

Government Agencies to Crack Down on Misclassification of Independent Contractors

The state and federal government have initiated a crack down on employers misclassifying independent contractors. Employers are being contacted by the Illinois Department of Employment Security (“IDES”), the United States Department of Labor (“U.S. DOL”) and the Illinois Department of Labor (“IDOL”) to ascertain classification status and conduct audits. The purpose is to determine whether the classifications of certain employees as independent contractors comport with federal and state laws. While these audits are frequently triggered by disgruntled employees and/or former employees, they have also been triggered by an increase in the deficit and an increase in the IRS, Department of Labor and IDES wage and hour divisions. Recent activity indicates that employers must take rapid steps to ensure that their employees are properly classified and prevent time consuming audits and substantial fines and penalties.

On November 9, 2009, the IRS announced that it would begin conducting random audits of over 6,000 companies beginning in the spring of 2010. The IRS proclaimed that its goal is to reduce the number of misclassified independent contractors while expanding revenues. This has occurred. The IRS has randomly selected companies for the next three (3) years to examine in comprehensive scope whether or not their employment tax returns paid and the documents submitted justify the classification of independent contractor status, fringe benefits and payroll taxes. Correspondingly, on November 19, 2009, the U.S. DOL and the wage and hour division added 250 more investigators to examine employment law violations, including and specifically, the misclassification of employees as independent contractors. The advent of these pronouncements has resulted in a substantial influx in independent contractor examinations in audits in the spring of 2010.

Employers who engage independent contractors should immediately review, assess and address the relationships with the following three (3) questions in mind:

1. How and why the independent contractor relationships are established;
2. What they as employers are doing in maintaining actual independence; and
3. What documents and records are on hand that will substantially prove that the relationships are *bona fide* and will serve as major detraction.

Under the IDES and IRS rules, the agencies are really looking to determine who is an employee versus who is an independent contractor. This determination is done by examining multiple factors including whether or not the independent contractor is free from control or direction, whether or not the independent contractor conducts outside business relationships, whether or not the independent contractor is incorporated, and whether or not the independent contractor utilizes their own tools and/or materials. The question as to whether or not an individual is an independent contractor is a costly one that can result in thousands of dollars in fines if answered incorrectly. A signed contract proclaiming that an individual is an independent contractor is insufficient to establish this status. Rather, the status is determined by multiple factors. As the U.S. DOL, IDOL and IDES are turning up the heat on employers regarding independent contractors, now is an opportune time to work with Mueller & Co., LLP and your labor and employment attorney to ascertain whether or not you are properly classifying individuals as independent contractors and to make the switch to prevent the influx in litigation and time consuming audits.

If you have any questions about this issue, please contact Julie A. Proscia, Esq. Julie Proscia is a partner at SmithAmundsen LLC and a labor and employment attorney that frequently advises clients in independent contractor and classification issues. Julie may be contacted at (630) 587-7911 or at jproscia@salawus.com.

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