

New Law Redefines “Independent Contractor”

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A new law becomes effective in Illinois on January 1, 2008, which significantly narrows the definition of “independent contractors” and imposes serious penalties on employers who do not comply with the new law. The Illinois Employee Classification Act of 2007 (“the Act”) was signed into effect on August 6, 2007, but will not be enforced until after the first of the year. The Act applies to the construction industry, including public and private construction, residential and commercial building, street, bridge, sewer, water works, railroad and excavation work, as well as maintenance, repair, landscape, decorating work and the moving of construction related materials on the job site to or from the job site.

Tests for Independent Contractor Status:

The Act creates a presumption that any individual performing any service for a construction contractor is an employee, *unless* one of two different several-factor tests is satisfied.

The first test includes three criteria and is being referred to as the “ABC test.” It provides that an individual performing services for a contractor is deemed to be an employee of the contractor unless 1) the individual is free from control or direction over the performance of the service for the contractor; 2) the service performed by the individual is outside the usual course of services performed by the contractor; AND 3) the individual is engaged in an independently established trade, occupation, profession or business.

Alternatively, there is a second test under the Act which provides a list of twelve criteria that must be met in order to show that the individual performing services for a contractor is an independent contractor by virtue of being a legitimate sole proprietor or partnership. To be deemed a legitimate sole proprietor or partnership under this test, the individual performing services for the contractor must 1) be free from direction and control over the means and manner of providing the service; 2) continue beyond severance of the relationship with the contractor; 3) have a substantial investment of capital in the sole proprietorship or partnership beyond ordinary tools and equipment and a personal vehicle; 4) own the capital goods and experience the gains and losses; 5) make its services available to the general public or the business community on a continuing basis; 6) include services rendered on a Federal Income Tax Schedule as an independent business or profession; 7) perform services under its own name; 8) obtain any required licenses or permits in its own name; 9) furnish the tools and equipment necessary to provide the service; 10) if necessary, hire its own employees without contractor approval, pay the employees without reimbursement from the contractor and report the income to the IRS; 11) not be represented by the contractor as its employee; AND 12) have the right to perform similar services for others on whatever basis and whenever it chooses.

Penalties for Violations:

The Act includes a surprisingly severe penalties section which creates the ability for “any interested party” to file a complaint with the Department of Labor if they suspect that an employer has violated the Act. Individuals are incentivized to file a complaint because the Act provides that 10% of the amount recovered for violations shall be awarded to the complaining party. Such a complaint then authorizes the Department to conduct an investigation and inspect documents related to the determination of an individual’s status as either an independent contractor. If violations are discovered, the Department may assess *finest of up to \$1,500 for each individual and for each day, or up to \$2,500 for each repeat violation within a 5 year period*. If violations are found to be willful, the penalties may be doubled and the employer will be liable to the employee for punitive damages in an amount equal to the penalties. Two violations within a 5 year period will prevent the employer from being awarded any state contracts. Additionally, the Act creates a private right of action under which an interested party may file suit in circuit court to recover damages including any lost wages and benefits plus an equal amount in liquidated damages, up to \$500 for each violation, and attorneys fees and costs. Finally, the Act provides that it is a Class C misdemeanor for an employer to attempt to induce any individual to waive any provision of the Act.

Recommendations:

Although no one knows for sure what the impact of the Act will be, there is plenty of reason to be concerned. One major question is whether incorporated independent contractors or LLCs are exempt from the Act? The answer is unclear because the 12-part test refers only to partnerships and sole proprietorships, but there is no mention in the Act of other business entities, such as corporations. One logical explanation suggests that the reason other entities are not mentioned in the Act is that the legislators intended them to be exempt from either test and from the requirements of the Act. However, until regulations or further guidance from the courts or the Department of Labor come out, we do not advise that employers assume that incorporated independent contractors or LLCs are immune from being classified as employees.

One way that employers may be able to protect themselves is with carefully drafted independent contractor agreements which mirror each provision of the 12-part test. While an agreement is not a guarantee of compliance, employers with detailed agreements and a course of conduct that follows the agreement will be in a much better position than employers who do not. The attorneys here at Golan & Christie are available to answer questions or assist in drafting such documents. In our consultation we can work together to determine how to best conform each independent contractor relationship to the new requirements. Additionally, Section 15 of the Act requires employers to post summaries of this Act at all job sites where there are individuals who may be included in its scope, but it also states that the Department of Labor will create and provide the summaries on its website, which, thusfar, it has failed to do. We are in contact with the Department of Labor and will be happy to assist employers in obtaining the appropriate posters.

Please feel free to contact me or any of the attorneys at Golan & Christie LLP if you have any questions or concerns related to the Act.