



April 2010

**1099'd:
Misclassification of Employees as "Independent Contractors"**

Employers of low-income workers frequently misclassify their employees as "independent contractors" (either by giving them an IRS Form 1099 instead of a W-2, or by paying them in cash and not withholding any taxes). And who can blame them? The result is that the worker gets *no coverage* of most labor and employment laws. This decreases employers' payroll costs by 15 to 30%. It also lets employers off the hook for rules protecting "employees," including the responsibility to pay minimum wage and overtime, provide workers' compensation, and to bargain with unions.

Independent contractor misclassification has been common in some sectors historically, including in agriculture and day labor jobs. Its use is on the rise, however, and can now be seen in nearly every segment of today's economy, in particular in the low-wage immigrant-dominated sectors of home health care, construction, delivery services, and janitorial.

Misclassification is Not Just Bad for Workers

Because of their status as non-employees, misclassified "independent contractors" miss out on: minimum wage and overtime requirements, workers' compensation, unemployment insurance, the right to form a union and bargain collectively, and other workplace protections like the right to safe and healthy worksites and to be free from discrimination in employment. Independent contractors have to pay more taxes, too: they are responsible for paying the employer- and employee-side FICA and FUTA taxes, or 15 % of their gross wages, while employees pay only 7.65%, for instance.

States lose out, too, because they don't receive the payroll and related taxes employers contribute on behalf of employees, and workers' compensation premiums are lost. The U.S. Government Accountability Office projections estimated that misclassification of employees as independent contractors would reduce federal tax revenues by up to \$4.7 billion by 2004.¹ A government-sponsored national unemployment audit found \$436

¹ U.S. General Accounting Office, Pub.No. GAO\GGD-89-107, *Tax Administration Information: Returns Can Be Used to Identify Employers Who Misclassify Employees* (1989).

million in underreported wages.² A recent Massachusetts study found unpaid workers' compensation premiums of \$91 million a year due to independent contractor misclassification; \$7 million of those unpaid premiums were in construction.³

Finally, law-abiding businesses that do not misclassify their employees as independent contractors lose out, because they have to compete with those that misclassify and cut their labor costs. This lowers wages and benefits for all workers as firms race to the bottom to underbid each other in today's competitive economies.

What Can Be Done?

Just because employers say a worker is an independent contractor does not make it legally true!

An employer's label attached to a worker (independent contractor, freelancer, etc.) does not mean that the worker is not an employee, and workers can pursue labor and employment rights even when they have been treated as an independent contractor.

Worker organizing groups have developed a variety of innovative strategies to combat employee independent contractor abuses. Some of the more successful are:

- **Organize a coalition** of labor, immigrant, business, government and other community groups to publicize the problem and come up with creative solutions, as did Nebraska Appleseed and its allies to combat 1099 abuses in the construction industry.
- If you notice many worker rights being violated or benefits being denied, don't give up! Workers can **file claims with administrative agencies**: go to the workers' compensation board, the unemployment insurance office, the state or federal department of labor, or the NLRB and file a claim on behalf of a worker, stating that the worker is a covered employee. Force the employer to prove that the worker is an independent contractor and not protected.

Practice tip: remember different laws have different definitions of who's an employee, so get your facts straight beforehand. See, [NELP's Employment Relationships Checklist](#).

² Planmatics, Inc., *Independent Contractors: Prevalence and Implications for Unemployment Insurance Programs* (February 2000).

³ Bernard and Herrick, "The Social and Economic Costs of Employee Misclassification in Construction," A report of the Construction Policy Research Center at Harvard Law School and Harvard School of Public Health (December 2004), at p. 2.

Practice tip: make sure you are aware of immigration status issues. For example, undocumented workers cannot collect unemployment insurance. Immigration status should not impact most other laws. Stand firm against agency pressure to answer immigration status questions.

- **Fill out an [IRS Form SS-8](#)**, which requires the IRS to investigate whether a worker is an employee or independent contractor for federal tax purposes.

Practice tip: keep in mind that the IRS will notify the employer of receipt of an SS-8 Form, in order to do its investigation. Workers concerned about employer retaliation should weigh the risks.

- **Organize to pass legislation to study or correct the problem** of employer misclassification. For example,

Washington, [HB3122\(2008\)](#): creates a presumption of employee status for coverage under the state's workers' compensation and unemployment insurance statutes.

Minnesota, § [181.723](#): creates the presumption of an employee-employer relationship in the construction industry, unless an individual is granted an "exemption certificate" issued by the state, certifying that the individual meets all the criteria of the 9-part test for an independent contractor.

A few states have created **inter-agency task forces** to increase enforcement against misclassification. See, CA [Unempl. Ins. Code § 329](#); New Hampshire, [SB500](#); Connecticut, [PA 08-156](#); Utah, [SB 189](#).

For periodic listing of reforms, see NELP's [Summary of Independent Contractor Reforms](#).

- **Go to your state Attorney General** and ask that it enforce state laws against misclassification, including tax, workers' comp, prevailing wage and other workplace laws. Groups in NY, NC, IL, and MA have found this strategy successful recently.

