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DOL Coordinates With IRS, States On Independent Contractor Misclassification

By [Bill Pokorny](#) on September 22, 2011

AUDIT

Earlier this week, the U.S. Department of Labor [held a ceremony](#) at which Secretary of Labor Hilda Solis signed a memorandum of understanding with the Internal Revenue Service to "improve departmental efforts to end the business practice of misclassifying employees in order to avoid providing employment protections." The DOL also signed or has agreed to sign memorandums of understanding with officials in 11 states to coordinate efforts to crack down on independent contractor misclassification, including Connecticut, Hawaii, Illinois, Maryland, Massachusetts, Minnesota, Missouri, Montana, New York, Utah, and Washington.

Although misclassifying workers as independent contractors can result in violations of numerous laws, including the tax code and wage and hour laws, the various government agencies charged with enforcing those laws have historically not shared information or coordinated their enforcement efforts. That now now appears to be coming to an end, as the DOL becomes more aggressive in its enforcement efforts and state and federal governments look for opportunities to enhance their revenues.

At the same time, the IRS has [announced](#) a new "Voluntary Classification Settlement Program" to encourage employers who have misclassified workers in the past to "get into compliance by making a minimal payment covering past payroll tax obligations rather than waiting for an IRS audit." To be eligible for this program, applicant employers must (1) consistently have treated the workers as nonemployees, (2) have filed all required 1099s for the workers for the prior three years, and (3) not currently be under audit by the IRS, DOL, or a state agency concerning the classification of the affected workers. Employers accepted into the program will be required to pay an amount "effectively equaling just over one percent of the wages paid to the reclassified workers for the past year." No penalties or interest will be assessed, but for the first three years under the program, the employers must agree to an extended statute of limitations for the IRS to pursue payroll tax violations. Unfortunately for employers, the IRS program would not provide any amnesty for violations of other laws, such as state or federal overtime laws or state tax violations. The IRS announcement also makes no mention of whether the agency will share information from the settlement program with the Department of Labor or other agencies.

Because misclassification violations implicate a wide range of laws and frequently involve multiple workers, they can represent a significant liability for employers, particularly for small and midsize businesses without significant financial reserves to defend or settle these claims. Given the risks and

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the spotlight that the DOL is shining on this issue, businesses that use independent contractors should act now to ensure that their workers are properly classified. Among other things, this means making sure that when you classify a worker as an "independent contractor," you are prepared to prove that your classification decision is warranted under all of the relevant laws, including but not limited to the Fair Labor Standards Act, state wage and hour laws, workers' compensation statutes, and the state and federal tax codes. Unless you are well-versed in these laws, this is yet another area where a few hours of consultation with an experienced employment lawyer now may help avoid serious liability down the road.

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