Best Practices Tip 2012

Tricky Claim Issues
Part 2

In the last tip we talked about two of the three types of unemployment claims that can be a little tricky to understand. They were “seasonal employment” and “still employed.” In this tip we’re going to take a look at the third tricky claim type, “independent contractor vs. employee,” and why as an employer it’s so important to be well informed when dealing with this claim type.

Independent Contractor vs. Employee

The issue of how to classify a worker as an employee of a company or an independent contractor can often be confusing. A good way to differentiate the two is that an employer must generally

- withhold income taxes
- withhold and pay Social Security and Medicare taxes
- and pay unemployment tax (if applicable) on wages paid to an employee

However, an employer does not generally have to do the above for independent contractors because they are self employed. Generally the following definitions are applied:

- Employee= anyone who performs services and the company can control what is done.
- Independent Contractor= anyone who performs services and the company only has the right to control the result of the work and not the means and methods of accomplishing the result.

Each state ultimately classifies each worker as an employee or independent contractor as they deem appropriate, using either the ABC or Common Law Test.

Currently, 33 states use the ABC Test while 18 use the Common Law.

The ABC Test

Considers 3 factors to determine the relationship of the worker to the employer:

- The worker is free from direction and control
- The worker performs services outside the company’s usual course of business
- The worker is independently established in his/her own business.
The Common Law Test

Considers 20 factors to determine and define the employer-worker relationship, but its main focus for classification is the company’s right to control, as with the ABC test:

- Instructions
- Training
- Integration
- Services Rendered Personally
- Hiring, Supervising, and Paying Assistants
- Continuing Relationship
- Set Hours of Work
- Full Time Required
- Doing Work on Company Premises
- Order or Sequence Set
- Oral or Written Reports
- Payment by Hour, Week, or Month
- Payment of Business and/or Travel Expenses
- Furnishing Tools and Materials
- Significant Investment
- Realization of Profit or Loss
- Working For More than 1 Company at a Time
- Making Services Available to the General Public
- Right To Discharge
- Right to Terminate

So why is understanding this type of tricky claim so important for employers?

- **Rework**: misclassifying workers can result in significant rework for both the employer and the state.

- **Overpayments**: Each year, 9-10% of benefits paid result in an overpayment, which equals to millions of dollars a year.

- **Investigations**: If an employer reports that someone is an independent contractor, the state is going to delve deeper into it and could even initiate a full-blown investigation.

- **Penalties**: Through investigations, states may find an employer liable for delinquent unemployment taxes, as well as possible penalties. Unfortunately, the process does not usually end with just one. An investigation and penalties for one misclassified worker may result in additional investigations and penalties for other workers.