A Timely Analysis of Legal Developments

ASAP®

December 2011

Colorado Latest to Join U.S. DOL to Reduce Worker Misclassification

By Joshua Kirkpatrick and Stephanie Hankin

On December 5, 2011, the Colorado Department of Labor and Employment (CDLE) and the U.S. Department of Labor's (DOL) Wage and Hour Division signed a memorandum of understanding regarding the improper classification of employees as independent contractors.

In the memorandum of understanding, among other things, the agencies agreed to:

- Conduct joint investigations periodically in the State of Colorado;
- Coordinate their respective enforcement activities and assist each other with enforcement;
- Make referrals of potential violations of each other's statutes;
- Exchange information, including statistical data on the incidence of violations in specific industries and geographic areas;
- Establish a methodology for exchanging investigative leads, complaints, and referrals of possible violations;
- Coordinate and conduct joint outreach presentations; and
- Prepare and distribute publications of common concern.

Employees vs. Independent Contractors

The distinction between whether a worker is an employee or an independent contractor is critical for a host of reasons, including, but not limited to: determining whether a business is liable for withholding and remitting federal and state income, Social Security, and Medicare taxes from the worker's pay; whether minimum wage or overtime laws apply; whether a worker is entitled to workers' compensation insurance and unemployment compensation; and whether federal and state anti-discrimination and leave laws apply.

Employment status is examined on a case-by-case basis. In general, an independent contractor retains significantly more control over the means and methods of accomplishing his or her work than employees do. The courts, the DOL, the CDLE, the Colorado Unemployment Insurance Program, and the Internal Revenue Service (IRS) use different criteria when making classification determinations, but the types of facts they consider typically fall into three general categories:

Littler
Employment & Labor Law Solutions Worldwide™

Littler Mendelson, P.C. • www.littler.com • 1.888.littler • info@littler.com

1. **Behavior control:** whether the business has a right to direct and control how the work is performed, through instructions, training, or other means;
2. **Financial control:** whether the business has a right to control the business aspects of the worker's job, such as how the business pays the worker and the extent to which the worker makes his or her services available to the relevant market; and
3. **Type of relationship:** whether there is a written contract describing the parties' relationship; whether the worker is provided with employee-type benefits; the permanency of the relationship; and how integral the services are to the business's principal activity.

Recent Focus on Misclassification

The misclassification of employees as independent contractors has emerged as a hot button issue under the Obama administration. The memorandum of understanding between the DOL and the CDLE is part of the DOL's Misclassification Initiative, which is aimed at preventing, detecting, and remedying employee misclassification. In addition to the CDLE, state government agencies in Connecticut, Hawaii, Illinois, Maryland, Massachusetts, Minnesota, Missouri, Montana, Utah, and Washington have signed similar agreements with the DOL.

In 2010, the DOL's Wage and Hour Division collected nearly $4 million in back wages for minimum wage and overtime violations that resulted from employees being misclassified as independent contractors or otherwise not being treated as employees. This represented an increase of almost 400% from 2008, when the division collected just over $1.3 million for the same reasons.

Recently, Rep. Lynn Woolsey (D-CA) reintroduced legislation in the U.S. House of Representatives that would create new record-keeping requirements for employers that hire independent contractors and impose stricter penalties for misclassification. Among other things, the Employee Misclassification Prevention Act would amend the Fair Labor Standards Act (FLSA) and will require employers to keep records on and notify workers of their employment or independent contractor classification and their right to challenge that classification.

In June 2009, H.B. 1310 (Colo. Rev. Stat. §§ 8-72-114 *et seq.*) went into effect in Colorado, which requires the CDLE to accept and investigate complaints of employee misclassification, collect unpaid unemployment insurance premiums, and impose additional fines for willful misclassifications. The statute authorizes fines of up to $5,000 per misclassified employee for first-time willful violations, which can jump to $25,000 per misclassified employee for repeat violations, although, as of June 2011, no fines have yet been levied. Ellen Golombek, Executive Director of the CDLE, recently indicated that the state plans to increase penalties for misclassification in 2012.

The CDLE estimates that from June 2009 – when H.B. 1310 went into effect – to December 2010, 14.2% of workers in Colorado were misclassified. According to the CDLE, the estimated financial impact to the State due to worker misclassification is $167 million in lost income tax revenue annually and, from June 2009 to December 2010, $744,359 in underpaid unemployment premiums and interest. As such, it is no surprise that the State is increasing enforcement to try to capture this perceived loss in revenue.

Impact on Employers

In light of the recent agreement between the DOL and the CDLE, investigations into worker misclassification in Colorado will likely increase in the future. Moreover, employers who are investigated for worker misclassification will likely be investigated by both the DOL and the CDLE at the same time. Perhaps of greatest concern to employers, the memorandum of understanding provides for robust information sharing between the agencies, typically without the protections of the federal Freedom of Information Act (FOIA), because exchanges of information pursuant to the agreement are not considered "public disclosures" for purposes of having to comply with FOIA.

To avoid costly and time-consuming investigations by the DOL and the CDLE, employers who do business in Colorado (or any of the other states that have signed similar agreements) should closely examine whether they have properly classified workers as independent contractors and should contact outside counsel if they have any questions about classification.

Josh Kirkpatrick is a Shareholder, and Stephanie Hankin is an Associate, in Littler Mendelson's Denver office. If you would like further information, please contact your Littler attorney at 1.888.Littler or info@littler.com, Mr. Kirkpatrick at jkirkpatrick@littler.com, or Ms. Hankin at shankin@littler.com.