

Misclassification of Workers is an Increasing Problem

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Increased economic pressure, labor shortages, and a growing gig economy make it imperative for business owners and their Human Resource professionals to ensure proper separation between independent contractors and those employed by the organization. While HR may support those business functions carried out by independent contractors, it is critical to ensure HR is not "managing" them in a manner that leads courts or government agencies to conclude those contractors are improperly classified and should be considered employees.

The practice of hiring individuals as independent contractors while they perform the duties of a full-time employee is illegal, and what many companies misunderstand is that it's up to the company to define who is an employee and who is a freelancer.

Worker misclassification is a nationwide problem that has a negative impact on Pennsylvania's economy and unemployment compensation fund. It also creates an uneven playing field for employers who properly classify their workers. Misclassification occurs when employers treat certain employees as independent contractors when they should not be classified as such. This may be done to reduce payroll and other costs.

According to the Freelance Forward: 2022 report, 60 million Americans performed freelance work last year, which represents 39% of the U.S. workforce. This has attracted the attention of both the legal and tax systems. The difference in the legal obligations whether a company classifies a worker as either an employee or independent contractor is significant, particularly in terms of worker protections and tax revenue. Therefore, governments, both state and federal, have been taking a hard look at how companies are classifying their workers.

The legal and business consequences for a company that misclassified workers as independent contractors when the government or the tax authorities considers them to be employees can be costly, both in terms of financial penalties and a damaged reputation.

It is important to understand some key steps to avoid misclassification of workers. They are:

- **Conduct An Internal Audit of Your Classification Process**

The first step to ensuring that your independent contractors are classified properly is to conduct an internal audit of your current classification policies and practices. If you don't have formal policies or practices in place, this is a good time to create them. While a single common test to determine a worker's classification doesn't exist, there are some overarching themes that must be considered. In general, if you have control or direct how an independent contractor's work is completed, not just what's to be accomplished, the worker is more likely to be an employee, not a contractor.

- **Review And Revise Your Employment Agreements**

It is crucial that every contractor you hire has a properly drafted agreement, describing exactly what services the contractor is providing and laying out the parameters of their relationship with you. Well-drafted agreements are the foundation of your protection from misclassification. Your IC agreements should clearly define the scope of work, the time frame involved, their communication process with you, and the terms of payment. Additionally, the agreement should clearly state that the worker is responsible for his or her own workplace, equipment, expenses, and insurances. Finally, don't forget to include terms protecting your company's intellectual property. While this is typically a standard procedure with employment agreements, it may be overlooked with contractor agreements.

- **Implement And Enforce Classification**

The final step is to make certain the previous two steps are implemented and enforced. Your policies and agreements are worthless if they're not actually being followed. Using independent contractors can give your company an edge in today's challenging business environment, but if you're not careful, they can also be a serious liability. Consult a Labor and Employment attorney for guidance on the latest worker classification laws, how to develop and implement proper classification procedures, and for support in creating airtight agreements that protect your company.

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