

Personal Service Contracts – Employee vs. Independent Contractor

- Why it is important to know and understand the difference
- Recognize the realities of the relationship and correctly classify the worker





- A whole host of Employer obligations flow from a worker's status as an employee:
- Workers Compensation
 - Unemployment
 - Tax withholding
 - Minimum wage and overtime compensation
 - Indemnity obligations



- The realities of an employment relationship determine a worker's status
 - You cannot simply make someone an independent contractor by attaching a label in a contract



- A worker's status as an employee or independent contractor is not a singular determination
 - An individual may be an independent contractor for purposes of some legal requirements and an employee for other purposes

So-called Common Law Test

- Focus is on the employer's right to control the means and manner of performance
- Extensive list of factors that aide in determining the extent to which there is a right of control



Common Law Test

- (1) Instructions. A person who is required to comply with other persons' instructions about when, where, and how the person is to work is ordinarily an employee. This control factor is present if the person or persons for whom the services are performed have the right to require compliance with instructions.
- (2) Training. Training a person by requiring an experienced employee to work with the person, by corresponding with the person, by requiring the person to attend meetings, or by using other methods, indicates that the person or persons for whom the services are performed want the services performed in a particular method or manner.
- *(3) Integration. Integration of the person's services into the business operations generally shows that the person is subject to direction and control. When the success or continuation of a business depends to an appreciable degree upon the performance of certain services, the persons who perform those services must necessarily be subject to a certain amount of control by the owner of the business.
- (4) Services rendered personally. If the services must be rendered personally, presumably the person or persons for whom the services are performed are interested in the methods used to accomplish the work as well as in the results.
- (5) Hiring, supervising, and paying assistants. If the person or persons for whom the services are performed hire, supervise, and pay assistants, that factor generally shows control over the persons on the job. However, if one person hires, supervises, and pays the other assistants pursuant to a contract under which the person agrees to provide materials and labor and under which the person is responsible only for the attainment of a result, this factor indicates an independent contractor status.



Common Law Test

- *(6) Continuing relationship. A continuing relationship between the person and the person or persons for whom the services are performed indicates that an employer-employee relationship exists. A continuing relationship may exist when work is performed at frequently recurring although irregular intervals.
- (7) Set hours of work. The establishment of set hours of work by the person or persons for whom the services are performed is a factor indicating control.
- (8) Full time required. If the person must devote substantially full time to the business of the person or persons for whom the services are performed, such person or persons have control over the amount of time the person is able to do other gainful work. An independent contractor, on the other hand, is free to work when and for whom the person chooses.
- (9) Doing work on the premises of the person or persons for whom the services are performed. If the work is performed on the premises of the person or persons for whom the services are performed, that factor suggests control over the person, especially if the work could be done elsewhere. Work done off the premises of the person or persons receiving the services, such as at the office of the worker, indicates some freedom from control. This fact by itself does not mean that the person is not an employee. The importance of this factor depends on the nature of the service involved and the extent to which an employer generally would require that employees perform such service on the employer's premises. Control over the place of work is indicated when the person or persons for whom the services are performed have the right to compel the worker to travel a designated route, to canvass a territory within a certain time, or to work at specific places as required.

Common Law Test

- (10) Order or sequence set. If a person must perform services in the order or sequence set by the person or persons for whom the services are performed, that factor shows that the person is not free to follow the person's own pattern of work but must follow the established routines and schedules of the person or persons for whom the services are performed. Often, because of the nature of an occupation, the person or persons for whom the services are performed do not set the order of the services or set the order infrequently. It is sufficient to show control, however, if such person or persons retain the right to do so.
- (11) Oral or written reports. A requirement that the person submit regular or written reports to the person or persons for whom the services are performed indicates control. By contract, however, parties can agree that services are to be performed by certain dates and the persons performing those services can be required to report as to the status of the services being performed so that the person for whom the services are being performed can coordinate other contracts that person may have which are required in the successful total completion of a particular project.
- (12) Payment by hour, week, month. Payment by the hour, week, or month indicates an employer-employee relationship, provided that this method of payment is not just a convenient way of paying a lump sum agreed upon as the cost of a job. Payment made by the job or on a straight commission generally indicates that the worker is an independent contractor.
- (13) Payment of business or traveling expenses, or both. If the person or persons for whom the services are performed ordinarily pay the person's business or traveling expenses, or both, the person is an employee. An employer, to be able to control expenses, generally retains the right to regulate and direct the person's business activities.

Common Law Test

- (14) Furnishing of tools and materials. If the person or persons for whom the services are performed furnished significant tools, materials, and other equipment, it is an indication an employer-employee relationship exists.
- *(15) Significant investment. If the person invests in facilities that are used by the person in performing services and are not typically maintained by employees (such as the maintenance of an office rented at fair value from an unrelated party), or if the person invests in other business expenses (such as equipment and supplies, vehicles, liability insurance, advertising, or other promotion of services), that factor tends to indicate that the person is an independent contractor. Lack of investment in expenses relative to the performance of services indicates dependence on the person or persons for whom the services are performed for such facilities and indicates the existence of an employer employee relationship.
- *(16) Realization of profit or loss. A person who may realize a profit or suffer a loss as a result of the person's services (in addition to the profit or loss ordinarily realized by employees) is generally an independent contractor, but the person who cannot is an employee. If the person is subject to a risk of economic loss due to significant investment or a bona fide liability for expenses, that indicates that the person is an independent contractor. The risk that a person will not receive payment for services, however, is common to both independent contractors and employees and thus does not constitute a sufficient economic risk to support a finding of an independent contractor.



Common Law Test

- *(17) Working for more than one firm at a time. If a person performs services under multiple contracts for unrelated persons or firms at the same time, that generally indicates that the person is an independent contractor. A person who performs services for more than one person may be an employee for each of the persons, especially when such persons are part of the same service arrangement.
- *(18) Making service available to general public. If a person makes the person's services available to the general public on a regular and consistent basis that indicates an independent contractor relationship.
- *(19) Right to dismissal. The right to dismiss a person indicates that the person is an employee and the person possessing the right is an employer. An employer exercises control through the right of dismissal, which causes the person to obey the employer's instruction. An independent contractor, on the other hand, cannot be fired without liability for breach of contract so long as the independent contractor produces a result that meets the contract specifications.
- *(20) Right to terminate. If either person has the right to end the relationship with the person for whom the services are performed at any time the person wishes without incurring liability, that indicates an employer-employee relationship. If a contract can be terminated by the mutual agreement of the parties before its completion or by one of the parties to the contract before its completion to prevent a further breach of contract or to minimize damages, that indicates an independent contractor relationship.



Economic Realities Test

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- Focus is on whether the worker is economically dependent on the business to which service is rendered, or whether as a matter of economic reality the worker is in business for himself.

Economic Realities Test (USDOL)

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- **1) The extent to which the work performed is an integral part of the employer's business.** If the work performed by a worker is integral to the employer's business, it is more likely that the worker is economically dependent on the employer and less likely that the worker is in business for himself or herself. For example, work is integral to the employer's business if it is a part of its production process or if it is a service that the employer is in business to provide.
 - **2) Whether the worker's managerial skills affect his or her opportunity for profit and loss.** Managerial skill may be indicated by the hiring and supervision of workers or by investment in equipment. Analysis of this factor should focus on whether the worker exercises managerial skills and, if so, whether those skills affect that worker's opportunity for both profit and loss.
 - **3) The relative investments in facilities and equipment by the worker and the employer.** The worker must make some investment compared to the employer's investment (and bear some risk for a loss) in order for there to be an indication that he/she is an independent contractor in business for himself or herself. A worker's investment in tools and equipment to perform the work does not necessarily indicate independent contractor status, because such tools and equipment may simply be required to perform the work for the employer. If a worker's business investment compares favorably enough to the employer's that they appear to be sharing risk of loss, this factor indicates that the worker may be an independent contractor.

Economic Realities Test (USDOL)

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- **4) The worker's skill and initiative.** Both employees and independent contractors may be skilled workers. To indicate possible independent contractor status, the worker's skills should demonstrate that he or she exercises independent business judgment. Further, the fact that a worker is in open market competition with others would suggest independent contractor status. For example, specialized skills possessed by carpenters, construction workers, and electricians are not themselves indicative of independent contractor status; rather, it is whether these workers take initiative to operate as independent businesses, as opposed to being economically dependent, that suggests independent contractor status.
 - 5) The permanency of the worker's relationship with the employer. Permanency or indefiniteness in the worker's relationship with the employer suggests that the worker is an employee, as opposed to an independent contractor. However, a worker's lack of a permanent relationship with the employer does not necessarily suggest independent contractor status because the impermanent relationship may be due to industry-specific factors, or the fact that an employer routinely uses staffing agencies.

Economic Realities Test (USDOL)

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- 6) The nature and degree of control by the employer. Analysis of this factor includes who sets pay amounts and work hours and who determines how the work is performed, as well as whether the worker is free to work for others and hire helpers. An independent contractor generally works free from control by the employer (or anyone else, including the employer's clients). This is a complex factor that warrants careful review because both employees and independent contractors can have work situations that include minimal control by the employer. However, this factor does not hold any greater weight than the other factors. For example, a worker's control of his or her own work hours is not necessarily indicative of independent contractor status; instead, the worker must control meaningful aspects of the working relationship. Further, the mere fact that a worker works from home or offsite is not indicative of independent contractor status because the employer may exercise substantial control over the working relationship even if it exercises less day-to-day control over the employee's work at the remote worksite.



- Inquiries are similar and overlap in many respects but can yield different outcomes depending on the underlying remedial purpose sought.
 - FLSA: “to suffer or permit to work.”
 - Courts: “A broader more comprehensive coverage of employees would be difficult to frame.”

Increased Focus on Proper Classification

- U.S. DOL Administrator Interpretation No. 2015-1
- <http://www.dol.gov/whd/workers/misclassification/>



Consequences of Improper Classification

- Tax & ACA Fines/Penalties
- Overtime/minimum wages(treble damages)
- Willful violations-criminal responsibility





Consequences of Improper Classification- Worker Compensation

Workers Compensation

- Workers compensation law presumes employment
- Common law test with weighted factors laid out in Administrative Code
- WSI issues a Notice of Decision which may be appealed or becomes final





- The Issue Presents Itself:
 - an application for coverage
 - an underwriting referral
 - an audit referral
 - a payroll report edit
 - a claim for benefits
 - an employer inquiry
 - a hotline tip

Consequences

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- Assuming or Asserting an Independent Contractor relationship:
 - Assessment of back premium, penalty and interest up to six years of noncompliance
 - “uninsured” status at the time of a claim
 - Assessment of actual claims costs
 - Loss of immunity
 - Inability to raise common law defenses

Consequences

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- Determination of willful noncompliance:
 - Back premium up to six years, penalties (3x the premium owed) and interest
 - Assessment of actual claims costs
 - Loss of immunity
 - Inability to raise common law defenses
 - Criminal responsibility

Address Business Needs and Structure the Relationship Accordingly

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- Do we need to retain the right to control the means and manner of performance or are we simply looking for an outcome?
 - Are there numerous ways to achieve the outcome desired, or is there a set process that must be followed?
 - What purpose is served by outlining any details of expected performance?

Example

➤ Needs Assessment Report

- Contractor shall meet twice in each of the following cities with the following groups.
- Contractor shall submit a draft agenda and survey for department approval.
- Contractor shall be paid \$25 hour, not to exceed \$1500, with per diem, mileage and hotel expenses reimbursed at State rates.



Example

➤ Needs Assessment Report

- Contractor shall use its expertise and professional judgment in designing and implementing a needs assessment for department meeting the following goals.
- Contractor shall provide department with a final report outlining the methods chosen by the contractor in securing reliable data together with specific professional recommendations.
- Contractor shall be paid a flat fee of \$2500.



