilateral right to discharge the worker.
20. Whether the worker has the right to terminate the relationship without being liable under contract.

**Illinois Unemployment Insurance Act “ABC” Test**

The Illinois Unemployment Insurance Act outlines a three part test, known as the “ABC” test, to determine whether a worker is properly classified as an independent contractor. Under the “ABC” test, a worker is an employee unless:

- The worker is free from control or direction over the performance of the services, both under contract and in fact; AND
- The services are either outside the usual course of business of the company, or is performed outside the company's place of business; AND
- The worker is engaged in an independently established trade, occupation, profession, or business.

820 ILCS 185/1-999. IDES regulations list a number of factors IDES considers in evaluating whether each part of the “ABC” test is satisfied. Recently, particular emphasis has been placed on part C of the test, and IDES auditors have indicated that, regardless of any other factors, they will presume that a worker is an employee if the worker performs services for only one company.

The Illinois Appellate Court recently decided *Veterans Messenger Service, Inc. v. Jordan*, upholding IDES’ determination that couriers were employees of a delivery brokerage service. No. 1-08-004, (1st Dist., Ill. App., Aug. 3, 2009). Veterans Messenger Service contracted with the couriers to carry out delivery orders for its customers. Despite the fact that the couriers controlled the manner of their work, set their own hours, hired their own helpers, were free to reject any deliveries offered by dispatchers, and were free to perform delivery services for others, the court found that they were properly classified as employees under the Illinois Unemployment insurance Act. The court focused on part C of the "ABC" test, emphasizing that the couriers did not make their businesses available to the general public, reported no wages of any workers they hired to IDES, did not maintain business listings in phone directories or trade journals, and made no payments for courier licenses to any common carrier authority in their own names.

**Illinois Employee Classification Act Test**

The independent contractor test outlined in the ECA is very similar to the Unemployment Insurance Act “ABC” test. Under the ECA, a worker is properly classified as an independent contractor where the "ABC" test is satisfied, OR where the worker is deemed to be a legitimate sole proprietor or partnership. A sole proprietor or partnership performing services for a contractor as a subcontractor is deemed legitimate if it is shown that:

1. the sole proprietor or partnership is performing the service free from the direction or control over the means and manner of providing the service, subject only to the right of the contractor for whom the service is provided to specify the desired result;
2. the sole proprietor or partnership is not subject to cancellation or dissolution upon severance of the relationship with the contractor;
3. the sole proprietor or partnership has a substantial investment of capital in the sole proprietorship or partnership beyond ordinary tools and equipment and a personal vehicle;
4. the sole proprietor or partnership owns the capital goods and gains the profits and bears the losses of the sole proprietorship or partnership;
5. the sole proprietor or partnership makes its services available to the general public or the business community on a continuing basis;
6. the sole proprietor or partnership includes services rendered on a Federal Income Tax Schedule as an independent business or profession;
7. the sole proprietor or partnership performs services for the contractor under the sole proprietorship’s or partnership’s name;
8. when the services being provided require a license or permit, the sole proprietor or partnership obtains and pays for the license or permit in the sole proprietorship’s or partnership’s name;
9. the sole proprietor or partnership furnishes the tools and equipment necessary to provide the service;
10. if necessary, the sole proprietor or partnership hires its own employees without contractor approval, pays the employees without reimbursement from the contractor and reports the employees’ income to the Internal Revenue Service;
11. the contractor does not represent the sole proprietorship or partnership as an employee of the contractor to its customers; and
12. the sole proprietor or partnership has the right to perform similar services for others on whatever basis and whenever it chooses.

820 ILCS 185/10.

Avoiding Liability for Worker Misclassification

To avoid costly penalties, past-due contributions, back wages, back benefits and other potential exposure, companies should carefully review their worker classifications to ensure compliance with applicable laws. Many companies conduct their own internal audits to confirm whether their workers are properly classified and correct any inadvertent misclassification—before governmental enforcement agencies knock at the door.

We are happy to assist you in conducting such audits or in dealing with any of the various governmental agencies in the event you receive notice that they will be visiting your business or that an independent contractor has filed a claim asserting that you are the employer. Please feel free to contact your primary attorney at Wildman Harrold; or David L. Weinstein at (312) 201-2685 or at weinstein@wildman.com; or Elizabeth A. Peters at (312) 201-2644 or at epeters@wildman.com in Wildman Harrold’s Employment & Labor Practice.