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Director - Member Programs

Alexandria, Virginia 22314

Re: Beware the Independent Contractor Classification

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Businesses across the nation are faced with increasing federal and state legal challenges to their classification determinations that workers are “independent contractors” rather than “employees.”

Your member-businesses should be aware that the Obama Administration is committed to a legislative and administrative agenda that narrowly interprets independent contractor status. Whether viewed as a payback to President Obama’s union and plaintiff lawyer supporters or as an effort to cure systemic misclassification of “employees” as “independent contractors,” the impact on employers will be problematic. Note carefully the following proposed laws that are moving through Congress at this time.

Independent Contractor Proper Classification Act (“ICPC”): The ICPC, if enacted, would, *inter alia*, allow the IRS to develop a process for workers to demand an evaluation of their independent contractor classification to verify its propriety. ICPC would invite individuals classified as independent contractors to challenge that status. Additionally, ICPC would impose new obligations on the U.S. Department of Labor (“DOL”) to review the employer’s independent contractor classification decisions under federal wage and hour laws. ICPC would also require employers to pay a misclassified employee's attorney's fees and expert witness fees.

The stakes are high, because misclassification of “employees” as “independent contractors” makes them ineligible for employee benefits and overtime pay, and results in the employer’s nonpayment of employment taxes. The classification of workers as independent contractors typically removes them from the protections of most labor and employment laws, and insulates these individuals from union organizational efforts. The damages available to remedy such violations and to make employees “whole” can create enormous liability. Punitive, liquidated, other special damages that are available for misclassification under particular federal and state laws further incentivize litigation in this area.

Employee Misclassification Prevention Act (“EMPA”): The EMPA, another proposed law before Congress that was co-sponsored by then-Senator Obama and Senator Ted Kennedy, would amend the Fair Labor Standards Act “to require employers to keep records of nonemployees who perform labor or services for remuneration and to provide a special penalty [double liquidated damages and fines of up to \$10,000.00 for each violation] for employers who misclassify employees as non-employees, and for other purposes.” As with ICPC, EMPA would require employers to inform workers of their right to challenge their employer’s contractor classification, while also requiring DOL to ensure that at least 25 percent of the employer audits conducted by its Wage and Hour Division focus on the possible misclassifications of employees as independent contractors.

Going Forward: While ICPC and EMPA have yet to be enacted into law, the warning message to employers from the Obama Administration as to its sympathies and enforcement posture under current law is clear and unmistakable.

- Decisive action in this area is recommended, and employers utilizing independent contractors should immediately undertake an in-depth review and verification of all contractor status determinations to ensure that those individuals, in fact, are “contractors” and not “employees.”
- In conducting that internal analysis, note that each labor and employment (and other statute) that may come into play in this area has its own particular test for “contractor” status, although there are similarities in the required analysis under these laws.

This Firm has counseled many employers and trade groups as to the key criteria that determine legitimate independent contractor status, and we would be available to provide guidance to your membership in this area. Feel free to contact ----- of my office at 202-338-2172 if you would like to arrange a seminar on this topic.

Note: To ensure compliance with requirements imposed by the IRS, be advised that no U.S. federal tax advice is contained in this document, which, in any event, is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing, or recommending to another party any transaction or matter addressed herein.