

5 BIGGEST HR MISTAKES SMALL BUSINESSES MAKE AND HOW TO FIX THEM



About This Guide

Running a small business is both exciting and rewarding. But keeping up with all the latest employment laws can be complicated. The last thing you want to do is put your business at risk by making a mistake that could result in costly legal fees or fines.

What's the best way to avoid serious consequences? First, you have to know what to look for — the “red flags” that indicate you may not be following the law. Then you can take steps to correct any situations that could lead to trouble.

In this e-guide, we'll take a look at these five common HR mistakes:

- 1 Treating independent contractors like employees**
- 2 Practicing “accidental” discrimination when hiring**
- 3 Not properly verifying work eligibility (via I-9 forms)**
- 4 Putting employees who don't legally qualify on salary**
- 5 Not displaying all required labor law postings**

Each section will cover why these laws matter, how to identify whether you have a potential problem, and what immediate steps you can take to address them.

Let's get started!

MISTAKE #1:

Treating Independent Contractors Like Employees

Hiring an independent contractor is a common way to expand business productivity without adding overhead. Maybe you only need temporary help for a short-term project or during a busy season. Perhaps you want to avoid having to lay anyone off if business slows down again. There's nothing wrong with that. In fact, financially, it may be a very smart business move.

Just don't make the mistake of treating independent contractors like employees. Legally, independent contractors and employees are very different, and the distinctions go beyond a W-2 or 1099.

You can't call a worker an independent contractor if he or she meets the state or federal government's definition of an employee. The guidelines are complex and can vary state by state.

But keep in mind that government agencies and laws tend to favor the employee classification. For you, that could mean paying back taxes and fines if the government decides you misclassified an employee as an independent contractor.

ComplyRight Tip

You may use different terms to describe independent contractors — such as “freelancers,” “project workers” or even “1099ers.” The one thing you should never call a contractor is a “1099 employee.”

There is no such thing as a 1099 employee, and using that term indicates you don't recognize the distinction. .

Don't make the mistake of thinking it doesn't really matter. From the IRS to the Department of Labor (DOL), government agencies are cracking down on this kind of misclassification.

Why do government agencies care?

Taxes are the main reason. It's harder for those agencies to collect employment taxes from independent contractors than employees. Plus, billions of dollars in Social Security and workers' compensation taxes go unpaid when employees are misclassified as contractors.

DID YOU KNOW?

Approximately 30% of audited businesses have misclassified employees as independent contractors (intentionally or not).

Workers' rights are another. The legal rights of workers — such as minimum wage, family and medical leave, overtime pay and civil rights protections (e.g., discrimination) — may be sidestepped when employers misclassify workers as contractors.

And the penalties for misclassifying of employees can add up quickly. To start, you may have to pay back taxes totaling as much as 41.5% of the contractor's wages going back three years and FICA payments totaling 100% of the employer's portion plus 40% of the employee's portion.

You also could face fines amounting to 1.5% of wages not withheld from income tax, .5% of unpaid tax liability, and \$50 for each failure to file a W-2 or obtain a Social Security number.

If the IRS believes you intentionally misclassified workers, it may also seek criminal penalties that can carry fines up to \$100,000 and up to five years in jail.

Red Flags

What are some of the signs that your contractor should really be considered an employee? A key factor is typically the amount of control you have over how the worker does the job.

An independent contractor is responsible for delivering a certain result, but he or she decides how to achieve that result. With employees, on the other hand, you can tell them what to do, when to do it and how to do it.

Some Other Red Flags Include:

- **The worker performs core business services.** Contractors provide supplemental services that aren't an integral part of your business. For example, if you have a car-detailing company and hire a graphic design contractor to create signs, that work is not core to your business. But if you run a graphic design company, and use contractors to do the design work, that could potentially be a problem.
- **You manage the worker hands-on.** If someone in your company manages the worker's role day to day, that is a sign the contractor is really an employee. Contractors typically work independently and don't require hands-on management from their clients.
- **You set specific hours for the worker.** Contractors generally set their own hours and are paid for a project or result, not for being on the clock. If you require the contractor to work specific hours, or stick to a schedule, you may be within the confines of employee status.
- **The contractor works full time at your office or for your business.** Independent contractors typically work with more than one client. If your contractor is only working for you, and does so at your workplace, that could be an indicator that he or she would be considered an employee under the law.
- **You provide the equipment the worker uses.** Independent contractors use their own tools, equipment and supplies to perform the job. If you're providing a computer, blowtorch or delivery truck, chances are good the IRS will see your worker as an employee.

- **The relationship is open-ended.** A job with no clear scope or deadline signals an employee relationship rather than a contract arrangement. Contractors work on a temporary basis (it can be long-term) and usually have a signed agreement stating the terms and deliverables.
- **The worker doesn't provide an Employer Identification Number (EIN).** If the contractor provides a SSN, rather than a business EIN for tax purposes, it signals employee standing to the IRS. Independent contractors should be business owners with the appropriate tax status.
- **The worker is being paid from a payroll account.** A contractor should be treated as a vendor with invoices paid under accounts payable.
- **The worker does not assume profit-and-loss risk of a business.** Contractors assume some risk in accepting a job in which they may either make a profit or suffer a loss. They also likely pay their own business expenses and advertise their services in some way.

How to Fix It

Did any of the red flags listed above concern you? If so, take steps now to remedy your situation before the IRS comes knocking. Here are some practical tips for how to make positive changes.

- Work with independent contractors that have a business name and EIN.
- Use an “Independent Contractor Agreement” with an end date signed by both parties.
- Define a scope of work and establish deliverables or milestones up front with a delivery date.
- Require the independent contractor to use his or her own equipment, supplies and helpers.



- Set up the independent contractor as a vendor and require him or her to submit invoices.
- Pay the contractor's invoices out of an accounts payable account.
- Issue a 1099 (not W-2) at year-end.
- Don't use the same contractor for indefinite periods of time.
- Hire employees to perform core business functions.

Remember, many state laws presume workers are employees and make it the employer's responsibility to show that contractors are truly independent. When in doubt, treat workers as employees by putting them on payroll and withholding the proper taxes.

MISTAKE #2:

Practicing “Accidental” Discrimination When Hiring

Discrimination is not always intentional. It may not be the result of overt prejudice or a conscious desire to favor one type of person over another. Sometimes subconscious bias can affect the screening process and final decision. This kind of unintended discrimination can be just as damaging, and could even lead to lawsuits.

Granted, hiring inherently requires some amount of subjective decision-making.

- Does the candidate have strong communication skills?
- Does the candidate have a good work ethic?
- Is the candidate strong enough to do the physical work required?
- Will the candidate be a good cultural fit for the business?

In making those assessments, it's essential to stick to what matters for the position being filled. Small talk and “off the cuff” interview questions can be landmines — whether or not the information gathered is used in the decision-making process. Avoiding the perception or appearance of discrimination is critical. Otherwise you run the risk of an Equal Employment Opportunity Commission (EEOC) discrimination claim or lawsuit from a rejected candidate.

Inappropriate job requirements can also spark discrimination claims by inadvertently discriminating against a certain gender or legally protected group. For example:

- Setting height, weight or strength requirements that are not absolutely essential to perform the job duties (and disqualify certain people unfairly)

- Requiring employees to be available to work any day of the week (making it impossible for people of certain religions to comply)
- Dress code or grooming requirements that conflict with religious practices

Do you have any hiring practices in your company that could put you at risk for a discrimination lawsuit?

Red Flags

Certain interview and hiring processes open your company up for discrimination claims. To avoid accidental discrimination, look out for these risky practices.

- Hiring decisions made primarily on “gut” rather than specific criteria
- Vague job descriptions or ads that do not clearly define requirements (such as training/education, certifications, skills, physical requirements, years of experience, etc.)
- Job requirements that are not essential to the doing the actual job (for example, including “ability to lift 50 pounds” when the job only calls for lifting 20 pounds, or requiring a college degree when it’s not typical for that sort of position)
- Inconsistent interview questions for the same position
- Inconsistent pre-employment testing for the same position
- Excessive “small talk” or personal questions in interviews
- Hand-written notes made on resumes or job applications (such as “heavy accent,” “salt-and-pepper hair” or “no Saturdays due to religion”)

ComplyRight Tip

Don’t review the application as the applicant is sitting across the desk from you. Interview the candidate only after you’ve scrutinized the application, compared it to the job description and requirements, and identified the questions that remain unanswered.

How to Fix It

In addition to creating a job description that accurately reflects a position's responsibilities and requirements, take steps to make sure your hiring paperwork is compliant.

- 1. Formalize the hiring process.** Establish a consistent application and interview process. Prepare thorough job descriptions for each position based on the essential functions needed to perform the work. Use legally sound job applications that comply with state laws. If you require testing for a position, be sure all applicants take the same test.
- 2. Prepare written interview questions.** Avoid small talk and any potentially discriminatory questions, such as "Are you a citizen?" or "How old are you?". Develop questions based on the essential job functions. Be sure to use the same questions for all applicants. (Your follow-up questions can be different, however, depending on each interviewee's responses or the specific gaps you identify in each individual's application.)
- 3. Focus interview questions on ability, not lifestyle or beliefs.** Ask questions that assess a candidate's ability to perform essential job functions. You can ask about interpersonal skills and self-motivation, but avoid asking a candidate personal questions such as, "Do you plan to have kids?" If physical ability to perform aspects of a job is important, be sure to ask all candidates if they can perform the job functions, not only those who appear disabled or physically different.
- 4. Document all answers.** Write notes about each candidate's responses, but keep the notes separate from the resume or application (which must be kept on file by law). Avoid writing comments that could be seen as prejudicial (such as "wears burka") even if the purpose is just to jog your memory when interviewing multiple



candidates. Your notes will be useful in case of discrimination accusations, but they are also important for helping you make sound hiring decisions.

5. **Team up in interviews.** Never let inexperienced people interview alone. And, no matter your amount of interview experience, it's always a good idea to invite another colleague to sit in the interview with you. Having additional witnesses is valuable if you are ever accused of discrimination. Train all who hire or interview on the points listed above.
6. **Review your notes about qualifications.** Referencing notes about each candidate's abilities or qualifications for the listed job requirements helps ensure your decision is based on specific criteria and not subjective impressions. When possible, compare your notes with those of other team members who interviewed the same candidates before making a final selection.
7. **Record your decisions.** Document your reasons for selection (or not) based on each candidate's qualifications.

Keep in mind that the statute of limitations to file a complaint of discrimination is 180 days from the date of the incident. It can, however, be extended to 300 days in some circumstances. To be safe, keep all your hiring paperwork, including resumes and interview notes, for one year after a position is filled. Then it's a best practice to discard.

MISTAKE #3:

Not Properly Verifying Work Eligibility (I-9)

It's against the law for any employer to knowingly hire employees who are not authorized to work in the United States. That doesn't mean your employees have to be U.S. citizens — it means they must be legally authorized to work here.

You're required to have a properly completed I-9 Employment Eligibility Verification Form on file for every new hire, regardless of citizenship. All employees must provide proof that they are eligible to be employed in the United States.

Some of the requirements can be confusing. After all, the I-9 Form guidelines include 15 pages of employee instructions and a 65-page employer handbook. Your responsibilities include keeping accurate records for the period required by law, as well as using the most updated version of the I-9 form.

DID YOU KNOW?

You are more likely to be audited if you're in an industry that depends heavily on immigrant labor, such as food services, hospitality, agriculture or construction.

Not checking appropriate documentation from new employees means you can be fined between \$216 and \$2,156 for each violation. Government agencies have been stepping up enforcement. Even small companies can be targeted based on complaints or tips.

Red Flags

Are your I-9 forms in perfect order? To avoid being caught in a legal predicament, consider whether your business is guilty of any of these potential problems.

- I-9 forms kept in individual employee files, and not in separate, centralized location
- Missing or incomplete I-9 forms
- I-9 forms kept indefinitely, even after employees leave
- Inconsistent document verification process
- No process for updating expired documents

How to Fix It

- **Ensure all new hires complete I-9 forms.** Every employee, whether or not you know their legal status (such as in the case of a family member), must complete a Form I-9 by the first day of work. You have until day three to complete the employer section and inspect documentation.
- **Centralize your I-9 records. Keep all I-9 forms in one place, separate from other employee records.** This makes it easier to conduct internal audits and is also a best practice in case of an ICE investigation.
- **Audit your files regularly.** Schedule periodic reviews to make sure your I-9 forms are complete and accurate.
- **Make necessary corrections.** If you find any missing information on an I-9 form, correct it right away. Initial and date any changes or additions. Never use corrective fluid (“white out”) or backdate a Form I-9.

ComplyRight Tip

As immigration rules are tightened and enforcement is increased, Form I-9 is subject to frequent changes. Be sure to use the most recently issued version of the form when onboarding each new hire. Or, consider an electronic I-9 solution that guarantees you will always have the most recent form at hand.

- **Remember to reverify expired documents.** In some cases, work authorization is temporary. When onboarding an employee who presents documentation that expires, set a reminder in your calendar to request updated documentation before the expiration date. (Reverifying documentation is not required for U.S. citizens or permanent residents.)
- **Discard documents that are not required.** Discard I-9 forms that are more than three years past an employee's date of hire or one year past termination date, whichever comes later.



ComplyRight Tip

You must keep I-9 forms on file for at least three years from the date of hire, or one year after employment ends, whichever is longer. Simply put, this means you should have an I-9 on file for all current employees as well as all employees who have left your company within the past year.

MISTAKE #4:

Putting Employees Who Don't Qualify on Salary

In everyday terms, employees are typically categorized as “hourly” or “salaried.” Hourly employees are those who are paid by the hour and are entitled to overtime pay when they work more than 40 hours in a week. Salaried employees, on the other hand, are paid a fixed amount, regardless of the number of hours worked each week.

For employers, paying employees a salary certainly makes things easier, administratively speaking. After all, salaried employees don't have to track hours, and their employers don't have to calculate pay each week based on hours worked and overtime earned. Paying a salary also helps employers to eliminate overtime costs and normalize payroll expenses week to week. As a result, many employers prefer to pay a salary. However, this practice is illegal unless the salaried employees are legitimately considered “exempt” from overtime pay under the law.

The problem is that the rules for exemption are complex and easily misinterpreted. In fact, by some estimates, 70%-90% of employers get it wrong. Employees themselves are often unaware of these rules and may accept a salaried pay option for a job that doesn't qualify as exempt — until they discover the error and make the acquaintance of an eager attorney.

The risks for getting this critical classification wrong include fines, back wages and attorney fees.

Under the Federal Labor Standards Act (FLSA), an employee can be considered exempt based on two factors: (1) compensation and (2) Department of Labor (DOL) “job duties” tests.

First, exempt employees must receive a minimum of \$455 a week (\$23,660 annually) on a fixed salary basis. If you have employees who make less than that, they are generally considered non-exempt and eligible for overtime pay (regardless of their job duties).

With respect to job duties, exempt employees generally fall into one of three defined categories listed below. An exempt employee must pass every requirement under one of the DOL job duties tests. The tests are quite complicated, but these are the main points:

- **Executive Exemption Test:** The employee must manage a team or department, direct the work of two or more employees, and have authority to hire and fire.
- **Administrative Exemption Test:** The employee must perform non-manual work, manage “back-office” general business operations, and have decision-making authority on significant matters.
- **Professional Exemption Test:** The employee must perform tasks requiring advanced knowledge, have advanced education or special training, and be specialized in a field of science or learning.



If you have employees who don't pass either one of these tests, they should be categorized as non-exempt (paid hourly + overtime). Again, the only way an employee can be exempt from overtime is if he or she makes the minimum salary and passes every criterion of one of the DOL tests.

Red Flags

What are the signs that you may be crossing the line when it comes to paying employees a salary? Here are some indications that your categorization may be suspect:

- Everybody's exempt and on salary, including administrative and entry-level employees.
- Employees are exempt based on title, not actual job duties.
- Workers with similar job duties are paid differently (some salary, some hourly).
- Exempt employees are frequently required to work overtime.
- Exempt employees are micromanaged.

How to Fix It

If you're concerned you may have compliance issues regarding exempt and non-exempt employees, take the time to review your employee job descriptions and consider reclassifying them. Follow these tips:

- Write a thorough job description for each employee or distinct role.
- Reclassify each person or role based on actual assigned job duties (not titles).
- If in doubt, pay hourly plus overtime — you can never be wrong with this approach.
- Implement formal policies to control overtime expenses.



ComplyRight Tip

Where allowed by law, paying employees a salary offers certain benefits, including simplified recordkeeping and more predictable payroll expense. Just keep in mind that paying a salary is always optional for the employer, and choosing to pay a legally exempt employee by the hour (with overtime where earned) is never illegal.

MISTAKE #5:

Not Displaying Required Labor Law Postings

You probably know that certain workplace posters are required by various government agencies. But you may not be aware that many cities and counties now require employee postings, or how frequently employee postings can become outdated these days.

Keeping up with ever-changing labor law posting requirements can be a huge burden for small businesses. The postings are issued by multiple federal, state and local agencies, and there is no “one stop” government resource for full posting compliance. Plus, laws change frequently and the agencies don’t notify employers when the posters need to be updated. The burden is completely on you to stay current.

Not doing so can mean fines from the various agencies. But the bigger risk is employee lawsuits. Missing or outdated postings weaken your case if you are sued, and can even extend the statute of limitations, giving employees more time to file in the first place.

That’s why it’s important to stay up to date on posting regulations.

DID YOU KNOW?

The purpose of workplace postings is to inform employees of their legal rights and responsibilities under federal, state and local laws. As a U.S. employer, you’re responsible for giving all your workers access to this important information. Not doing so can result in fines and, more significantly, can extend the statute of limitations for certain employment lawsuits.

Red Flags

What are some signs that you may not be in compliance with current posting regulations? Here are a few to watch out for:

- No employment law postings in your common area(s)
- Obviously old or outdated postings (for example, incorrect minimum wage or a print date older than a couple of years)
- No state postings (some states have as many as 15 mandatory posters)
- You have not updated postings for more than a year
- You operate multiple work locations but have only one set of posters

How to Fix It

If any of the red flags above apply to you, the obvious solution is to update all of your postings immediately. You might consider an automatic poster replacement service to keep you on top of updates and new regulations. Look for a service that guarantees compliance with all federal, state and local posting laws.

Conclusion

Keeping your business compliant with the multitude of employment laws can be tricky. You not only have to stay on top of changing regulations, but also have to implement processes within your company that ensure laws are followed. That may mean scheduling regular audits of your employment files, monitoring interview procedures, reviewing employee payroll statuses, and checking posters to ensure updates have been made.

Finding the right partner to help you manage the process can offer peace of mind. [ComplyRight](#) offers practical, affordable tools that can help you solve any HR challenge at hand. Whatever comes your way, you'll find the solution you need to stay in control and in compliance, with full confidence and minimum effort.

From HR to labor law to tax solutions, ComplyRight has you covered with tools and resources that ease your compliance burden, help you manage your employees and keep your records up to date.